

4-1990

Judicial "Pruning" of "Garden Variety Fraud" Civil RICO Cases Does Not Work: It's Time for Congress to Act

Susan Getzendanner

Follow this and additional works at: <https://scholarship.law.vanderbilt.edu/vlr>



Part of the [Courts Commons](#), and the [Criminal Procedure Commons](#)

Recommended Citation

Susan Getzendanner, Judicial "Pruning" of "Garden Variety Fraud" Civil RICO Cases Does Not Work: It's Time for Congress to Act, 43 *Vanderbilt Law Review* 673 (1990)
Available at: <https://scholarship.law.vanderbilt.edu/vlr/vol43/iss3/5>

This Symposium is brought to you for free and open access by Scholarship@Vanderbilt Law. It has been accepted for inclusion in Vanderbilt Law Review by an authorized editor of Scholarship@Vanderbilt Law. For more information, please contact mark.j.williams@vanderbilt.edu.

Judicial “Pruning” of “Garden Variety Fraud” Civil RICO Cases Does Not Work: It’s Time for Congress to Act

*Susan Getzendanner**

I. INTRODUCTION	673
II. CIVIL RICO: THE STATUTORY UNDERLAYMENT	675
III. THE USE OF CIVIL RICO	677
IV. REFORM OF THE CIVIL RICO PREDICATE OFFENSES	678
A. “Garden Variety Fraud”	679
B. Multiple Victims	681
C. Securities Fraud	683
D. Civil RICO Cases Based on Other Predicate Offenses	684
V. OTHER PROPOSED REFORMS	685
A. Redacting “Racketeering”	685
B. Automatic Treble Damages	685
C. Double Punitive Damages	687
D. Statute of Limitations	688
E. Universal Service of Process	688
F. Affirmative Defense	689
VI. CONCLUSION	689

I. INTRODUCTION

After many years of effort, Congress actually may amend substantively the civil provisions of the Racketeer Influenced and Corrupt Organizations Act¹—“RICO”—this year.² So I am delighted to accept the timely invitation of the *Vanderbilt Law Review* to add my view of how

* The Author is a partner at Skadden, Arps, Slate, Meagher & Flom in the Chicago office, a former United States District Court Judge in Chicago 1980-87, and a self-declared member of the RICO bar. Ms. Getzendanner gratefully acknowledges the contribution of Montgomery K. Fisher, an associate in Skadden’s Washington, D.C. office.

1. Organized Crime Control Act of 1970, Pub. L. No. 91-452, tit. IX, 84 Stat. 941, 947-48 (1971) (codified at 18 U.S.C. §§ 1961-1968 (1988)).

2. See, e.g., *Amending RICO*, NAT’L J., Oct. 7, 1989, at 2489.

the law should be revised.

My RICO perspective comes from my years as a federal district court judge in Chicago from 1980 to 1987, when I witnessed the real birth and growth of civil RICO.³ I am told by my co-panelist, Professor G. Robert Blakey, that for a time I had written more RICO opinions than any other judge in the country. (This had nothing to do with my decision to leave the bench.) As I dealt with these cases, it became clear to me that most civil RICO cases simply should not be in federal court. The majority of civil RICO cases involve commonplace commercial controversies, the facts of which reveal an ordinary business relationship gone sour. These mercantile melees are recharacterized by resourceful attorneys to conform with the requirements of RICO: adding a few allegations of the use of the mails or wires in furtherance of a fraudulent scheme, describing how the mail or wire fraud offenses form a pattern, and explaining how the defendants conducted the affairs of an appropriate enterprise. Thus transmogrified, the ordinary state law fraud or contract action becomes a federal "racketeering" case, threatening treble damages, costs, and attorney's fees. Not only is this transformation unfair to the typical commercial defendant, but it also burdens the dockets of the federal courts and multiplies the legal costs for both sides in otherwise straightforward litigation.

Civil RICO is not intrinsically evil, however. It was designed to enable private plaintiffs to bring civil actions against persons engaged in a pattern of criminal activity. This intention is admirable, and RICO has succeeded in facilitating such civil actions. No one has claimed that the civil provision of the statute has failed to achieve its goal. The complaint is that civil RICO has succeeded too well.

RICO has become a well-established feature of the legal landscape. There is a RICO bar, of which I am a member, that brings and defends civil RICO actions for large corporate clients. The RICO bar is well entrenched, and it will be difficult to dislodge. Moreover, the traditional plaintiffs' bar and the "consumers' lobbies"⁴ also enthusiastically support RICO.

Recognizing the futility of any effort to eliminate or substantially to narrow civil RICO, I offer a straightforward solution: eliminate mail

3. Although RICO was enacted in 1970, the civil provisions were not used extensively until the early 1980s. As reported by a RICO task force of the American Bar Association, of approximately 270 trial court decisions between 1970 and 1985, 3% were decided before 1980, 2% in 1980, 7% in 1981, 13% in 1982, 33% in 1983, and 43% in 1984. See A.B.A. SECTION OF CORP., BANKING & BUS. LAW, REPORT OF THE AD HOC CIVIL RICO TASK FORCE 55 (1985) [hereinafter ABA RICO REPORT].

4. See Corrigan, *Rolling Back RICO*, NAT'L J., Sept. 6, 1986, at 2114, 2116 (stating that RICO gives "consumers protection against corporate swindles").

and wire fraud as RICO predicate offenses for civil actions, except in class actions in which one hundred or more plaintiffs participate. This simple change will reduce substantially the number of civil RICO cases and eliminate the "garden variety" fraud and contract disputes that now find their way into federal court as RICO actions. I also would join others in excluding securities fraud as a predicate offense for civil RICO. If the changes I propose are enacted, the piecemeal changes often urged in the name of RICO reform would become unnecessary.

II. CIVIL RICO: THE STATUTORY UNDERLAYMENT

RICO is chapter 96, sections 1961 to 1968, of title 18 of the United States Code. Section 1964(c)⁵ of the RICO statute provides a private civil action to recover treble damages, plus costs and attorney's fees, for injury caused by a violation of section 1962, which prohibits engaging in or investing the profits from "a pattern of racketeering activity or through collection of an unlawful debt."⁶ "Racketeering activity" is defined in section 1961(1) as any act "chargeable" under several generically described state criminal laws; any act "indictable" under

5. Section 1964(c) states: "Any person injured in his business or property by reason of a violation of section 1962 of this chapter may sue therefor in any appropriate United States district court and shall recover threefold the damages he sustains and the cost of the suit, including a reasonable attorney's fee." 18 U.S.C. § 1964(c) (1988).

6. *Id.* § 1962(a). Section 1962 states:

(a) It shall be unlawful for any person who has received any income derived, directly or indirectly, from a pattern of racketeering activity or through collection of an unlawful debt in which such person has participated as a principal within the meaning of section 2, title 18, United States Code, to use or invest, directly or indirectly, any part of such income, or the proceeds of such income, in acquisition of any interest in, or the establishment or operation of, any enterprise which is engaged in, or the activities of which affect, interstate or foreign commerce. A purchase of securities on the open market for purposes of investment, and without the intention of controlling or participating in the control of the issuer, or of assisting another to do so, shall not be unlawful under this subsection if the securities of the issuer held by the purchaser, the members of his immediate family, and his or their accomplices in any pattern or racketeering activity or the collection of an unlawful debt after such purchase do not amount in the aggregate to one percent of the outstanding securities of any one class, and do not confer, either in law or in fact, the power to elect one or more directors of the issuer.

(b) It shall be unlawful for any person through a pattern of racketeering activity or through collection of an unlawful debt to acquire or maintain, directly or indirectly, any interest in or control of any enterprise which is engaged in, or the activities of which affect, interstate or foreign commerce.

(c) It shall be unlawful for any person employed by or associated with any enterprise engaged in, or the activities of which affect, interstate or foreign commerce, to conduct or participate, directly or indirectly, in the conduct of such enterprise's affairs through a pattern of racketeering activity or collection of unlawful debt.

(d) It shall be unlawful for any person to conspire to violate any of the provisions of subsection (a), (b), or (c) of this section.

Id.

numerous specific federal criminal offenses—including mail and wire fraud—and any “offense” involving bankruptcy or securities fraud or drug-related activities that is “punishable” under federal law.⁷

A RICO “pattern” is defined in section 1961(5), which says simply that a pattern “requires at least two acts of racketeering activity, one of which occurred after [October 15, 1970] and the last of which occurred within ten years (excluding any period of imprisonment) after the commission of a prior act of racketeering activity.”⁸ The Supreme Court recently clarified the pattern requirement: “[T]o prove a pattern of racketeering activity a plaintiff or prosecutor must show that the racketeering predicates are related, *and* that they amount to or pose a threat of continued criminal activity.”⁹ The Court added, “What a plaintiff or

7. RICO defines “racketeering activity”:

(A) any act or threat involving murder, kidnaping, gambling, arson, robbery, bribery, extortion, dealing in obscene matter, or dealing in narcotic or other dangerous drugs, which is chargeable under State law and punishable by imprisonment for more than one year; (B) any act which is indictable under any of the following provisions of title 18, United State Code: Section 201 (relating to bribery), section 224 (relating to sports bribery), sections 471, 472, and 473 (relating to counterfeiting), section 659 (relating to theft from interstate shipment) if the act indictable under section 659 is felonious, section 664 (relating to embezzlement from pension and welfare funds), sections 891-894 (relating to extortionate credit transactions), section 1029 (relating to fraud and related activity in connection with access devices), section 1084 (relating to the transmission of gambling information), section 1341 (relating to mail fraud), section 1343 (relating to wire fraud), sections 1461-1465 (relating to obscene matter), section 1503 (relating to obstruction of justice), section 1510 (relating to obstruction of criminal investigations), section 1511 (relating to the obstruction of State or local law enforcement), section 1512 (relating to tampering with a witness, victim, or an informant), section 1513 (relating to retaliating against a witness, victim, or an informant), section 1951 (relating to interference with commerce, robbery, or extortion), section 1952 (relating to racketeering), section 1953 (relating to interstate transportation of wagering paraphernalia), section 1954 (relating to unlawful welfare fund payments), section 1955 (relating to the prohibition of illegal gambling businesses), section 1956 (relating to the laundering of monetary instruments), section 1957 (relating to engaging in monetary transactions in property derived from specified unlawful activity), sections 2251-2252 (relating to sexual exploitation of children), section 1958 (relating to use of interstate commerce facilities in the commission of murder-for-hire), sections 2251-2252 (relating to sexual exploitation of children),, [sic] sections 2312 and 2313 (relating to interstate transportation of stolen motor vehicles), sections 2314 and 2315 (relating to interstate transportation of stolen property), section 2321 (relating to trafficking in certain motor vehicles or motor vehicle parts), sections 2341-2346 (relating to trafficking in contraband cigarettes), sections 2421-24 (relating to white slave traffic), (C) any act which is indictable under title 29, United State Code, section 186 (dealing with restrictions on payments and loans to labor organizations) or section 501(c) (relating to embezzlement from union funds), (D) any offense involving fraud connected with a case under title 11, fraud in the sale of securities, or the felonious manufacture, importation, receiving, concealment, buying, selling, or otherwise dealing in narcotic or other dangerous drugs, punishable under any law of the United States, or (E) any act with is indictable under the Currency and Foreign Transactions Reporting Act.

Id. § 1961(1).

8. *Id.* § 1961(5).

9. *H.J. Inc. v. Northwestern Bell Tel. Co.*, 109 S. Ct. 2893, 2900 (1989) (citations omitted). The Court then adopted, for the “relationship” part of its RICO “pattern” definition, the “pat-

prosecutor must prove is continuity of racketeering activity, or its threat, *simpliciter*. This may be done in a variety of ways, thus making it difficult to formulate in the abstract any general test for continuity."¹⁰

Justice Scalia predicted that the lower courts likely would find the Court's "continuity plus relationship" description of a pattern "about as helpful to the conduct of their affairs as 'life is a fountain.'"¹¹ I am not so pessimistic. In the Seventh Circuit, the court early adopted the view that, like obscenity, you will know a pattern when you see one.¹² After analyzing patterns in a number of cases,¹³ I found identifying patterns a relatively easy, low-risk task.

III. THE USE OF CIVIL RICO

Everyone who has examined the legislative history of RICO, with the exception of Professor G. Robert Blakey, has pointed out that Congress added the private civil treble damages remedy to RICO with vir-

tern" definition found in 18 U.S.C. § 3575(e) (1988): "[C]riminal conduct forms a pattern if it embraces criminal acts that have the same or similar purposes, results, participants, victims, or methods of commission, or otherwise are interrelated by distinguishing characteristics and are not isolated events." *H.J. Inc.*, 109 S. Ct. at 2901.

10. *H.J. Inc.*, 109 S. Ct. at 2901. "Continuity" is both a closed- and open-ended concept, referring either to a closed period of repeated conduct, or to past conduct that by its nature projects into the future with a threat of repetition. It is, in either case, centrally a temporal concept—and particularly so in the RICO context, where *what* must be continuous, RICO's predicate acts or offenses, and the *relationship* these predicates must bear one to another, are distinct requirements. *Id.* at 2902.

11. *Id.* at 2907 (Scalia, J., concurring).

12. See *Morgan v. Bank of Waukegan*, 804 F.2d 970, 977 (7th Cir. 1986). Despite the angst of some commentators and members of the judiciary, as exemplified by Justice Antonin Scalia's concurrence in *H.J. Inc.*, none of the proposed bills to reform RICO attempts to redefine "pattern."

13. See *United States v. Roth*, No. 85-CR-763 (N.D. Ill. Aug. 17, 1987) (LEXIS, Genfed library, Dist file); *United States v. Roth*, No. 85-CR-763 (N.D. Ill. June 15, 1987) (LEXIS, Genfed library, Dist file); *Radionic Indus., Inc. v. GTE Prods. Corp.*, 665 F. Supp. 622 (N.D. Ill. 1987); *Levit v. Brodner*, No. 85-C-7196 (N.D. Ill. Feb. 25, 1987) (LEXIS, Genfed library, Dist file); *Heritage Ins. Co. of Am. v. First Nat'l Bank*, No. 84-C-8747 (N.D. Ill. Jan. 22, 1987) (LEXIS, Genfed library, Dist file); *Armetta v. Hess*, No. 85-C-4688 (N.D. Ill. Jan. 16, 1987) (LEXIS, Genfed library, Dist file); *Bachmeier v. Bank of Ravenswood*, 663 F. Supp. 1207 (N.D. Ill. 1987); *Techreations, Inc. v. National Safety Council*, 650 F. Supp. 337 (N.D. Ill. 1986); *Edward George Co. v. Buck Stoves N.W., Inc.*, No. 85-C-10548 (N.D. Ill. May 8, 1986) (LEXIS, Genfed library, Dist file); *Gault v. Foster*, No. 83-C-1688 (N.D. Ill. Mar. 25, 1986) (LEXIS, Genfed library, Dist file); *Medical Emergency Serv. Assoc. v. Foulke*, 633 F. Supp. 156 (N.D. Ill. 1986); *Fagenbolz v. A.M.F. Inc.*, No. 85-C-3456 (N.D. Ill. Dec. 5, 1985) (LEXIS, Genfed library, Dist file); *Fye v. First Nat'l Bank*, No. 85-C-0700 (N.D. Ill. Dec. 3, 1985) (LEXIS, Genfed library, Dist file); *Graham v. Slaughter*, 624 F. Supp. 222 (N.D. Ill. 1985); *In re Olympia Brewing Co. Sec. Litig.*, 612 F. Supp. 1370 (N.D. Ill. 1985); *United States v. Novack*, No. 85-CR-26 (N.D. Ill. Apr. 24, 1985) (LEXIS, Genfed library, Dist file); *D & S Auto Parts, Inc. v. Schwartz*, No. 82-C-5279 (N.D. Ill. July 6, 1984) (LEXIS, Genfed library, Dist file); *Kosch v. Parkway Bank & Trust Co.*, No. 83-C-4832 (N.D. Ill. Mar. 9, 1984) (LEXIS, Genfed library, Dist file); *States Sec. Ins. Co. v. Mercantile Bond Agency, Inc.*, No. 83-C-285 (N.D. Ill. Sept. 2, 1983) (LEXIS, Genfed library, Dist file).

tually no consideration of its purpose or consequences.¹⁴ After its enactment, civil RICO percolated for several years before coming to life, not as a complement to the criminal actions pursued by prosecutors against nefarious evildoers, but as "a tool for everyday fraud cases brought against 'respected and legitimate 'enterprises.''"¹⁵ In *Sedima, S.P.R.L. v. Imrex Co., Inc.*¹⁶ the Second Circuit attempted to limit the reach of civil RICO by requiring the plaintiff to allege that the defendant had been convicted of either a RICO violation or the predicate acts upon which the RICO claim was based, and that the injury was caused by an activity which RICO was designed to deter.¹⁷

The Supreme Court reversed, noting that "RICO is to be read broadly"¹⁸ as "an aggressive initiative to supplement old remedies and develop new methods for fighting crime."¹⁹ The Court steadfastly refused to place any limits on the use of civil RICO against those perceived to be "respected and legitimate 'enterprises.'"²⁰ The Court acknowledged that "private civil actions under the statute are being brought almost solely against such defendants, rather than against the archetypal, intimidating mobster." The Court, however, declined to remedy the statute. "Yet this defect—if defect it is—is inherent in the statute as written, and its correction must lie with Congress."²¹ Defect it is, and appropriate Congressional correction is clearly necessary.

IV. REFORM OF THE CIVIL RICO PREDICATE OFFENSES

Civil RICO cases can be divided into two broad categories: fraud and all others. The vast majority of civil RICO cases use mail, wire, or securities fraud as the predicate offense.²² In the past two years I have

14. See, e.g., *Sedima, S.P.R.L. v. Imrex Co.*, 473 U.S. 479, 486-88 (1985); *County of Suffolk v. Long Island Lighting Co.*, 710 F. Supp. 1387, 1394 (E.D.N.Y. 1989) (stating that "[w]ith almost no legislative debate or comment, [RICO] was extended as an afterthought to civil cases to encourage private suits as a supplement to the efforts of federal law enforcement agencies"); ABA RICO REPORT, *supra* note 3, at 112-20.

15. *Sedima*, 473 U.S. at 499 (quoting *Sedima, S.P.R.L. v. Imrex Co.*, 741 F.2d 482, 487 (2d Cir. 1984)).

16. 741 F.2d 482 (2d Cir. 1984).

17. *Id.* at 495-502.

18. *Sedima*, 473 U.S. at 497.

19. *Id.* at 498.

20. *Id.* at 499. The Court stated:

Yet Congress wanted to reach both "legitimate" and "illegitimate" enterprises. The former enjoy neither an inherent incapacity for criminal activity nor immunity from its consequences. The fact that § 1964(c) is used against respected businesses allegedly engaged in a pattern of specifically identified criminal conduct is hardly a sufficient reason for assuming that the provision is being misconstrued.

Id.

21. *Id.* at 499.

22. See ABA RICO REPORT, *supra* note 3, at 57.

drafted eight civil RICO complaints. Each involved a single commercial transaction (frequently a deal that “went south”), corporate parties, and a great deal of money. The predicate acts were always mail or wire fraud. The pattern was the most difficult RICO pleading requirement, but I met that requirement in most of these draft complaints. Under my proposed amendment of civil RICO, not one of these complaints could have been drafted.

A. “Garden Variety Fraud”

Virtually every published case of which I am aware, in which the RICO claims were predicated exclusively on mail or wire fraud, concerns a commercial dispute to which the attorney has added unremarkable fraud allegations. Some recent examples include the following:

- A foreign participant in a joint venture sued its domestic partner when it became convinced that its partner was overstating its expenses and thereby collecting more than its fair share of the venture’s profits.²³

- Several businesses brought an action against a bank for charging a higher rate of interest than stated in the loan agreements.²⁴

- An insurance purchaser sued the insurance agent when the agent’s insurance company became insolvent and failed to pay its claims.²⁵

- Oil suppliers brought an action against a purchaser after supplying oil to the purchaser far in excess of the purchaser’s credit limit.²⁶

- Investors in a tax shelter scheme who subsequently suffered both actual losses and loss of expected tax benefits sued the orchestrators of the scheme.²⁷

- A savings and loan sued its former president-chief executive officer, who, it alleged, “solicited and received kickbacks from [Sun’s] customers for whom he approved large loans.”²⁸

- State tax collectors sued to recover treble damages—that is, trebled taxes—for the filing of inaccurate state tax returns.²⁹

- A seller sued a buyer who had an agreement to purchase all of the seller’s stock but terminated the agreement after completing due

23. *Sedima*, 473 U.S. at 483-84.

24. *Haroco, Inc. v. American Nat’l Bank & Trust Co.*, 747 F.2d 384, 385 (7th Cir. 1984), *aff’d*, 473 U.S. 606 (1985).

25. *Ocean Energy II, Inc. v. Alexander & Alexander, Inc.*, 868 F.2d 740, 741-42 (5th Cir. 1989).

26. *Ashland Oil, Inc. v. Arnett*, 875 F.2d 1271 (7th Cir. 1989).

27. *Fleischhauer v. Feltner*, 879 F.2d 1290, 1293-95, 1300 (6th Cir. 1989) (limiting RICO recovery to trebled actual, not expectation, damages).

28. *Sun Sav. & Loan Ass’n v. Dierdorff*, 825 F.2d 187, 190 (9th Cir. 1987).

29. *Illinois Dep’t of Revenue v. Phillips*, 771 F.2d 312, 313 (7th Cir. 1985).

diligence.³⁰

In these cases, the disputes grew out of business matters or relationships, and in most of the cases the plaintiffs also had state remedies which they were pursuing simultaneously in the RICO case. Because treble damages and attorney's fees are available when a RICO claim succeeds, however, the plaintiffs' lawyers add RICO claims to complaints and go to federal court whenever possible; indeed, it has been suggested that *not* doing so could be legal malpractice.³¹

The mail and wire fraud statutes enable the federal government to prosecute virtually anyone who uses either of these ubiquitous means in furtherance of a fraudulent scheme.³² Other than via RICO, there is no federal private cause of action for the victims of mail and wire fraud.³³ By allowing only government prosecution under the mail and wire fraud statutes, Congress limited their application. Prosecutorial discretion and limited resources combine to restrict the number of cases brought under the statutes. Civil RICO bypasses these limitations by providing a private cause of action for mail and wire fraud. Some RICO practitioners argue that the requirement under civil RICO that all of the elements of the mail and wire fraud offenses be met for each predicate act³⁴ allows for considerable judicial "pruning" of the multitude of "garden variety fraud" cases that plaintiffs endeavor to bring.³⁵ This judicial "pruning" does not happen. The plaintiffs in these "garden variety fraud" cases do not need treble damages as encouragement and, moreover, most of these cases have no place in federal court. The disputes are nothing more than commercial disagreements, well suited to resolu-

30. *Metropolitan Int'l, Inc. v. Alco Standard Corp.*, 657 F. Supp. 627, 629 (M.D. Pa. 1986).

31. See, e.g., Rehnquist, *Reforming Diversity Jurisdiction and Civil RICO*, 21 ST. MARY'S L.J. 5, 10 (1989) (originally presented at the Brookings Institution's Eleventh Seminar on the Administration of Justice, Apr. 7, 1989) (stating that "[a]ny good lawyer who can bring himself within the terms of the federal civil RICO provisions will sue in federal court because of the prospect of treble damages and attorney's fees which civil RICO holds out"); Note, *Clarifying a "Pattern" of Confusion: A Multi-Factor Approach to Civil RICO's Pattern Requirement*, 86 MICH. L. REV. 1745, 1770 (1988) (stating that "[i]ndeed, it is so easy and tempting to allege a RICO claim that counsel may commit malpractice if a RICO claim is not made when the section 1962 statutory elements have been satisfied").

32. 18 U.S.C. § 1341 (1988) (mail fraud); *id.* § 1343 (wire fraud).

33. See *Ryan v. Ohio Edison Co.*, 611 F.2d 1170 (6th Cir. 1979) (mail fraud); *Bell v. Health-Mor, Inc.*, 549 F.2d 342 (5th Cir. 1977) (mail fraud); *Napper v. Anderson, Henley, Shields, Bradford & Pritchard*, 500 F.2d 634, 636 (5th Cir. 1974) (wire fraud), *cert. denied*, 423 U.S. 837 (1975); *Moss v. Morgan Stanley, Inc.*, 553 F. Supp. 1347, 1361 (S.D.N.Y.) (mail fraud), *aff'd*, 719 F.2d 5 (2d Cir. 1983), *cert. denied*, 465 U.S. 1025 (1984); *Milburn v. Blackfrica Promotions, Inc.*, 392 F. Supp. 434, 435 (S.D.N.Y. 1974) (mail fraud).

34. See generally Buffone, *Civil RICO: The Use of Mail and Wire Fraud As Predicate Offenses*, 1989 RICO LITIGATION UPDATE 389.

35. See Best & Paull, *Stopping Civil RICO at the Garden Gate: The Judicial Pruning of Mail and Wire Fraud As Predicate Offenses*, 1988 RICO LITIGATION UPDATE 333.

tion under state laws in state courts.

The ease with which plaintiffs can recast ordinary state fraud complaints as RICO allegations also skews the balance developed under state law and gives RICO plaintiffs a super-plaintiff status. For example, RICO makes it easier to bring a state court fraud case in federal court by providing RICO plaintiffs with an easier burden of proof than in state court. An allegation of common-law fraud requires proof by "clear and convincing" evidence,³⁶ because of the moral stigma that society attaches to such a determination.³⁷ The federal courts, however, consistently have rejected a more stringent burden of proof than "preponderance of the evidence" in RICO actions predicated on fraud claims.³⁸

Excising mail and wire fraud as predicate offenses generally would remove these cases from federal court and would eliminate the super-plaintiff status that RICO accords fraud plaintiffs. This deletion would cure the primary misuse of RICO.

B. Multiple Victims

There are those, however, who see RICO as a salutary statute that laudably facilitates federal civil actions by the victims of fraud, and who for that reason would object to the deletion of mail and wire fraud as predicate offenses for civil RICO actions.³⁹ I would meet these objections by maintaining mail and wire fraud as predicate offenses in cases involving one hundred or more victims. Litigants and attorneys should be encouraged to pursue litigation in fraud cases in which there are a large number of dispersed victims, because absent collective action and treble damages, each victim has insufficient incentive to sue. The full panoply of civil RICO predicate offenses should therefore remain avail-

36. See 9 J. WIGMORE, EVIDENCE IN TRIALS AT COMMON LAW § 2498, at 424 & n.13 (Chadbourn rev. ed. 1981 & Supp. 1989).

37. See, e.g., *Addington v. Texas*, 441 U.S. 418, 424 (1979) (stating that "[t]he interests at stake in those cases are deemed to be more substantial than mere loss of money and some jurisdictions accordingly reduce the risk to the defendant of having his reputation tarnished erroneously by increasing the plaintiff's burden of proof"); *Schneiderman v. United States*, 320 U.S. 118, 178 (1943) (Stone, J., dissenting) (noting that "fraud, which involves personal moral obliquity, must be proved by clear and convincing evidence").

38. See *Fleischhauer v. Feltner*, 879 F.2d 1290, 1296 (6th Cir. 1989); cf. *Sedima, S.P.R.L. v. Imrex Co.*, 473 U.S. 479, 491 (1985) (hinting that preponderance is the appropriate burden of proof); *Wilcox v. First Interstate Bank of Oregon*, 815 F.2d 522, 530-31 (9th Cir. 1987) (asserting that a RICO claim is not collaterally estopped by an adverse judgment on a common-law fraud claim in state court, because of the lower burden of proof under RICO).

39. See, e.g., Goldsmith, *Civil RICO Reform: The Basis for Compromise*, 71 MINN. L. REV. 827, 832-37 (1987); Goldsmith & Keith, *Civil RICO Abuse: The Allegations in Context*, 55 B.Y.U. L. REV. 55, 78-84 (1986); Schanzle-Haskins, *Opinion*, RICO LITIGATION REP., Jan. 1985, at 1. See generally Corrigan, *supra* note 4, at 2116.

able only when there are one hundred or more victims and the action can qualify as a class action pursuant to rule 23(b)(3) of the Federal Rules of Civil Procedure.⁴⁰

Subdivision (b)(3) of rule 23 allows an action to be maintained as a class action if the prerequisites of subdivision (a) are satisfied, and "the court finds that the questions of law or fact common to the members of the class predominate over any questions affecting only individual members, and that a class action is superior to other available methods for the fair and efficient adjudication of the controversy."⁴¹ The policy considerations that have shaped the development of the law of rule 23(b)(3), as explained by the Advisory Committee, are very similar to those which motivate preserving multiple-victim civil RICO actions predicated on mail or wire fraud: continuing to allow these cases "would achieve economies of time, effort, and expense, and promote uniformity of decision as to persons similarly situated, without sacrificing procedural fairness or bringing about other undesirable results."⁴² The Committee observed further that "a fraud perpetrated on numerous persons by the use of similar misrepresentations may be an appealing situation for a class action. . . ."⁴³

Recent examples of the type of fraud-based RICO claims that would be preserved include classes of ratepayers who were overcharged by their electric utility,⁴⁴ tenants in a huge apartment complex undergoing condominium conversion who were misled by the owners,⁴⁵ and

40. This exception to the proposed deletions should be approved by the "consumers' lobbies." See 7B C. WRIGHT, A. MILLER & M. KANE, FEDERAL PRACTICE AND PROCEDURE § 1782 (1986 & Supp. 1988). This authority suggests:

A Rule 23(b)(3) action also may prove to be the most effective means of providing relief to the consumer class The knowledge that aggrieved parties may act independently through the courts to preserve their rights also could have a significant deterrent effect on businesses that might engage in practices that are harmful to the consumer and contrary to public policies

Id. § 1782, at 56-57.

41. FED. R. CIV. P. 23(b)(3). The rule guides the court's consideration of this inquiry by adding the following:

The matters pertinent to the findings include: (A) the interest of members of the class in individually controlling the prosecution or defense of separate actions; (B) the extent and nature of any litigation concerning the controversy already commenced by or against members of the class; (C) the desirability or undesirability of concentrating the litigation of the claims in the particular forum; (D) the difficulties likely to be encountered in the management of a class action.

Id.

42. FED. R. CIV. P. 23(b)(3) advisory committee's note to 1966 amendment.

43. *Id.*

44. *County of Suffolk v. Long Island Lighting Co.*, 710 F. Supp. 1428 (E.D.N.Y. 1989) (approving class settlement); *County of Suffolk v. Long Island Lighting Co.*, 710 F. Supp. 1407 (E.D.N.Y. 1989) (certifying class).

45. *Beauford v. Helmsley*, 865 F.2d 1386 (2d Cir.) (en banc), *vacated*, 109 S. Ct. 3236, *aff'd*,

consumer purchasers who had been duped into agreeing to unfavorable purchase financing.⁴⁶ Thus, an important advantage of the class approach is that it would build upon on a substantial body of well developed law.

C. Securities Fraud

Many authors have written about the impact of RICO on the private remedies available under the securities laws, and no attempt will be made to duplicate those efforts here.⁴⁷ Justice Thurgood Marshall explained the problem in his dissent in *Sedima*⁴⁸ in which three other Justices joined. He observed that RICO

virtually eliminates decades of legislative and judicial development of private civil remedies under the federal securities laws. Over the years, courts have paid close attention to matters such as standing, culpability, causation, reliance, and materiality, as well as the definitions of "securities" and "fraud." All of this law is now an endangered species because plaintiffs can avoid the limitations of the securities laws merely by alleging violations of other predicate acts.⁴⁹

Furthermore, Congress has considered directly the appropriate remedy for violation of the securities laws, and in section 28(a) of the Securities Exchange Act of 1934⁵⁰ it chose to limit such damages to actual damages. Daniel L. Goelzer, the General Counsel of the Securities and Exchange Commission, recently noted:

as Section 28(a) reflects, damages in excess of actual injury are unnecessary to accomplish the goals of the federal securities laws, and, indeed, may work at cross purposes with such goals. The possibility of such liability can deter legitimate en-

893 F.2d 1433 (2d Cir.), *cert. denied*, 110 S. Ct. 539 (1989).

46. *Heastie v. Community Bank*, 125 F.R.D. 669 (N.D. Ill. 1989).

47. *See, e.g.*, ABA RICO REPORT, *supra* note 3, at 240 n.363.

48. *Sedima, S.P.R.L. v. Imrex Co.*, 473 U.S. 479, 500 (1985) (Marshall, J., dissenting).

49. *Id.* at 505 (citation omitted). Justice Thurgood Marshall supplied several examples of this "endangered species" law:

[E]ven in cases in which the investment instrument is not a "security" covered by the federal securities laws, RICO will provide a treble-damages remedy to a plaintiff who can prove the required pattern of mail or wire fraud. Before RICO, of course, the plaintiff could not have recovered under federal law for the mail or wire fraud violation.

Similarly, a customer who refrained from selling a security during a period in which its market value was declining could allege that, on two occasions, his broker recommended by telephone, as part of a scheme to defraud, that the customer not sell the security. The customer might thereby prevail under civil RICO even though, as neither a purchaser nor a seller, he would not have had standing to bring an action under the federal securities laws.

The effect of civil RICO on federal remedial schemes is not limited to the securities laws. For example, even though commodities fraud is not a predicate offense listed in § 1961, the carefully crafted private damages causes of action under the Commodity Exchange Act may be circumvented in a commodities case through civil RICO actions alleging mail or wire fraud. *Id.* at 505-06 (citations omitted). Of course, commodities fraud RICO actions, as in *Parnes v. Heind Commodities, Inc.*, 487 F. Supp. 645 (N.D. Ill. 1980), cited by Justice Marshall, would be precluded by eliminating mail and wire fraud as predicate offenses.

50. 15 U.S.C. § 78bb(a) (1988).

terprise, impede the raising of capital, and impose excessive litigation costs, costs that inevitably are borne by consumers and investors.⁵¹

There is simply no general need to encourage litigation for securities fraud as civil RICO does nor is there justification for shifting the balance in such litigation as drastically in favor of a securities fraud plaintiff as RICO does by threatening treble damages and attorney's fees. Eliminating securities fraud from the list of predicate offenses would restore the level playing field to securities litigation.

D. Civil RICO Cases Based on Other Predicate Offenses

I perceive no systematic misuse in the reported civil RICO actions which are based on the other predicate offenses. A few recent cases illustrate my point:

- In a class action, customers sued a public utility for bribing members of a state regulatory body and thereby causing that body to approve excessive rates to be charged by the utility to its customers. The RICO claims were predicated on a state bribery statute.⁵²

- A women's health center brought an action against pro-life activists for repeated physical attacks on its premises, employees, and patients in an effort to force the center out of business. The predicate acts were violations of the Hobbs Act, 18 U.S.C. section 1951, which relates to "[i]nterference with commerce by threats or violence."⁵³

- A small private bus company alleged that a union local had threatened the bus company's property or employees in the course of a labor organizing effort. The RICO claim was predicated on the threats of violence.⁵⁴

Some commentators like to cite these types of cases as examples of the overbreadth of civil RICO.⁵⁵ But these are precisely the types of cases that, with only slightly different facts, would enable civil recovery by the victims of classic mobster behavior. These defendants did just what would be expected from the mob; for example, if we substitute

51. *Hearings on H.R. 1046 Before the Subcomm. on Crime of the House Comm. on the Judiciary*, 101st Cong., 1st Sess. (1989) (hearings not officially printed as of current date) (summary of statement of Mr. Goelzer).

52. *H.J. Inc. v. Northwestern Bell Tel. Co.*, 109 S. Ct. 2893, 2897 (1989). In a similar case, a county sued a public utility for lying to the public rate commission to obtain higher rates. After a jury verdict awarding \$22.9 million in trebled damages to the county, the court granted the utility's motion for judgment notwithstanding the verdict on rather vague state sovereignty grounds. *County of Suffolk v. Long Island Lighting Co.*, 710 F. Supp. 1387 (E.D.N.Y. 1989).

53. *Northeast Women's Center, Inc. v. McMonagle*, 868 F.2d 1342, 1348-50 (3d Cir.), *cert. denied*, 110 S. Ct. 261 (1989).

54. *Yellow Bus Lines, Inc. v. Drivers, Chauffeurs & Helpers Local Union 639*, 883 F.2d 132 (D.C. Cir. 1989).

55. *See, e.g., Rehnquist, supra* note 31, at 11 (referring to the abortion clinic and labor union cases as examples of the "tremendous reach" of civil RICO).

“sham pro-life activists employed by a rival clinic run by organized crime” for “pro-life activists,” or “mob-infiltrated union local” for “union local,” it is apparent that the acts the defendants committed in those cases are exactly what RICO was crafted to target. Consequently, there is no need to cut back on the use of predicate offenses other than mail, wire, and securities fraud.

V. OTHER PROPOSED REFORMS

Bills have been introduced to amend—and reform—RICO every year in recent memory, and this year is no exception.⁵⁶ Deletion of the fraud predicate offenses is the crucial reform. After that deletion, civil RICO will not require any other profound changes. Nonetheless, comments on some of the changes that have been proposed are included below.

A. Redacting “Racketeering”

No one, especially an accountant, wants to be called a racketeer: “We are a profession that lives on its reputation. So if somebody runs around impugning our integrity, we take that very seriously. You shouldn’t allow any ordinary citizen to jump up and scream, ‘Racketeer!’”⁵⁷

Once mail, wire, and securities fraud have been removed as predicate offenses for civil RICO, thus removing routine business disputes from the reach of the statute, there will be less perceived need to be rid of the R-word. RICO should remain “RICO.” One idea that seems altogether unworkable is, while leaving “racketeer” in the Act, prohibiting the attorneys in civil actions from using that word in written or oral presentations to the court.⁵⁸

B. Automatic Treble Damages

Most proposed amendments of civil RICO restrict automatic treble damages, costs, and attorney’s fees to “government entity” plaintiffs⁵⁹

56. For some of the recent House efforts, see H.R. 1046, 101st Cong., 1st Sess. (1989); H.R. 4920, 100th Cong., 2d Sess. (1988); H.R. 4923, 100th Cong., 2d Sess. (1988); H.R. 3240, 100th Cong., 1st Sess. (1987); and H.R. 2983, 100th Cong., 1st Sess. (1987).

57. Corrigan, *supra* note 4, at 2114 (quoting Theodore C. Barreaux, of the American Institute of Certified Public Accountants).

58. See H.R. 1046, *supra* note 56, § 4 (proposed 18 U.S.C. § 1964(c)(10)). For example, how is RICO to be referred to? “This action is brought pursuant to the ***** Influenced and Corrupt Organizations Act (* ICO’) Under * ICO”

59. A “government[al] entity” is the United States or a State, including any agency or department thereof, or a unit of local government (determined by its ability to (1) levy taxes and spend funds, and (2) to exercise general corporate and police powers). See *id.* § 4 (proposed 18 U.S.C. § 1964(c)(1)(A)).

or predicate-offense-convicted defendants. This seems odd: government entities do not need to be encouraged to bring litigation, and no benefit to society arises from implicitly encouraging potential wrongdoers to redirect their racketeering activity away from government entities and toward private individuals.⁶⁰

Furthermore, the effect of the criminal conviction requirement would be peculiar. Part of the reason treble damages, costs, and attorney's fees are provided is to encourage the bringing of civil actions that might be difficult to win and which therefore might not otherwise be brought. This usual justification is absent when a criminal conviction has already been obtained. Because the civil RICO action requires proof by only a preponderance of the evidence and the defendant already has been proven guilty of the predicate offenses beyond a reasonable doubt, these actions would seem to be nearly guaranteed winners. Besides, another function of civil RICO is to complement the efforts of prosecutors, which is hardly promoted by allowing automatic treble damages and attorney's fees only after the prosecutors have done their work.

If, on the other hand, the idea behind a criminal conviction requirement is that treble damages and attorney's fees are appropriate *because* the defendant has been proven guilty of the predicate offenses beyond a reasonable doubt, then why not just allow automatic treble damages and attorney's fees whenever the plaintiff can prove the predicate offenses to that level of certainty? Why should some plaintiffs, equally injured, be able to recover less in damages just because their defendants were not prosecuted for their crimes? Looking at it from the other side, why should the miscreants who luckily have avoided prosecution for their crimes be blessed with the extra good fortune of freedom from treble damages and attorney's fees in a civil RICO action brought by their wasted victims?

60. The care with which the legislative proposals preserve the ability of state and local governments to win treble damages under civil RICO is interesting. This preservation is the result of intensive lobbying efforts by state attorneys general and municipal corporation counsels. *See, e.g.,* Corrigan, *supra* note 4, at 2114 (quoting Steven Twist, chief assistant attorney general of Arizona). Twist, who has been active in save-RICO efforts by the National Association of Attorneys General, stated that "[t]he elimination of the triple damages remedy emasculates the statute." *Id.*; *see also* *Hearings on H.R. 1046 Before the Subcomm. on Crime of the House Comm. on the Judiciary*, 101st Cong., 1st Sess. (1989) (hearings not officially printed as of current date) (statement of Peter L. Zimroth, Corporation Counsel of the City of New York) (noting that "[t]he City has been very successful with RICO").

The state and local government lawyers have lobbied vigorously to preserve for themselves a remedy in federal court, which they obviously find preferable to what their own legislatures have provided. Thus, for example, this provision will preserve the ability of state tax officials to obtain treble damages from state tax cheats under civil RICO, a remedy denied them by their own legislatures. *See Illinois Dep't of Revenue v. Phillips*, 771 F.2d 312 (7th Cir. 1985) (predicate offense: mail fraud).

C. Double Punitive Damages

Another common feature of recent legislative proposals is to limit RICO damages to actual damages upon proof by a preponderance of the evidence, initially, and then to allow certain classes of plaintiffs to recover costs and attorney's fees. These favored plaintiffs also would be granted punitive damages up to twice the amount of actual damages if they can prove by clear and convincing evidence that the defendant's actions were reckless.⁶¹ Recent bills specially favor the plaintiff who is (1) a unit of local government that is not a "government entity" or (2) a natural person, tax-exempt organization, trust, pension fund, or investment company, and the injury is caused by insider trading, or (3) a natural person or consumer and no remedy is available from securities or commodities laws, or (4) a natural person who suffers serious bodily injury by reason of a violent predicate offense.⁶²

All of these machinations obviously are intended to exclude ordinary businesses from pursuing civil RICO actions. However, straining to exclude ordinary business from treble damages and limiting most other plaintiffs to only the possibility of double punitive damages ignores the two-sided objective of treble damages: rewarding, and thus encouraging, the pursuit of difficult litigation, and punishing, and thus deterring, the perpetrators.

Nor is the manner in which this scheme roughly correlates remedy with proof appropriate: proof beyond a reasonable doubt, as determined beforehand in a criminal trial, entitles the civil RICO plaintiff to automatic treble damages;⁶³ proof of recklessness by clear and convincing evidence makes the preferred plaintiff eligible for double punitive damages;⁶⁴ proof by a mere preponderance of the evidence provides only actual damages.⁶⁵ This approach turns the traditional notion of damages on its head: it would no longer matter what the defendant had done, but only how well the plaintiff could prove it.

The complicated mixing of burdens of proof with mens rea in these

61. See H.R. 1046, *supra* note 56, § 4 (proposed 18 U.S.C. § 1964(c)(3)(D)). While previous bills tended to employ the usual recklessness language—"conscious and wanton disregard of the consequences," this year a completely new expression, not to be found in any federal case or statute, has arisen—"consciously malicious, or so egregious and deliberate that malice may be implied." *Id.* As a novel expression, this phrase certainly would lead lawyers to argue, and courts to conclude, all quite reasonably, that Congress intended a meaning different from "conscious and wanton disregard." Whatever the drafters mean by this new expression, they should endeavor to make it clear in the statute and absolutely crystalline in the committee reports.

62. See *id.* § 4 (proposed 18 U.S.C. § 1964(c)(2)(B)).

63. *Id.* (proposed 18 U.S.C. § 1964(c)(5)).

64. *Id.* (proposed 18 U.S.C. § 1964(c)(2)(C)).

65. See *id.* § 4 (proposed 18 U.S.C. § 1964(c)(2)(A), (c)(3)).

proposals is another problem.⁶⁶ Most of the predicate acts are specific intent crimes, such that the civil RICO plaintiff must prove, by a preponderance of the evidence, that the defendant intentionally committed the predicate offenses. Then, to qualify for punitive damages, the preferred plaintiff additionally must prove by a higher burden of proof, clear and convincing evidence, that the defendant acted with a lesser mens rea level, recklessness, in perpetrating the RICO pattern of predicate offenses. This sequence of proof and mens rea levels seems subtle beyond meaning.

D. Statute of Limitations

Recent proposals have tended to provide a standard four year statute of limitations, or two years after a criminal conviction, or six years for government entities, all tolled during the pendency of a government civil or criminal action.⁶⁷ A system of different limitations periods for different plaintiffs is needlessly complex and reflects inappropriate priorities. The purpose of civil RICO is to encourage private victims to enforce their rights against wrongdoers—so why give preferential treatment to government entities, which are far better equipped to discover wrongdoing and muster the resources to pursue litigation to recover for it than are private parties? The extra two years after a conviction are also superfluous: why particularly facilitate those civil actions?

The statute of limitations for civil RICO actions should be that of the last predicate offense. The standard federal criminal limitations period is five years,⁶⁸ and shortening the period vis-a-vis ordinary plaintiffs and lengthening it for governmental plaintiffs, and lengthening it even further after a criminal conviction, is unjustified. None of the purposes of having a limitations period is furthered by having different periods for different plaintiffs.

E. Universal Service of Process

The recent reform bills extend the reach of service of process in civil RICO actions, beyond "any judicial district of the United States" to "anywhere."⁶⁹ Such a provision for service of process does not comport with due process constraints on the ability of a federal court to exercise personal jurisdiction over foreign parties. Rather than forcing the courts to deal with this issue *ab initio*, Congress should make explicit its intent in this regard.

66. *Id.*

67. *See id.* (proposed 18 U.S.C. § 1964(c)(6)).

68. 18 U.S.C. § 3282 (1988).

69. *See* H.R. 1046, *supra* note 56, § 5.

F. Affirmative Defense

Recent bills have introduced an affirmative defense of good faith reliance on governmental action.⁷⁰ No such defense is needed or desirable, because whether good faith reliance is an adequate defense is a question to be resolved with regard to each predicate offense. If, under the established law controlling the predicate offenses at issue in a particular case, a defendant is denied good faith reliance as an affirmative defense, that denial should resolve the issue for the RICO claim as well.

VI. CONCLUSION

The problem with civil RICO is generally well understood: too many commonplace commercial disputes are brought as civil RICO actions in federal court. And it is a problem with a simple solution: delete mail, wire, and securities fraud as predicate offenses, except in large class actions.

This is a straightforward, easily accomplished solution that goes to the core of the problem. The solutions thus far proposed by Congress go too far and gut civil RICO or create new problems that will require yet another round of motions, decisions, and appeals in an already over-RICOed court system.

70. See *id.* § 4 (proposed 18 U.S.C. § 1964(c)(7)).

