THE USES AND MISUSES OF RICO IN CIVIL LITIGATION: A GUIDE FOR PLAINTIFFS AND DEFENDANTS

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I. Introduction

The Racketeer Influenced and Corrupt Organizations Act (RICO)\(^1\) has, since its enactment in 1970, been utilized in an increasing number of private civil actions under the federal securities laws and, to a lesser extent, under federal antitrust laws. The emerging use of RICO in the context of traditional civil lawsuits presents unique opportunities and risks both for plaintiffs who invoke the statute and for defendants who find themselves confronting RICO-based claims.

From the standpoint of the plaintiff, the inclusion of RICO claims as part of a securities or antitrust action tends to enhance the magnitude of the case, primarily since a violation of RICO can lead to treble damage awards as well as attorneys' fees.\(^2\) At the same time, however, a complaint which alleges RICO violations generates complex issues of pleading and proof which may significantly complicate the prosecu-

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2. See infra note 12 and accompanying text.
tion of the underlying claims of securities fraud or antitrust violation.

Concomitantly, from the defendant's standpoint, the assertion of a RICO claim also increases the magnitude and potential significance of the case. An alleged RICO violation confronts the defendant with the specter of quasi-criminal allegations which could stigmatize as "racketeers" those individuals—such as investment advisers, accountants, lawyers, and executives of publicly-held companies—who are the typical defendants in securities and antitrust litigation.

As conflicting recent decisions demonstrate, no firm guidelines have emerged in the thirteen years since RICO's enactment on the viability of including a claim of racketeering in a traditional securities or antitrust litigation. Some courts have treated RICO as an effective civil remedy fashioned by Congress to regulate patterns of abuse in the securities industry and in other sectors of the economy. Other courts have criticized the "growing number of cases which improperly . . . exploit the vague language of the civil provisions of the federal racketeering statute in an attempt to recoup investment losses." Partly due to the volatile development of the law in this area, several well-known financial institutions which in the past have been targets of RICO claims are now turning to aggressive use of the statute as plaintiffs.

3. This conflict has been dramatically illustrated by recent decisions in the Second Circuit. One opinion, Moss v. Morgan Stanley, Inc., 719 F.2d 5 (2d Cir. 1983) (discussed infra note 88), explicitly favors civil RICO actions while the other, Trane Co. v. O'Connor Securities, 718 F.2d 26 (2d Cir. 1983) (discussed infra text accompanying notes 101-104), suggests that they should be curtailed. The contrary positions have already been noted by another commentator. See, e.g., Brodsky, Civil RICO Actions—What is Position of Second Circuit?, 190 N.Y.L.J. 76, at 1, col. 1 (Oct. 19, 1983). See also infra cases in notes 49 & 50 (note 49 listing cases dismissing civil RICO actions; note 50 listing cases allowing them).

4. See infra text accompanying note 40.


Judge Duffy later reiterated this view in permitting plaintiff to amend the complaint. See Mauriber v. Shearson/American Express, 567 F. Supp. 1231 (S.D.N.Y. 1983). See infra text at note 59. See also Schacht v. Brown, 711 F.2d 1343 (7th Cir.), cert. denied, 52 U.S.L.W. 3423 (Nov. 28, 1983). The Seventh Circuit, although refusing to dismiss a civil RICO action for alleged business fraud, observed: "Congress . . . may well have created a runaway treble damage bonanza for the already excessively litigious." Schacht 711 F.2d at 1361. The Supreme Court recently denied certiorari in the case, thereby declining its first invitation to construe RICO in a civil context. The writ was denied without comment.

In order to delineate the more significant issues raised by the use of RICO in civil litigation, this article describes the relevant provisions of the statute and explores the legislative history of its civil remedy provision. The article then identifies the predominant legal and strategic issues which the plaintiff and defendant must assess in preparing their respective cases. Finally, the article analyzes the decisions arising under RICO in order to clarify the current state of the law.

II. THE STATUTORY BACKGROUND

An extensive array of criminal activities are proscribed by RICO. Consistent with its dominant legislative purpose to control organized crime, the statute declares it unlawful for any person (1) to use or invest any income derived from "a pattern of racketeering activity . . . in acquisition of any interest in, or the establishment or operation of, any enterprise which is engaged in . . . interstate or foreign commerce";7 (2) to acquire or maintain through a pattern of racketeering "any interest in or control of any enterprise engaged in . . . interstate or foreign commerce";8 (3) "to conduct or participate . . . in the conduct of [an] enterprise's affairs through a pattern of racketeering activity or collection of unlawful debt";9 and (4) to conspire to violate any of the above provisions.10

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1982), discussed infra text accompanying notes 76-78; Cenco, Inc. v. Seidman & Seidman, 686 F.2d 449 (7th Cir.), cert. denied, 103 S. Ct. 177 (1982), discussed infra text accompanying notes 110-116.

7. 18 U.S.C. § 1962(a) provides, in relevant part, as follows:
   It shall be unlawful for any person who has received any income, 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.

8. 18 U.S.C. § 1962(b) is as follows: "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."

9. 18 U.S.C. § 1962(c) provides in full:
   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.

RICO also contains an expansive provision which defines "racketeering activity" so as to include a wide range of state and federal offenses and violations of the antifraud provisions of the federal securities laws.\textsuperscript{11} A "pattern" requires only two acts of racketeering activity within ten years of each other, one of which must have occurred after the effective date of the statute, October 15, 1970.\textsuperscript{12} Contributing further to the expansive application of the statute is the fact that each criminal act is counted as an act of racketeering activity, even if numerous acts arise from the same episode.\textsuperscript{13}

RICO, in addition to authorizing the government to seek substantial criminal\textsuperscript{14} and civil penalties,\textsuperscript{15} expressly grants a private right

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\item 18 U.S.C. § 1961(1)(D). More specifically, the statute defines "racketeering activity" to include "any offense involving fraud connected with a case under title 11 [the bankruptcy code] [or] fraud in the sale of securities . . . punishable under any law of the United States." \textit{Id.}
\item 14. 18 U.S.C. § 1963 on criminal penalties provides:
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\item (a) Whoever violates any provision of section 1962 of this chapter shall be fined not more than $25,000 or imprisoned not more than twenty years, or both, and shall forfeit to the United States (1) any interest he has acquired or maintained in violation of section 1962, and (a) any interest in, security of, claim against, or property or contractual right of any kind affording a source of influence over, any enterprise which he has established, operated, controlled, conducted, or participated in the conduct of, in violation of section 1962.
\item (b) In any action brought by the United States under this section, the district courts of the United States shall have jurisdiction to enter such restraining orders or prohibitions, or to take such other actions, including, but not limited to, the acceptance of satisfactory performance bonds, in connection with any property or other interest subject to forfeiture under this section, as it shall deem proper.
\item (c) Upon conviction of a person under this section, the court shall authorize the Attorney General to seize all property or other interest declared forfeited under this section upon such terms and conditions as the court shall deem proper. If a property right or other interest is not exercisable or transferable for value by the United States, it shall expire, and shall not revert to the convicted person. All provisions of law relating to the disposition of property, or the proceeds from the sale thereof, or the remission or mitigation of forfeitures for violation of the customs laws, and the compromise of claims and the award of compensation to informers in respect of such forfeitures shall apply to forfeitures incurred, or alleged to have been incurred, under the provisions of this section, insofar as applicable and not inconsistent with the provisions hereof. Such duties as are imposed upon the collector of customs or any other person with respect to the disposition of property under the customs laws shall be performed under this chapter by the Attorney General. The United States shall dispose of all such property as soon as commercially feasible, making due provision for the rights of innocent persons.
\item 15. 18 U.S.C. § 1964 on civil remedies provides:
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of action for treble damages to anyone injured "by reason" of a violation of the statute.  

III. THE LEGISLATIVE HISTORY

The legislative history of RICO has provided fertile support for sharply conflicting interpretations of the scope of the statute's civil remedy provisions. The Senate Report accompanying the legislation

(a) The district courts of the United States shall have jurisdiction to prevent and restrain violations of section 1962 of this chapter by issuing appropriate orders, including, but not limited to: ordering any person to divest himself of any interest, direct or indirect, in any enterprise; imposing reasonable restrictions on the future activities or investments of any person, including, but not limited to, prohibiting any person from engaging in the same type of endeavor as the enterprise engaged in, the activities of which affect interstate or foreign commerce; or ordering dissolution or reorganization of any enterprise, making due provision for the rights of innocent persons.

(b) The Attorney General may institute proceedings under this section. In any action brought by the United States under this section, the court shall proceed as soon as practicable to the hearing and determination thereof. Pending final determination thereof, the court may at any time enter such restraining orders or prohibitions, or take such other actions, including the acceptance of satisfactory performance bonds, as it shall deem proper.

(c) 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.

(d) A final judgment or decree rendered in favor of the United States in any criminal proceeding brought by the United States under this chapter shall estop the defendant from denying the essential allegations of the criminal offense in any subsequent civil proceeding brought by the United States.

16. U.S.C. § 1964(c). The statute also authorized the imposition of attorneys' fees in favor of the prevailing party. Among the civil remedies which the government may seek in an action under RICO are the divestiture of the violator's business interests, dissolution of the enterprise, and injunctions against a violator's participation in similar enterprises. 18 U.S.C. § 1964(a)-(b), (d). A previous criminal conviction under RICO operates to estop the defendant from denying the essential allegations in a subsequent civil proceeding by the government. Collateral estoppel has also been applied in subsequent non-governmental proceedings. In County of Cook v. Lynch, 560 F. Supp. 136 (N.D. Ill. 1982), a local governmental agency was permitted to use a prior criminal conviction for offensive collateral estoppel purposes. In permitting the use of offensive collateral estoppel by a party to a civil proceeding other than the United States government, the court in Lynch observed that "section 904(a) of RICO . . . specifically directs that its provisions 'shall be liberally construed to effectuate its remedial purposes,' . . ." id. at 139, and concluded that a prior criminal conviction can be utilized by any party to a subsequent civil proceeding because "[i]t would thus be most inconsistent with the intent of Congress for this court to rely on a negative inference [i.e., that only the United States government could offensively use a prior criminal conviction] from the statutory language to deny a remedy against RICO violators which the federal common law . . . would otherwise provide." Id.

17. The legislative history of RICO includes: Organized Crime Control: Hearings
broadly stated that the act “has as its purpose the elimination of the infiltration of organized crime and racketeering into legitimate organizations operating in interstate commerce.”¹⁸

This broad policy objective also characterizes earlier Congressional statements regarding the legislation eventually enacted as RICO. In 1950, the Kefauver Committee, in disclosing the problems of the infiltration of business by organized crime, conceived of the precursor to RICO as a supplement to the federal antitrust laws which had long provided express civil remedies.¹⁹ The Kefauver Committee asserted that criminal methods were widely used to infiltrate legitimate businesses and create monopolies and unfair competition. As a result, the Kefauver Committee envisioned the use of civil sanctions analogous to antitrust remedies as a means of achieving the proposed statutory purpose of preventing the establishment of monopolies through racketeering activity.²⁰

Similarly, in 1967, a Presidential commission recommended the adoption of regulatory measures to control the infiltration of business by organized crime, stressing the importance and value of civil remedies modeled on the antitrust laws.²¹

RICO was ultimately enacted as a result of intense Congressional activity from 1967 through 1970.²² Congress consistently recognized that the inclusion of civil remedies entailed an “immense,” broadening of the scope of RICO.²³ However, Congress did not include pro-

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23. As one representative noted in the House debate:
visions in the statute to address potential legal issues associated with the creation of a private treble-damages remedy. RICO provides an ample array of remedies for a wide variety of conduct, “balancing the need to redress a broad social ill against the virtues of tight, but possibly overly astringent, legislative draftsmanship.”24 In emphasizing the intentional breadth of the remedial civil provisions, Senator Dole of Kansas stated, in a comment typifying other policy announcements: “It is impossible to overstate the importance of S.30’s legislative attack on organized crime . . . Title IX of the Organized Crime Control Act . . . contains a proposal designed to curtail—and eventually to eradicate—the vast expansion of organized crime’s economic power.”25

Given the sweep of the statute’s remedial nature, RICO’s definition of racketeering activity was broadly worded and deliberately contained no reference to the term “organized crime” or to the related concepts of crime families and criminal syndicates. Representative Biaggi of New York expressed the congressional view that flexibility in the application of the statute was essential, asserting that a restrictive definition of organized crime would impose unnecessary limitations on the use of the law.26 He also advanced the widely held view that a precise definition of organized crime “would raise serious constitutional problems” and that “to require a general showing that organized crime is involved as a predicate for the use of investigative techniques would be to cripple those techniques.”27 Representative Poff doubted that a meaningful definition of “organized crime” was even possible, emphasizing that the “concept of organized criminal activity is broader in scope than the concept of organized crime; it is meant to include any criminal activity collectively undertaken.”28

The expansive—and not coherently articulated—nature of the civil

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My objection to the bill in toto is that whatever its motives to begin with, we will end up with cases involving all kinds of things not intended to be covered, and a potpourri of language by which you can parade all kinds of horribles of overreach . . . [Suppose] five or more of [my colleagues] engage in . . . a game of poker and it lasts past midnight . . . thus continuing for a period of two days, then [they] have been running an organized gambling business and [they] can get 20 years and the federal government can grab off the pot besides.

24. See Schacht, 711 F.2d at 1354-55.
27. Id.
remedy provision was summarized in the House Report, which stated in part:

Section 1964 provides civil remedies for the violation of section 1962 . . . . Subsection (a) contains broad provisions to allow for reform of corrupted organizations. Although certain remedies are set out, the list is not meant to be exhaustive, and the only limit on remedies is that they accomplish the aim set out of removing the corrupting influence . . . . 29

Congress viewed these sweeping remedial provisions as a means of "striking a mortal blow against the property interests of organized crime." 30 The House Committee on the Judiciary explicitly viewed the civil remedy provision as a means of intensifying, through the vehicle of a private remedy, the severity of the financial consequences which would flow from racketeering activity. 31

It is clear from the legislative history that Congress deliberately refrained from anticipating the ultimate contours of the specific application of the civil remedy provision. Equally clear is that Congress envisioned the civil liability provision as an integral and potentially wide-ranging feature of the statute. It is against this background of such broad statements of Congressional intent and policy that the recent cases have reached their conflicting results.

IV. Overview: The Impact of RICO on the Litigation Strategies of Plaintiffs and Defendants

The emergence of RICO as a significant aspect of federal securities and antitrust litigation has created a number of alternatives which both plaintiffs and defendants must consider in devising litigation strategy in such cases. The development of strategies in this area is complex and uncertain because courts continue to reach divergent results on

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the basis of facts which are not easily distinguishable. Nevertheless, a few basic considerations have emerged.

In preparing a complaint under either the securities laws or the antitrust laws, the plaintiff faces a fundamental decision of whether to include a RICO-based claim. That decision initially depends on the determination of whether the facts reasonably support the inclusion of a racketeering claim. Because of RICO's broad definition of racketeering activity and the Act's specific reference to fraud in the sale of securities, there seems to be no significant obstacle to asserting a RICO claim, at least at the pleading stage.

If a decision is that a securities or antitrust action can also support a RICO claim, the plaintiff then must evaluate the risks and benefits of interposing such a claim. The potential benefits fall essentially into two categories. First, a RICO claim, if successfully prosecuted, enhances and magnifies the scope of potential recovery. Since RICO permits recovery of treble damages and attorneys' fees once liability is established, there is a significant increase in the value of the lawsuit because the measure of damages under the Securities Exchange Act of 1934 is generally limited to the actual loss sustained. Punitive damages in actions under the federal securities law are typically unavailable and the courts have cautioned against awards which are "grossly disproportionate to the harm done."

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32. See infra notes 49-50 and cases cited therein.
33. Rule 11 of the Federal Rules of Civil Procedure requires that an attorney sign a complaint and that the signature "constitute a certificate by him that ... to the best of his knowledge, information, and belief there is good ground to support" the pleading. See Fed. R. Civ. P. 11.
34. See supra note 16 and accompanying text.
35. See, e.g., 15 U.S.C. § 78r(a) dealing with liability for misleading statements under the 1934 Securities Act. The section provides:

Any person who shall make or cause to be made any statement in any application, report, or document filed pursuant to this chapter or any rule or regulation thereunder or any undertaking contained in a registration statement as provided in subsection (d) of section 780 of this title, which statement was at the time and in the light of the circumstances under which it was made false or misleading with respect to any material fact, shall be liable to any person (not knowing that such statement was false or misleading) who, in reliance upon such statement, shall have purchased or sold a security at a price which was affected by such statement, for damages caused by such reliance, unless the person sued shall prove that he acted in good faith and had no knowledge that such statement was false or misleading. A person seeking to enforce such liability may sue at law or in equity in any court of competent jurisdiction. In any such suit the court may, in its discretion, require an undertaking for the payment of the costs of such suit, and assess reasonable costs, including attorneys' fees, against either party litigant.
36. See, e.g., Green v. Wolf Corp., 406 F.2d 291, 303 (2d Cir. 1969), cert. denied,
The second potential benefit of including a RICO claim is more substantive. "Standing" under Rule 10b-5 is limited to actual purchasers or sellers of a security as a result of the Supreme Court's 1975 decision in Blue Chip Stamps v. Manor Drug Store. However, no such restriction on "standing" is embodied in RICO. Moreover, with the rising level of challenge to the assertion of a private remedy under the antifraud provisions of the federal securities laws, RICO provides an explicit private remedy for "fraud in the sale of securities."

Plaintiffs face significant hazards, however, when asserting a RICO-based claim in a typical securities or antitrust action. First, the filing of an action embodying RICO allegations materially increases the possibility that the defendants will move to dismiss for failure to state a claim under Federal Rules of Civil Procedure 12(b)(6). In effect, the early phases of the lawsuit are likely to be consumed in extensive litigation as to whether or not the RICO claims have stated a cause of action. This added risk of motions to dismiss or for summary judgment obviously increases the expense and difficulty, from the plaintiff's perspective, in prosecuting his case as efficiently and economically as possible.

There are other risks associated with asserting a securities claim grounded on RICO. If the case is assigned to a judge who has, in prior decisions, indicated a restrictive attitude toward the use of RICO in private actions, the assertion of the claim (which is properly regarded

395 U.S. 977 (1970). See also de Haas v. Empire Petroleum Co., 435 F.2d 1223 (10th Cir. 1970); Globus v. Law Research Serv., Inc., 418 F.2d 1276 (2d Cir. 1969) (any marginal deterrence of an award of punitive damages under the federal securities laws must be weighed against potentially massive injuries).


38. Section 1964(c) confers the right to sue on "[a]ny person injured in his business or property by reason of a violation of section 1962 of this chapter . . ." 18 U.S.C. § 1964(c). The courts have interpreted "business" in its ordinary sense and "property" in a broad manner, thus lessening the plaintiff's burden of showing standing. See Blakey & Gettings, Racketeer Influenced and Corrupt Organizations (RICO): Basic Concepts—Criminal and Civil Remedies, 53 TEMP. L.Q. 1009, 1040-43 (1980), and cases cited therein.

39. See supra note 11.

as a serious accusation of wrongdoing) might tend to discredit the validity and legitimacy of the underlying securities or antitrust claims. In addition, substantial problems of proof under RICO may tend to complicate the plaintiff’s task of establishing both the basic securities or antitrust violation and the RICO violation, thus materially increasing the cost of prosecuting the action.

Finally, a plaintiff devising his litigation strategy must also recognize that there are no reported decisions in which a litigant has successfully prevailed at trial on a RICO claim in which the litigation is essentially either a securities or antitrust action. This dearth of precedent to support a RICO claim may weigh heavily in plaintiff’s decision as to whether to include such a claim in his cause of action.

From the defendant’s standpoint, the assertion of a RICO claim raises equally significant, complex, and troublesome issues. Most of the recent RICO litigation involves corporate defendants, their management, lawyers, accountants, investment advisers, and banks. These defendants typically and justifiably react with deep concern to a complaint which includes a racketeering allegation. As one court has perceptively observed, the mere pendency of a RICO suit against a defendant involves a stigma which could affect the reputation, business, and personal life of that defendant. In this situation, the dominant first reaction of defendants is to seek an order dismissing the RICO aspect of the complaint.

But there are inherent problems in moving for an order of dismissal with respect to a RICO claim. The practical hazard is that the court may determine, as a technical pleading matter, that the RICO claim states a cause of action under Federal Rules of Civil Procedure
12(b)(6). Such a determination tends to elevate the RICO claim to a level of prominence in the litigation which it might not otherwise have occupied had it been allowed to remain as a mere adjunct of the underlying securities or antitrust claim. Also implicit in such a ruling is the court’s determination that a claim has been stated entitling the plaintiff to a trial in which the defendants would be required to defend the assertion that they engaged in racketeering activity.

Another risk in seeking a dismissal of the RICO claim is that if the motion is successful, the claim, in the majority of cases, will be deleted from the lawsuit without prejudice to its renewal. This creates a situation in which, even if the litigation is ultimately settled, the dismissed claim will not have been adjudicated and could then be reasserted by another plaintiff. On the other hand, if the RICO claim is not contested and the litigation is ultimately compromised, the settlement can be structured so that the dismissal acts as a bar to all the claims, including the RICO contentions, thus freeing the defendants from the possibility of continued litigation on the same events which gave rise to the RICO claim.

In the event the decision is made to include a RICO claim in a civil action, both the plaintiff and the defendant face a wide array of complex issues and strategic choices in prosecuting and defending the allegation. In recent months, an extensive body of case law has developed which sheds light on the available means of prosecuting—and defeating—claims which are grounded on RICO. Some of these cases will be discussed below.

V. THE OFFENSIVE USE OF RICO BY PLAINTIFFS

In the thirteen years since its enactment, RICO has generated conflicting results in the extent to which the federal courts have permitted the assertion of racketeering claims in “garden variety” securities


46. Where the parties enter into a stipulation recorded in the minutes of the court, the settlement agreement terminates all of the claims of the parties theretofore made before the action, and the agreement becomes enforceable as a contract binding on all parties thereto. Biener v. Hystron Fibers, Inc., 78 A.D.2d 162, 167, 434 N.Y.S.2d 343, 347 (1980); see also 15A Am. Jur. 2d Compromise and Settlement §§ 25 and cases cited therein.

47. See supra notes 22, 40 & 42; see also Schacht v. Brown, 711 F.2d 1343 (7th Cir.), cert. denied, 52 U.S.L.W. 3423 (Nov. 28, 1983) (refusing to limit the civil use of RICO); Mauriber, 567 F. Supp. at 1239 (Second Circuit announced “reluctant agreement” with Seventh Circuit decision in Schacht (see infra text accompanying notes 52-60); Hanna Mining v. Norcen, Fed. Sec. L. Rep. (CCH) ¶ 98,742 (N.D. Ohio 1982) (see infra text accompanying notes 60-73); Bennett v. Berg, 685 F.2d 1053 (8th
and antitrust lawsuits. Until the last two years, defendants prevailed in the majority of reported decisions which resolved the issue. Recently, however, a growing number of courts have permitted such claims. The newer decisions have concentrated on the broad remedial purposes of RICO and the expansiveness of the civil provisions in sustaining a cause of action. A consequence of the courts’ expansive reading of RICO has been that defendants themselves are interposing RICO counterclaims and, in some instances, traditional defendants, such as brokers, banks, and accountants, are affirmatively pursuing RICO claims as plaintiffs.

An example of the willingness of courts to expand the use of RICO in civil litigation is *Mauriber v. Shearson/American Express, Inc.*, where the court characterized as “simplistic” the defendants’ argument that a plaintiff was required to allege that “organized crime” had infiltrated a legitimate business. Defendants in *Mauriber*, who were primarily

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48. See supra note 3 where a recent conflict in the Second Circuit is noted.


51. See supra note 6; see also Bache Halsey Stuart Shields, Inc. v. Tracy Collins Bank & Trust Co., 558 F. Supp. 1042 (D. Utah 1983).


53. Id. at 396.

54. Id. Similarly, the court in *Lode v. Leonardo*, 557 F. Supp. 675, 680 (N.D. Ill. 1982), rejected the defense argument, advanced by two state-chartered banks, that RICO is a potent weapon designed for use in the battle against “organized crime” and that it was therefore inapplicable to a case such as this one involving only what the defendants characterized as “garden
directors and executives of a prominent brokerage firm, sought to dismiss the claim and argued that the absence of allegations that the firm was involved in organized crime warranted the dismissal.

Categorically rejecting that approach, the court in Mauriber ruled that RICO did not require an allegation that organized crime was operating an enterprise through a pattern of racketeering activity. Such a requirement might, in fact, according to the Mauriber court, defeat the purpose of the statute: "‘RICO’s definition of racketeering activity is broad and without explicit reference to ‘organized crime.’’"55 The court in Mauriber then held:

Therefore, until Congress promulgates more precise language for the invocation of RICO’s civil provision, I am constrained to find that if the racketeering activity explicitly proscribed by the statute is proven, RICO damages may be awarded to the appropriate plaintiff without proof that the defendant is connected to organized crime.56

Judge Duffy in Mauriber also rejected the defendant’s contention—frequently accepted by other courts in the earlier years of experience with RICO—that a securities fraud violation under section 10(b) of the Securities Exchange Act of 1934 is never actionable under RICO. Noting that "racketeering activity under RICO” specifically includes “fraud in the sale of securities,” the court concluded: "‘This leads to the inescapable conclusion that Congress intended there to be some overlap, and under the appropriate circumstances a violation of the securities laws may result in RICO liability.’"57

Although the plaintiff’s complaint in Mauriber was dismissed for failure to allege the underlying securities fraud with particularity, an amended complaint survived defendants’ motion to dismiss.58 In denying this second motion to dismiss, Judge Duffy reiterated his earlier view, finding himself “in reluctant agreement” with the view of the

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56. Id.
Seventh Circuit announced in Schacht v. Brown.59 The Schacht position is one of deference to the unambiguous language of RICO as enacted by Congress and asserts that the courts have no place in qualifying the civil use of the statute in a manner not intended by Congress.60

Like the Mauriber opinion, the decision in Hanna Mining Co. v. Norcen Energy Resources Ltd.61 also typifies recent cases which have permitted RICO claims in the context of securities and other commercial litigation. In fact, Norcen provides an outstanding example of such lawsuits for close analysis.

In Norcen the Hanna Mining Company (Hanna) and its chief executive officers attempted to defeat a hostile tender offer by Norcen Energy Resources Ltd. (Norcen).62 The complaint alleged violations of the antifraud provisions of the Securities Exchange Act of 193463 and the proxy and tender offer provisions of that statute.64 Named

59. Id. at 1239.
60. See Schacht, 711 F.2d at 1361 (quoting United States v. Turkette, 452 U.S. 576, 586-87 (1981): "The legislature having spoken, it is not our role to reassess the costs and benefits associated with the creation of a dramatically expansive, and perhaps insufficiently discriminate, tool for combatting organized crime." Turkette was a criminal case. As of this writing, the court has remained silent on the expanding use of RICO in civil actions. See supra note 5.).
62. Id. at 93,733.
64. Hanna, Fed. Sec. L. Rep. (CCH) at 93,733. Specifically the complaint alleged violations of §§ 10(b), 13(d), 14(3), and 20(a) of the Securities Act of 1934, 15 U.S.C. §§ 78j(b), 78m(d), 78n(e), and 78t(a). 15 U.S.C. § 78j(b) provides: It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national security exchange—(b) to use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.
15 U.S.C. § 78m(d) provides:
(1) Any person who, after acquiring directly or indirectly the beneficial ownership of any equity security of a class which is registered pursuant to section 78l of this title, or any equity security of an insurance company which would have been required to be so registered except for the exemption contained in section 78l(g)(2)(G) of this title, or any equity security issued by a closed-end investment company registered under the Investment Company Act of 1940 [15 U.S.C. § 80a-1 et seq.], is directly or indirectly the beneficial owner of more than 5 per centum of such class shall, within ten days after such acquisition, send to the issuer of the security at its prin-
as defendants were Norcen, its principal executive officers, and Lehman Brothers Kuhn Loeb, Inc., an investment banker retained in connection with the tender offer.

principal executive office, by registered or certified mail, send to each exchange where the security is traded, and file with the Commission, a statement containing such of the following information, and such additional information, as the Commission may by rules and regulations, prescribe as necessary or appropriate in the public interest or for the protection of investors—

(A) the background, and identity, residence, and citizenship of, and the nature of such beneficial ownership by, such person and all other persons by whom or on whose behalf the purchases have been or are to be effected;

(B) the source and amount of the funds or other consideration used or to be used in making the purchases, and if any part of the purchase price is represented or is to be represented by funds or other consideration borrowed or otherwise obtained for the purpose of acquiring, holding, or trading such security, a description of the transaction and the names of the parties thereto, except that where a source of funds is a loan made in the ordinary course of business by a bank, as defined in section 78c(a)(6) of this title, if the person filing such statement so requests, the name of the bank shall not be made available to the public;

(C) if the purpose of the purchases or prospective purchases is to acquire control of the business of the issuer of the securities, any plans or proposals which such persons may have to liquidate such issuer, to sell its assets or to merge it with any other persons, or to make any other major change in its business or corporate structure;

(D) the number of shares of such security which are beneficially owned, and the number of shares concerning which there is a right to acquire, directly or indirectly, by (i) such person, and (ii) by each associate of such person, giving the background, identity, residence, and citizenship of each such associate; and

(E) information as to any contracts, arrangements, or understandings with any person with respect to any securities of the issuer, including but not limited to transfer of any of the securities, joint ventures, loan or option arrangements, puts or calls, guaranties of loans, guaranties against loss, or guaranties of profits, division of losses or profits, or the giving or withholding of proxies, naming the persons with whom such contracts, arrangements, or understandings have been entered into, and giving the details thereof.

(2) If any material change occurs in the facts set forth in the statements to the issuer and the exchange, and in the statement filed with the Commission, an amendment shall be transmitted to the issuer and the exchange and shall be filed with the Commission, in accordance with such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

(3) When two or more persons act as a partnership, limited partnership, syndicate, or other group for the purpose of acquiring, holding, or disposing of securities of an issuer, such syndicate or group shall be deemed
Plaintiffs asserted that the same conduct in connection with the tender offer that gave rise to the securities claims also constituted a "person" for the purposes of this subsection.

(4) In determining, for purposes of this subsection, any percentage of a class of any security, such class shall be deemed to consist of the amount of the outstanding securities of such class, exclusive of any securities of such class held by or for the account of the issuer or a subsidiary of the issuer.

(5) The Commission, by rule or regulation or by order, may permit any person to file in lieu of the statement required by paragraph (1) of this subsection or the rules and regulations thereunder, a notice stating the name of such person, the number of shares of any equity securities subject to paragraph (1) which are owned by him, the date of their acquisition and such other information as the Commission may specify. If it appears to the Commission that such securities were acquired by such person in the ordinary course of his business and were not acquired for the purpose of and do not have the effect of changing or influencing the control of the issuer nor in connection with or as a participant in any transaction having such purpose or effect.

(6) The provisions of this subsection shall not apply to—

(A) any acquisition or offer to acquire securities made or proposed to be made by means of a registration statement under the Securities Act of 1933 [15 U.S.C. § 77a et seq.];

(B) any acquisition of the beneficial ownership of a security which, together with all other acquisitions by the same person of securities of the same class during the preceding twelve months, does not exceed 2 per centum of that class;

(C) any acquisition of an equity security by the issuer of such security;

(D) any acquisition or proposed acquisition of a security which the Commission, by rules or regulations or by order, shall exempt from the provisions of this subsection as not entered into for the purpose of, and not having the effect of, changing or influencing the control of the issuer or otherwise as not comprehended within the purpose of this subsection.

15 U.S.C. § 78n(e) states:

It shall be unlawful for any person to make any untrue statement of a material fact or omit to state any material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading, or to engage in any fraudulent, deceptive, or manipulative acts or practices, in connection with any tender offer or request or invitation for tenders, or any solicitation of security holders in opposition to or in favor of any such offer, request, or invitation. The Commission shall, for the purposes of this subsection, by rules and regulations define, and prescribe means reasonably designed to prevent, such acts and practices as are fraudulent, deceptive, or manipulative.

15 U.S.C. § 78t(a) provides:

Every person who, directly or indirectly, controls any person liable under any provision of this chapter or of any rule or regulation thereunder shall also be liable jointly and severally with and to the same extent as such controlled person to any person to whom such controlled person is liable, unless the controlling person acted in good faith and did not directly or indirectly induce the act or acts constituting the violation or cause of action.
violation of RICO. 65 Defendants sought the dismissal of the RICO claim. As is typically the case on such a motion, the defendants urged that dismissal was required because (1) RICO does not create a private cause of action for violation of the federal securities laws, and (2) fraud in connection with the purchase of securities in a tender offer does not constitute an offense on which liability under RICO can be predicated. 66

The Norcen court rejected each of these defense contentions. As for the claim that RICO did not create a private cause of action in the context of the federal securities laws, the court turned aside defendants’ policy argument—frequently enunciated in the thirteen years since RICO’s enactment—that to provide a private remedy “would effectively turn RICO into a catchall, Federal common law of fraud.” 67

In rejecting that position, the court in Norcen turned to the legislative history of the statute, focusing in particular on the remedial provisions of section 1964(c). 68 The Norcen court discredited what has traditionally become one of the prime defense arguments advanced in RICO litigation—that the plaintiff must plead and prove that the defendant is a member of organized crime in order to state a RICO claim. 69 Such a requirement would tend to insulate from RICO claims defendants such as corporate executives, investment brokerage firms, accountants, and lawyers. Finding definitive statutory grounds for broad civil remedies under RICO, and recognizing that his decision would implicate as defendants individuals not commonly associated with racketeering, Judge Manos asserted in Norcen:

Any restriction on the availability of a private right of action under 18 U.S.C. § 1964(c) should come from Congress and not be engrafted on the statute by the courts. Since, when enacted, no such restriction appeared in RICO and Congress was “well aware” that it was enlarging federal jurisdiction, the court holds that defendants’ . . . contention that

66. Id. at 93,734.
67. Id.
68. Id. at ¶ 98,735-737; see also supra notes 22-26 and accompanying text for the discussion on legislative history showing Congress’ intent to make RICO a broad piece of legislation.
69. See, e.g., Barr v. WUI/TAS, Inc., 66 F.R.D. 109 (S.D.N.Y. 1975) (see infra text accompanying notes 84-87), one of the earliest cases to inject the requirement of membership in “organized crime” as an element in civil RICO litigation.
RICO does not create a cause of action for violation of the federal securities laws to be without merit.  

Also significant in Norcen was the court's refusal to accept another widely urged defense contention—that a plaintiff must allege "competitive injury" in order to establish a civil RICO claim. In essence, the "competitive injury" concept stresses that RICO provides a damages remedy not for the direct victims of the offenses on which the RICO violation is predicated, but instead only for those plaintiffs who claim that they have been injured as a result of the illegitimate advantage derived by the defendant in operating an enterprise through racketeering activity. This concept relies on a purported analogy between the treble damages provisions of the antitrust laws and RICO. Judge Manos definitely rejected this judicial restriction on the scope of RICO, distinguishing the underlying purposes of the antitrust laws and the federal racketeering statute:

[T]his court finds that since the purposes of the federal antitrust laws (economic efficiency, protection of small business) are so divergent from the purposes of the civil damages provision of RICO (to deter commission of RICO's predicate offenses, threaten violators with financial ruin) that no reasonable comparison of the economic objectives underlying the two areas of law can be made. To conclude otherwise and restrict the right of action under 18 U.S.C. § 1964(c) only to those who or which are indirect victims of racketeeer-

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70. *Hanna*, Fed. Sec. L. Rep. (CCH) at 93,738 n.20 (citing United States v. Turkette, 452 U.S. 576 (1981)). According to the *Hanna* court, the Supreme Court found that "Congress was well aware that it was entering a new domain of federal involvement through the enactment of this measure." *See also* Meineke Discount Muffler Shops, Inc. v. Noto, 546 F. Supp. 352, 354 (E.D.N.Y. 1982) (McLaughlin, J.) ("Defendants assert that plaintiff fails to state a RICO claim because it has not alleged either a racketeering enterprise injury or that the defendants are members of organized crime . . . These arguments are without merit."). *See* N.Y. Times, June 27, 1983, at D-1, col. 3.


73. This analogy has been recognized by other courts. *See, e.g.*, Harper v. New Japan Sec. Int'l, Inc., 545 F. Supp. 1002 (C.D. Cal. 1982).
ing activity would leave undisturbed racketeers whose activity does not infringe on their competitors’ markets.\textsuperscript{74}

As in Norcen, RICO claims were also successfully interposed in \textit{Spencer Cos. v. Agency Rent-A-Car, Inc.}\textsuperscript{75} In \textit{Spencer}, the court held that the plaintiff, a corporation which was the target of a tender offer, stated a claim under RICO. The plaintiff alleged that the tender offeror misrepresented its purpose as one of investment in a situation where defendant’s actual intent was either to gain control of the plaintiff or force it to repurchase the shares at an inflated price. As a consequence of the court’s decision, potential RICO liability was expanded to include corporate executives and investment advisers.

Banks and other financial institutions, which have often vigorously assailed the use of RICO in actions naming them as defendants, have recently turned to the statute to obtain affirmative relief. In \textit{Crocker National Bank v. Rockwell International Corp.}\textsuperscript{76} a national bank coupled a RICO claim with allegations that Lehman Brothers Kuhn Loeb, Inc. (Lehman Brothers), an investment advisory firm, and others had violated federal and state securities laws. The litigation had its genesis in the widely publicized activities of the now bankrupt O.P.M. Leasing Services, Inc. (OPM).\textsuperscript{77} Plaintiff Crocker National Bank (Crocker) alleged that Lehman Brothers and the other defendants had violated the securities laws in connection with transactions by which “investment packages” relating to OPM leases were marketed.\textsuperscript{78}

Defendants sought dismissal of the RICO claims, contending that the national bank had failed to allege some nexus between defendants and organized crime or misconduct typical of organized crime.\textsuperscript{79} Denying the motion to dismiss, Judge Conti in \textit{Rockwell} relied on the legislative history of the statute in asserting that the scope of RICO was not limited to persons directly involved in organized crime.\textsuperscript{80} Judge Conti also rejected the defendants’ alternate proposed limitation on RICO—an asserted requirement that plaintiffs allege that defendants

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\textsuperscript{74} \textit{Hanna}, \textit{Fed. Sec. L. Rep.} (CCH) at 93,737.


\textsuperscript{76} 555 F. Supp. 47 (N.D. Cal. 1982).

\textsuperscript{77} \textit{Id.} at 48. O.P.M. Leasing Services leased computers to the defendant Rockwell International Corporation. In order to finance the acquisition of the equipment package to financial institutions through its investment banker, Lehman Brothers Kuhn Loeb, Inc.

\textsuperscript{78} \textit{Crocker}, 555 F. Supp. at 48.

\textsuperscript{79} \textit{Id.} at 49.

\textsuperscript{80} \textit{Id.}
\end{flushleft}
had engaged in activity typically associated with organized crime—as "unworkable . . . [since there is] no reasoned way to determine what activities are commonly associated with organized crime."\(^{81}\)

Judge Conti also found that Crocker had advanced all of the requisite allegations to support a racketeering claim against Lehman Brothers and the other defendants including accountants and lawyers.\(^{82}\) According to the *Rockwell* court, in language which is instructive on pleading techniques for any plaintiff framing a RICO complaint, Crocker sufficiently "allege[d] the existence of at lest one enterprise, the required acts of racketeering, and that [plaintiff] suffered damages as a proximate cause of defendants' activities."\(^{83}\)

VI. DEFENSES TO CIVIL RICO CLAIMS

A. Membership in Organized Crime, the "Enterprise" Concept and Prior Convictions

Beginning soon after the enactment of the statute, defendants confronting RICO claims in civil litigation have urged two closely related defenses in order to secure dismissal of the complaints. The first of the defenses is grounded on the contention that a plaintiff must plead and prove a connection between the defendant and organized crime; the second related concept is that a plaintiff must plead and prove that the defendants are engaged in an enterprise distinct from the alleged pattern of racketeering.

Both of these defenses—the alleged "organized crime" requirement and the "enterprise" concept—attracted considerable attention and approval from the courts in the first decade of RICO's existence. However, both defenses have sustained rapid and substantial damage in recent years, as more decisions have eschewed the limitations im-

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81. Id.
82. Id. The defendants included the law firm which had acted as legal counsel to O.P.M. Leasing Services in arranging the investment packages.
83. Id. Other courts have delineated the basic pleading requirements of a RICO claim. In *Lode v. Leonardo*, 557 F. Supp. 675, 681 (N.D. Ill. 1982), Judge Kocoras, in denying the application of two state-chartered banks to dismiss the RICO-based allegations of a complaint, said:

In the definition section of RICO, 18 U.S.C. § 1961, mail fraud is clearly listed as a "racketeering activity." Since the plaintiffs have alleged that at least two such acts of "racketeering activity" were committed by the defendants within a ten year period, they have unquestionably met the requirement for pleading the "pattern of racketeering activity" element of a RICO violation.

posed by the earlier cases. The doctrines, nevertheless, retain some vitality in those circuits, including the Sixth, Tenth, and Eleventh Circuits, which have not ruled on the issues. Moreover, the Supreme Court has never delineated the pleading requirements applicable to a civil action alleging RICO violations. Accordingly, until the final standards are established, it is reasonable to anticipate that the defenses will continue to be asserted in motions seeking dismissal of civil claims predicated on RICO.

One of the earliest and most frequently cited of the cases restrictively interpreting RICO's civil remedies was Barr v. WUI/TAS, Inc. 84 While vigorously criticized in decisions such as Norcen, 85 the opinion in Barr continues to serve as one of the starting points for defense contentions that RICO should not be extended as a remedy in cases involving traditional commercial, securities, and antitrust litigation.

The court in Barr refused to allow plaintiffs to amend their complaint against a telephone answering service to include a RICO claim predicated on the mailing of fraudulent statements, unless the plaintiffs showed the defendant's membership in a "society of criminals operating outside of the law." 86

In support of this highly restrictive position, the Barr court focuses on the "patently unfair" implication of a defendant's involvement in organized crime "that could raise from the mere granting of leave to file a [RICO] claim." While acknowledging that "the rather broad language of the Act appears to encompass the factual situation alleged [here]," the Barr decision characterized the RICO allegation as "spurious, frivolous and without merit" and relied on frequent references in the legislative history of the statute to "'racketeers,' 'organized crime' and 'organized crime families'" as the persons with whom RICO was concerned. 87

In part because of its vivid language and the vigor of its denunciation of the plaintiff's position, the decision in Barr at one time com-

85. See also Bennett v. Berg, 685 F.2d 1053 (8th Cir. 1982) (court rejected the Barr limitation of civil RICO liability to cases where ties to organized crime are alleged); Hunt Int'l Resources Corp. v. Binstein, 559 F. Supp. 601 (N.D. Tex. 1982) (RICO not limited to activities connected with "organized crime"); D'Iorio v. Adonizio, 554 F. Supp. 222 (M.D. Pa. 1982) (court rejects Barr, in that "'nexus' with organized crime is not required by criminal or civil RICO actions); Meineke Discount Muffler Shops, Inc. v. Noto, 548 F. Supp. 352 (E.D.N.Y. 1982); United States v. Gibson, 486 F. Supp. 1230 (S.D. Ohio 1980) (court stated in dictum, "We do not believe that the court in Barr correctly stated the law." Id. at 1241.).
86. Barr, 66 F.R.D. at 113.
87. Id. at 112-13.
Manded widespread attention from other courts. However, a defendant’s sole reliance on *Barr* is a serious tactical mistake because the basic position of *Barr*—that a plaintiff had to allege that the defendant was a member of “organized crime”—has since been substantially abandoned by the court which enunciated it. While not yet ruled on by the Supreme Court, *Barr* represents a position which has been abandoned by the Second Circuit and expressly rejected by the Seventh and Eighth Circuits. No definitive rulings have been made by other circuits, including the Sixth and the Tenth Circuits.\(^{88}\)

A decision which has been less vigorously attacked than *Barr* and thus could continue to provide a more tenable position for the RICO defendant is *Adair v. Hunt International Resources Corp.*\(^{89}\) In *Adair* the court dismissed a RICO claim brought on behalf of 1,300 individual

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Recently a federal court in New York placed one of the most restrictive interpretations on RICO in the statute’s thirteen year history only to have its reasoning expressly rejected by the Second Circuit shortly thereafter. In *Moss v. Morgan Stanley*, 553 F. Supp. 1347 (S.D.N.Y. 1983), *aff’d*, 719 F.2d 5 (2d Cir. 1983), the district court dismissed a RICO claim against an investment banking firm. The complaint alleged that the firm, in providing assistance to a tender offeror, permitted one of its employees to obtain access to confidential information regarding the tender offer. This information was later allegedly used by the employee and others to the detriment of the shareholders of the “target” company of the tender offer.

The district court, in granting the motion to dismiss, adhered closely to the “organized crime” requirement of *Barr*: “Unless a plaintiff can point to a factual basis for a charge that a defendant is a member of a structured criminal organization, civil litigation falls to the ground; indeed, such a charge infects the fundamental fairness of such litigation.” *Id.* at 1358. This was a class restatement of the *Barr* principle.

The Second Circuit affirmed the dismissal of the complaint but expressly rejected the reasoning of the district court. The court stated flatly that the “language of the statute . . . does not premise a RICO violation on proof or allegations of any connection with organized crime.” *Moss*, 719 F.2d at 21. Thus, according to *Moss*, this argument may not be interposed against a RICO claim. Similar results have been reached in the Seventh Circuit in *Cenco, Inc. v. Seidman & Seidman*, 686 F.2d 449 (7th Cir.), *cert. denied*, 103 S. Ct. 177 (1982), and in the Eighth Circuit in *Bennett v. Berg*, 685 F.2d 1053 (8th Cir. 1982). Among the circuits which have not ruled on the issue and in which the defense may maintain some vitality are the Sixth Circuit and the Tenth Circuit. *See, e.g.*, *Austin v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, Fed. Sec. L. Rep. (CCH) ¶ 99,510 (W.D. Mich. Sept. 13, 1983) and *In re Longhorn Sec. Litig.*, Fed. Sec. L. Rep. (CCH) ¶ 99,537 (W.D. Okla. July 28, 1983).

plaintiffs who were allegedly defrauded into purchasing worthless parcels of land in Colorado. The court acknowledged that "'[o]n first glance, plaintiffs' claims would seem to be authorized by the Act.'"90 The court then recited the fact that section 1964(c)

authorizes "'any person injured in his business or property by reason of a violation of § 1962' to sue for treble damages in district court. In turn, § 1962 makes it unlawful for any person to receive 'any income derived, directly or indirectly, from a pattern of racketeering activity ...'" And in § 1961, Congress defined "'racketeering activity' with broad strokes: it includes any act punishable under federal mail fraud statutes, or 'any offense involving fraud in the sale of securities.'"91

The Adair court attempted to qualify and circumscribe the statutory language with the assertion that "'it is 'a familiar rule, that a thing may be within the letter of the statute, and yet not within the statute, because not within its spirit, nor within the intention of its makers.'"92 The court in Adair concluded: "'An examination of [the legislative history and the purposes of the statute] indicates that [RICO] was not intended for the use proposed by plaintiffs—that of a federal common law fraud.'"93

A similar conclusion was reached in Waterman S.S. Corp. v. Avondale Shipyards, Inc.94 In strong language the court concluded that:

To give RICO the broad and unlimited application suggested by [plaintiff] would be to make a travesty of Congress' clear intent to the contrary. The civil remedies provisions of RICO were not designed to convert every fraud or misrepresentation action involving corporations who use the mails or telephones to conduct their business in interestate commerce into treble damages RICO actions.95

Closely related to the organized crime concept embodied in Barr,

90. Id.
91. Id.
95. Id. at 260. The court did acknowledge a split on the issue of the breadth of application of RICO to civil claims. Id. at 259.
Adair, Waterman S.S. Corp., and other decisions is the "enterprise" defense. Briefly described, this concept purports to require a plaintiff to allege and prove that defendants were engaged in an "enterprise" with an independent economic significance from the pattern of racketeering activity. More concretely, brokerage firms which are defendants in securities fraud actions have asserted that it is not enough, for RICO purposes, for a plaintiff to allege that employees of the brokerage firm engaged in a series of fraudulent transactions—in other words, the pattern of racketeering. According to the "enterprise" defense, association, or effort exists with an ascertainable structure independent of the alleged acts of racketeering.96

Expressly approved in some circuits but definitively rejected in others, the enterprise defense may continue to represent a significant defensive strategy in RICO litigation. In Bennett v. Berg, for example, the Eighth Circuit endorsed the approach that a plaintiff in a RICO action must "allege the existence of an enterprise distinct from the alleged pattern of racketeering."97 In stark contrast, the Second Circuit has expressly rejected the Eighth Circuit’s view in Bennett that "the evidence offered to prove the ‘enterprise’ and ‘pattern of racketeering’ must necessarily be distinct."98 According to the Second Circuit, particularly in cases where securities fraud is alleged, the same proof used to establish a pattern of racketeering activity will also operate to establish the "enterprise" element of a RICO claim. As characterized by the Second Circuit, the proof of a "pattern of racketeering" and "enterprise" frequently will "coalesce."99 Simply stated, no separate enterprise allegations are necessary in civil litigation involving RICO in the Second Circuit since the court has "upheld application of RICO to situations where the enterprise was, in effect, no more than the sum of the predicate racketeering acts."100

Recently, an additional and potentially significant line of defense has emerged, stemming at least in part from both the organized crime and "enterprise" concepts. In its recent decision in Tiane Co. v. O’Connor Securities,101 the Second Circuit, dismissing an appeal as moot, took the opportunity to declare that it was leaving to "another day" the

96. See, e.g., Bennett v. Berg, 685 F.2d 1053, 1060 (8th Cir. 1982); United States v. Anderson, 626 F.2d 1358, 1372 (8th Cir. 1980).
97. 685 F.2d at 1059-60.
98. Moss, 719 F.2d at 22.
99. Id.
101. 718 F.2d 26 (2d Cir. 1983).
"substantive RICO issue" of whether a plaintiff must plead and prove "for civil RICO purposes" that "there must have been securities law convictions . . . ." 102

To the extent that a requirement of proof of prior convictions is imposed, as suggested by the Second Circuit, this emerging defense would create obvious burdens in prosecuting a RICO claim and, in fact, would result in a drastic retraction of the scope of civil RICO actions predicated on securities law violations. This is a result of the fact that relatively few companies or individuals are convicted of securities violations as a result of indictment by federal or state authorities. In focusing attention on this new defense, the Second Circuit in Trane referred to the language of the statute which defines "racketeering activity" to include "any offense involving . . . fraud in the sale of securities . . . punishable under any law of the United States." 103

Significantly, the Second Circuit in Trane raised the possibility of a viable new defense in the same month that, in its decision in Moss v. Morgan Stanley, 104 the same court dealt significant damage to the "organized crime" and "enterprise" defenses.

B. Procedural Defenses to RICO Claims

Another judicially created approach to the restrictive application of RICO emphasizes procedural considerations, such as standing and pleading requirements. Some decisions, for example, have expressed reservations about extending RICO due to the possibility of creating a broad universe of new plaintiffs. In Landmark Savings & Loan v. Loeb Rhoades, Hornblower & Co., 105 the court observed:

If "organized crime" is as harmful to our society and economy as we have all been led to believe, then the number of potential plaintiffs who are not the direct victims of predicate crimes but who have treble damage claims because they have suffered racketeering enterprise injury to their business or property are limited only by imagination and the burden of proof. Does, for example, the State of Michigan have a treble damage action against an illegal gambling enterprise because of injury to its lottery business? Does a legitimate

102. Id. at 29.
103. Id.
business which loses a public bid because of a series of bribes by a competitor have a treble damage action under RICO?106

Similarly, several recent decisions have avoided reaching the RICO issues by finding that the racketeering allegations fail at the pleading stage. In Maryville Academy v. Loeb Rhoades & Co.,107 sixteen plaintiffs brought separate lawsuits against the investment banking firm Loeb Rhoades & Co., Inc. (Loeb Rhoades), alleging violations of the federal securities laws as a result of Loeb Rhoades’ alleged misrepresentations in inducing purchases of the securities of Olympia Brewing Company.

Invoking both RICO and Rule 10b-5, Loeb Rhoades counterclaimed against each of the plaintiffs. Loeb Rhoades asserted that plaintiffs’ conduct in filing the lawsuits was an attempt to “cover up” plaintiffs’ own alleged fraud, extending over a period of six years, in placing orders with Loeb Rhoades when plaintiffs had no intention of completing the purchases on the settlement dates, in secretly borrowing funds to purchase securities, and in “unlawfully forming a syndicate.”108 In its counterclaims Loeb Rhoades alleged that it sustained damage because of the costs of defending the plaintiffs’ suits, not as a result of the substantive violations alleged.

At the outset, the court in Maryville Academy dismissed the Loeb Rhoades’ counterclaims to the extent that they asserted liability under Rule 10b-5. The court found that the fraud claim was deficient because the conduct alleged was not “in connection with” the purchase or sale of a security. “[T]he cover-up—the filing of the suits—[was not] fraudulent conduct in connection with the purchase or sale of any securities,”109 the court concluded.

The RICO claims were also dismissed in the Maryville Academy decision which acknowledged the Seventh Circuit ruling that RICO “is not restricted to members of organized crime, but can be used to reach out for others if the statutory conditions are met.”110 Nonetheless, Judge Getzendanner did not reach the issue of the applicability of RICO to the securities transactions alleged by Loeb Rhoades. Instead, the Maryville Academy court found that the RICO counts fell along with the securities fraud claims as a technical pleading matter:

106. Id. at 209.
108. Id. at 1065.
109. Id.
110. Id. at 1069.
The court need not decide whether the RICO statute encompasses the securities violations alleged by Loeb Rhoades in its counterclaim, because the RICO count suffers from the same defect as the securities counts: failure to allege facts establishing causation. The RICO statute permits recovery of any injuries to business or property resulting from a pattern of racketeering activity . . . . The fraudulent conduct alleged did not result in any injury to Loeb Rhoades. The injuries Loeb Rhoades claims, the expense of litigation and damage to its reputation, did not arise "by reason of" the putative racketeering activity, the securities fraud, but resulted from the sixteen lawsuits filed against Loeb Rhoades. The court has determined that the filing of the lawsuits is not fraud in connection with a securities transaction; thus the filings are not within the scope of racketeering activity under the RICO statute.111

While they are frequently defendants in RICO claims, accountants have also affirmatively pursued racketeering charges in some cases against former clients. For example, the litigation, in Cenco, Inc. v. Seidman & Seidman,112 evolved from the "massive fraud" in which the management of Cenco, Inc. (Cenco) was allegedly engaged from 1970 to 1975. As described by the Seventh Circuit, "[t]he fraud began in Cenco's Medical/Health Division but eventually spread to the top management of Cenco."113 Notwithstanding the pervasiveness of the fraud, "Cenco's independent auditor throughout the period of the fraud, the accounting partnership of Seidman & Seidman, either never discovered the fraud or if it did failed to report it."114

The "unmasking" of the fraud led to the filing of a federal class action against Cenco, its managers, and Seidman & Seidman. The accounting firm contended that Cenco's corporate acquisitions with stock whose price had been inflated through violations of the federal securities laws violated RICO.

The Seventh Circuit sustained the district court's dismissal of the RICO claim, essentially on the ground that Seidman & Seidman lacked standing to maintain it. The circuit court correctly described the accounting firm as contending that it had been used as "a tool of the

111. Id. at 1069-70.
112. 686 F.2d 449 (7th Cir.), cert. denied, 103 S. Ct. 177 (1982).
113. Id. at 451.
114. Id.
criminal enterprise." The court asserted that the question of Congress’ intent to grant a treble damage remedy to a firm in the position of Seidman & Seidman was one of “first impression.”

In the absence of “useful legislative history,” the Cenco court concluded that a treble-damage action by auditors of publicly-held corporations against the corporations of their management would not “contribute to the compensatory and deterrent objectives of RICO.” While denying standing under RICO to auditors in suits against their clients, the Seventh Circuit was careful to distinguish the treatment of public investors, competitors, and customers who had suffered injuries as a result of corporate securities fraud:

This court has interpreted the RICO statute, in light of the long list of criminal offenses in section 1962, to forbid penetration of business enterprises by any “pattern of racketeering activity” embraced by that section, whether or not “organized crime” is involved. United States v. Aleman, 609 F.2d 298, 303-04 (7th Cir. 1979). What is critical here, rather, is that “the primary purpose of RICO is to cope with the infiltration of legitimate businesses.” United States v. Turkette, 101 S. Ct. 2524, 2533 (1981). It is presumably on behalf of the owners, perhaps also the customers and competitors, of such businesses that the civil damages remedy was created, and not on behalf of the people who supply office equipment or financial or legal services to criminal enterprises that may be violating RICO.

C. The “Competitive Injury” Standard

Another procedural restriction which the courts have imposed on RICO is described under the rubric of the “competitive injury” requirement. In North Barrington Development, Inc. v. Fanslow, the court ruled that RICO does not provide a damage remedy for the direct victims of the offenses on which the RICO violation is based. Instead, according to Fanslow, damages under RICO are available only to plaintiffs who allege “competitive injury” from the illegitimate advantage derived by the defendant in operating an enterprise through racketeering

115. Id. at 457.
116. Id.
117. Id.
118. Id.
activity. Concluding that the plaintiff in Fanslow had not sustained injury as a result of the conduct of a competitive enterprise dominated by racketeering activity, the court dismissed a RICO claim by a plaintiff who had allegedly been defrauded in a real estate transaction. A similar result was reached in Landmark Savings & Loan v. Loeb Rhoades, Hornblower & Co. The decision restricted the private right of action under RICO to plaintiffs who sustain “racketeering enterprise injury” and identified the “competitive injury” test as a standing requirement.

VI. Conclusion

The emerging use of RICO in corporate and commercial lawsuits involves some of the most unsettled and widely contested issues in contemporary civil litigation.

The assertion of a RICO claim adds a complex dimension to any lawsuit. When Congress enacted the statute, it was “well aware,” as the Supreme Court has noted, that it was significantly expanding the scope of liability. Taken in its totality, the legislative history reveals that Congress recognized that it was opening a broad and intentionally ill-defined scope of civil responsibility. Congress left the development of the specific nature of that liability to litigants and the courts.

The final contours of RICO, particularly in the area of civil liability, are not clear. On balance, the experience of thirteen years with the statute has evidenced a steady expansion of the civil remedy provision. The Supreme Court’s recent refusal to consider the civil litigation boundaries of RICO may well enhance this expansion in the coming months and years. In the absence of consistent judicial precedents, the assertion of a RICO claim inevitably presents a dynamic situation for plaintiffs, defendants, and the courts in which strategic choices are complex and results inherently unpredictable.

121. See supra note 56. But see supra notes 33-34 and accompanying text noting that the “competitive injury” requirement enunciated in Fanslow was categorically rejected in Hanna Mining Co. v. Norcen Energy Resources, Ltd., [1982 Transfer Binder] Fed. L. Sec. L. Rep. (CCH) ¶ 98,742 (N.D. Ohio 1982). The court in Norcen found that the purposes of the federal antitrust laws and RICO were “divergent,” although the RICO private remedy provision was conceptually modeled on treble damage recovery under the antitrust laws. Id. at 93,737.