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CLOSING THE RICO FLOODGATES IN THE AFTERMATH OF SEDIMA

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There is a new form of extortion sweeping the country. Business people of all types, and professionals such as accountants, bankers, insurance agents, and securities brokers are among its primary victims. They are being threatened with a weapon that can inflict huge damages and bring unjustified shame and ruin upon them. This new method of extortion can be more effective than brass knuckles, fire, or vandalism. Ironically, Congress inadvertently created it as part of a bill designed to help legitimate businesses defend themselves against organized crime. Instead, it has been turned against the very people Congress intended to aid. This weapon is the civil component of the Racketeer Influenced and Corrupt Organizations Act ("RICO").[1]

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1. 18 U.S.C.A. §§ 1961-1968 (West 1984 & Supp. 1985). Section 1962, Prohibited Activities, provides in part:

> (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 . . . .
>
> (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 subsections (a), (b), or (c) of this section.

Id. (footnote omitted).

Congressional reform of its provisions is urgently needed.

I. INTRODUCTION

In July 1985, a divided United States Supreme Court in *Sedima, S.P.R.L. v. Imrex Co.*[2] concluded that the civil remedy provisions of the Racketeer Influenced and Corrupt Organizations Act must be broadly construed. This decision has opened wide the gates of the federal courts to an expected tide of commercial fraud litigation and has greatly increased the exposure of legitimate business enterprises to liability. The Court's five-member majority believed that it could do no less, even though all nine Justices were of the view that RICO's civil remedy provisions were being employed for purposes wholly unintended by Congress.[3]

RICO was enacted by Congress in 1970, primarily for the purpose of arming federal law enforcement officials with a potent new weapon against organized criminal activity.[4] There is little quarrel that in the hands of government prosecutors, RICO has served as an effective instrument against criminal activity that, prior to the enactment of RICO, had evaded the reach of state and federal law enforcement.[5] Unfortunately, growing use by private plaintiffs of RICO's broad-based treble damage remedy for injuries resulting from activities punishable under the statute[6] holds the potential for significant abuse. With increasing frequency, private litigants in ordinary business disputes involving claims of commercial fraud or breach of contract are adding to

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2. 105 S. Ct. 3275 (1985).

3. *Id.* at 3302; *id.* at 3288 (Powell, J., dissenting); *id.* at 3293 (Marshall, J., dissenting).

4. RICO was enacted as Title IX of the Organized Crime Control Act of 1970, Pub. L. No. 91-452, tit. IX, § 901(a), 84 Stat. 941 (1970) (codified as amended at 18 U.S.C.A. §§ 1961-1968 (West 1984 & Supp. 1985)). The Senate Judiciary Committee, in which the Act (and the title embodying RICO) originated, made clear in the report accompanying the legislation that the bill's purpose was "the eradication of organized crime in the United States by strengthening the legal tools in the evidence-gathering process, by establishing new penal prohibitions, and by providing enhanced sanctions and new remedies to deal with the unlawful activities of those engaged in organized crime." S. REP. No. 617, 91st Cong., 1st Sess. 2 (1969).

5. For example, § 1962 makes it unlawful for any person to invest racketeering monies to establish, operate, maintain, or acquire an interest in an interstate enterprise. 18 U.S.C. § 1962(b) (1982). For an overview of the use of the RICO statute as a potent prosecutorial tool, see Tarlow, *RICO: The New Darling of the Prosecutor's Nursery*, 49 FORDHAM L. REV. 165 (1980-1981).

6. 18 U.S.C. § 1964(c), which provides:

> Any person injured in his business or property by reason of a violation of [the criminal prohibitions of RICO] 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.

Id.

their complaints a "RICO count" seeking treble damages.[7] The sweep of the statute is so broad that most litigation arising out of ordinary business disputes is based on facts that can reasonably be alleged to constitute a pattern of "racketeering activity" within the scope of RICO.[8]

Some federal courts, in an effort to stem the rising tide of RICO litigation, have attempted, through judicial construction, to constrict the ambit of the RICO treble damage remedy.[9] The majority of courts, however, have concluded that the statute does not tolerate such limiting construction.[10] When the issue finally reached the Supreme Court in *Sedima,* the Court acknowledged that "in its private civil version, RICO is evolving into something quite different from the original con-

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7. *See, e.g.,* Barker v. Underwriters at Lloyd's, London, 564 F. Supp. 352 (E.D. Mich. 1983) (alleging that insurers' and underwriters' activities in refusing to pay claims in an effort to force settlement for less than the amount entitled to, coupled with defendants' use of the United States Post Office, violated the RICO statute); American Soc'y of Contemporary Medicine v. Murray Communications, 547 F. Supp. 462 (N.D. Ill. 1982) (alleging breach of contract coupled with defendant's use of the United States Post Office violated the RICO statute).

8. This is largely due to the inclusion of wire, mail, and securities fraud within the definition of racketeering activity. 18 U.S.C.A. § 1961(1)(b), (d) (West 1984 & Supp. 1985). That definition otherwise encompasses a list of criminal activities associated with organized crime, such as murder, arson, kidnapping, extortion, embezzlement, and drug dealing. *See infra* notes 36-47 and accompanying text.

9. The decision of the Court of Appeals for the Second Circuit in *Sedima* construed the existing language of the statute to impose a prior criminal conviction requirement. Sedima, S.P.R.L. v. Imrex Co., 741 F.2d 482, 500-01 (2d Cir. 1984), *rev'd,* 105 S. Ct. 3275 (1985). For other decisions narrowing the statute's reach, see American Sav. Ass'n v. Sierra Fed. Sav. & Loan Ass'n, 586 F. Supp. 888 (D. Colo. 1984) (complaint dismissed for not alleging facts sufficient to connect defendant's activities with criminal activities of an organized nature); Harper v. New Japan Sec. Int'l, Inc., 545 F. Supp. 1002 (C.D. Cal. 1982) (amended complaint, construed liberally, did not allege an injury "by reason of" a violation of the RICO statute).

10. *See, e.g.,* Moss v. Morgan Stanley Inc., 719 F.2d 5, 21 (2d Cir. 1983) (citing legislative history and language of the statute, court rejected district court finding that a link to organized crime was an essential element to plead a RICO cause of action), *cert. denied,* 465 U.S. 1025 (1984); *see also* Sutliff, Inc. v. Donovan Cos., 727 F.2d 648, 654 (7th Cir. 1984) (holding that no connection to organized crime necessary to state a private cause of action under RICO because Congress intended to "cast the net of liability wide" in order to close loopholes that the "minions of organized crime" might crawl through); Alcorn County, Miss. v. United States Interstate Suppliers, 731 F.2d 1160, 1167 (5th Cir. 1984) (holding that it was error to dismiss a civil RICO complaint because plaintiff failed to allege an organized crime connection) (citing Owl Constr. Co. v. Ronald Adams Contractor, Inc., 727 F.2d 540 (5th Cir. 1984)); Alexander Grant & Co. v. Tiffany Indus., 742 F.2d 408, 413 (8th Cir. 1984) (holding that where plaintiff alleged that defendant's continued ability to stay in business was by use of mail and wire fraud, such allegations were sufficient to plead an injury "by reason of" a RICO violation); Schacht v. Brown, 711 F.2d 1343, 1351 (7th Cir.) (rejecting special injury requirement), *cert. denied,* 464 U.S. 1002 (1983).

ception of its enactors."[11] But the Court reasoned that this effect, however unintended, is embedded in the statute and its legislative history.[12] In short, the responsibility for reform of RICO's civil remedy was found to lie not with the courts, but with Congress.[13]

This article describes the history of the private civil RICO remedy, the misuse of that remedy, which has created the need for legislative reform, and the basis for this author's view that the most equitable and sensible means for redirecting the use of the civil remedy under RICO is to impose a requirement for prior criminal conviction before RICO's extraordinary remedies may be invoked.

II. THE ORIGINS OF CIVIL RICO

The enactment of RICO was the end result of extensive congressional inquiry into organized criminal activity.[14] A major focus of the inquiry was a well-founded concern that organized crime had begun to penetrate a wide range of legitimate businesses—from jukebox sales to securities firms.[15] While many of the means used by organized crime to infiltrate legitimate businesses, including murder, extortion, and arson, were already punishable under various federal and state laws,[16] Congress was convinced that many of those who benefitted directly could not be convicted of direct involvement with such criminal activity under then-existing law. For that reason, Congress created new criminal prohibitions aimed at punishing those who acquire interests in or control of business enterprises, or otherwise realize financial gain through "a pattern of racketeering activity."[17]

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11. 105 S. Ct. at 3287.

12. *Id.* at 3286.

13. *Id.* at 3287.

14. As noted by Senator McClellan, "[t]his action was the culmination of a year of detailed study, hearings, and consultations . . . ." 115 CONG. REC. 36,217 (1970).

15. *See, e.g., id.* (Senator McClellan notes: "In business, the mob bleeds a firm of assets, then takes bankruptcy. It steals securities and then uses the stolen securities to fraudulently obtain funds from lending institutions."); 116 CONG. REC. 591 (1970) (Congressman Poff outlines, in a hypothetical case, how organized crime can gain control over a jukebox company).

16. *See, e.g.,* 18 U.S.C. § 873 (1982). The statute states that "[w]hoever, under a threat of informing, or as consideration for not informing, against any violation of any law of the United States, demands or receives any money or other valuable thing, shall be fined . . . ." *Id.*; *see also, e.g.,* N.Y. PENAL LAW § 155.05(2)(e) (McKinney 1975) (defining larceny as including a wrongful taking, obtaining or withholding of another's property committed by, *inter alia*, extortion).

17. "Racketeering activity" includes an act chargeable under several generically described state criminal laws, including murder, kidnapping, gambling, arson, robbery, bribery, extortion, or dealing in narcotics or other dangerous drugs. 18 U.S.C.A. § 1961(1) (West 1984 & Supp. 1985). Racketeering also includes an extensive list of crimes indictable under various federal laws, including bribery, counterfeiting and embezzlement. Ad-

The criminal provisions of the RICO proposal were extensively debated.[18] By contrast, the civil RICO provision was not closely scrutinized.[19] The bill that passed the Senate did not contain a civil remedy.[20] During House consideration, the bill was amended to add a private remedy permitting any person who alleges and proves injury arising from a pattern of racketeering activity to recover treble damages and reasonable attorney's fees.[21] When the bill was returned to the Senate, the House-passed version was accepted without a conference and with sparse debate of the civil treble damages remedy. Indeed, Senator McClellan described the House amendments, including the addition of the civil treble damages provision, as relatively "minor changes."[22]

The legislative history of this amendment leaves no doubt that the private remedy under RICO was intended to be consistent with the general purpose of RICO: "to prevent and reverse the corrupt infiltration of legitimate commercial activities by ruthless organized criminal businesses."[23] The civil cause of action was designed to provide redress to those who suffer harm as a consequence of the infiltration of legiti-

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ditionally, racketeering activity includes mail fraud, wire fraud, and fraud in the sale of securities. *Id.*

18. *See, e.g.*, 116 CONG. REC. 607 (1970). Senator Byrd noted that Title IX criminal penalties "constitute a carefully structured program which can drastically curtail—and eventually eradicate—the vast expansion of organized crime's economic power." *Id.*

19. The Judiciary Committee's official report recommending passage of the Organized Crime Control Act limits its discussion of the private civil remedy to a single line. It merely states that § 1962(c) "provides for the recovery of treble damages by any person injured in his business or property by reason of the violation of section 1962." H.R. REP. No. 1549, 91st Cong., 2d Sess. 58, *reprinted in* 1970 U.S. CODE CONG. & AD. NEWS 4034.

20. Under the original Senate bill, § 1964 did define civil remedies; these definitions, however, were not directed toward aiding individuals injured by racketeering activities. Section 1964(a) stated that "[t]he 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 . . . ." 116 CONG. REC. 582 (1970).

21. Congressman Poff, in his remarks before the House, noted that "[a]t the suggestion of the gentleman from Arizona (Mr. Steiger) and also the American Bar Association and others, the committee has provided that private persons injured by reason of a violation of the title may recover treble damages in Federal Court." 116 CONG. REC. 35,295 (1970). The Committee's suggested amendment was incorporated into the House's final resolution. H.R. 1235, 91st Cong., 2d Sess., 116 CONG. REC. 35,364 (1970).

22. 116 CONG. REC. 36,293 (1970).

23. *Organized Crime Control: Hearings Before Subcomm. No. 5 of the Comm. on the Judiciary on S. 30 and Related Proposals Relating to the Control of Organized Crime in the United States*, 91st Cong., 2d Sess. 519 (1970). When the bill reached the floor, the civil treble damages provision garnered little debate, and was described by Chairman Emanuel Celler of the Judiciary Committee as "designated to inhibit the infiltration of legitimate business by organized crime." 116 CONG. REC. 35,196 (1970).

mate businesses by organized crime.[24] In the usual situation, such a victim is the competitor of an infiltrated organization. Tactics of harassment and intimidation are employed against the victim. Surveys of the development of civil RICO litigation, however, establish that the private civil RICO remedy has not provided redress for victims of organized crime to any meaningful extent.[25]

Perhaps the most comprehensive of such surveys is that undertaken by the American Bar Association's Ad Hoc Civil RICO Task Force. The Task Force reported that only nine percent of the hundreds of cases surveyed involved claims based on predicate offenses commonly associated with professional criminal activity.[26] By contrast, forty percent of the cases studied alleged securities fraud as the underlying predicate act, and an additional thirty-seven percent involved allegations of common-law fraud in a commercial setting.[27]

The rapidly increasing use of the civil RICO provision as a means to supplement and, quite effectively, "up the ante" in disputes over ordinary commercial and securities transactions is clearly invited by the broad language of the statute, specifically the inclusion of mail fraud, wire fraud, and fraud in the sale of securities on the list of predicate acts that constitute "racketeering" under the statute.[28]

Like RICO, federal mail fraud[29] and wire fraud statutes[30] are crea-

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24. H. REP. No. 1549, 91st Cong., 2d Sess. 58, *reprinted in* 1970 U.S. CODE CONG. & AD. NEWS 4007, 4034 (noting that § 1963(c) "provides for the recovery of treble damages by any person injured in his business or property by reason of the violation of section 1962").

25. *See, e.g.*, ABA SECTION OF CORP., BANKING & BUSINESS LAW, REPORT OF THE AD HOC CIVIL RICO TASK FORCE 56 (1985) (the report does not represent the official position of the American Bar Association or the Section of Corporation, Banking and Business Law) [hereinafter cited as RICO TASK FORCE REPORT] (of the 270 civil RICO cases decided, only nine percent have involved "allegations of criminal activity of a type generally associated with professional criminals").

26. *Id.* at 55-56.

27. *See id.*; *see also Sedima*, 105 S. Ct. at 3287 n.16. Both the majority and minority opinions acknowledged the statistical evidence demonstrating that civil RICO has been directed at a class of defendants engaged in ordinary business activity, rather than organized crime.

28. Interestingly, the original bill introduced by Senator McClellan did not include among RICO's "predicate acts" any reference to wire, mail, or securities fraud. However, based on concerns expressed by the Securities and Exchange Commission that organized crime figures were engaged in such activities as the sale of stolen or counterfeit securities, the list of predicate acts was expanded during Senate Committee consideration to include mail fraud, wire fraud, and "fraud in the sale of securities." *See* RICO TASK FORCE REPORT, *supra* note 25, at 99 n.130.

29. 18 U.S.C. § 1341 (1982). "Whoever, having devised . . . any scheme or artifice to defraud . . . [and] for the purpose of executing such a scheme or artifice . . . places in any post office or authorized depository for mail matter, any matter or thing whatever to be sent or delivered by the Post Office Department . . . shall be fined . . . ." *Id.*

30. 18 U.S.C. § 1343 (1982). "Whoever, having devised any scheme to defraud . . .

tures of congressional attempts to extend the reach of federal law enforcement into fraudulent activities that are not otherwise within the scope of state and federal criminal statutes or common law.[31] Federal courts have respected congressional intent and have been reluctant to circumscribe these criminal prohibitions with the precise standards and elements of proof that typically characterize the definition of other criminal offenses. In *United States v. Bohonus*,[32] for example, the Ninth Circuit stated that

> [t]he fraudulent nature of the "scheme or artifice to defraud" is measured by a non-technical standard . . . . Thus, schemes are condemned which are contrary to public policy or which fail to measure up to the "reflection of moral uprightness, of fundamental honesty, fair play and right dealing in the general and business life of members of society."[33]

Because there exist only these general guiding principles as to what constitutes a "scheme or artifice to defraud," almost every dispute over money invites the prospect of a RICO claim. The application of such broad readings to specific activities can raise significant questions, even in the hands of government officials who are restrained by conventions of prosecutorial discretion. No such limitations apply to private litigants.

Once a "scheme or artifice to defraud" is alleged, the only additional requirement imposed by the mail and wire fraud statutes is that the mails or the telephone must have been used in the commission of the fraud.[34] For purposes of making a RICO claim, two or more such jurisdictional acts—two telephone calls, two letters, or one of each concerning the same or different transactions—are sufficient to support an allegation that the actions constitute a "pattern of racketeering activ-

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cause to be transmitted by means of wire, radio or television communication . . . any writings, signs, pictures or sounds for the purpose of executing such scheme . . . shall be fined . . . ." *Id.*

31. This point was highlighted when, in 1970, § 1343 of Title 18 was amended. The purpose of the change was "to close a loophole in the present law, which limits the prosecution of frauds involving wire, radio, and television communication to interstate transactions only." 1956 U.S. CODE CONG. & AD. NEWS 3091, 3092.

32. 628 F.2d 1167, 1171 (9th Cir. 1980) (company president extorted kickbacks from insurers he utilized for his business).

33. *Id.* at 1171; *see* United States v. Dial, 757 F.2d 163, 170 (7th Cir. 1985) (courts "have been more concerned with making sure that no fraud escapes punishment than with drawing a bright line between fraudulent, and merely sharp, business practices"); United States v. Louderman, 576 F.2d 1383, 1388 (9th Cir. 1978) ("[T]he statute was not to be limited to the common law definition of false pretenses . . . . [but instead] 'includes a broad proscription for the purpose of protecting society.' ").

34. For the relevant portions of the mail and wire fraud statutes, see *supra* notes 29-30.

ity."[35] In view of the use of the mails and the telephone in virtually every business transaction, and the broad and unrestricted definitions of mail and wire fraud, the private right of action under RICO effectively encompasses the universe of commercial disputes.

Just as it is relatively simple to allege, if not to prove, claims of fraud in any commercial transaction involving contracts, the sale of securities, or other business transactions, it is now equally simple to allege a RICO claim. Any business dispute that reaches litigation is today a likely candidate for a RICO claim. In fact, RICO has been raised in litigation spawned by corporate takeover battles,[36] landlord-tenant controversies,[37] inheritance disputes,[38] and even matrimonial controversies.[39]

As a practical matter, RICO promises to have significant long-term effects on the conduct of commercial litigation at the federal level. It has opened the doors of the federal courtroom to litigation arising from commercial disputes that are traditionally the province of state courts.[40] The creation of a federal fraud remedy brings about a major alteration in the historic division of federal and state judicial purview. Congress did not, in enacting RICO, develop a record advancing the view that state tort and contract principles are inadequate to meet the needs of ordinary business disputes. In the absence of such a record, principles of federalism should constrain federal encroachment in these areas as a matter of public policy.[41] Moreover, even if one concludes

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35. *See* 18 U.S.C. § 1961(5) (1982). The statute states that a " 'pattern of racketeering activity' requires at least two acts of racketeering activity, one of which occurred after the effective date of this chapter and the last of which occurred within ten years (excluding any period of imprisonment) after the commission of a prior act of racketeering activity." *Id.*

36. Warner Communications, Inc. v. Murdoch, 581 F. Supp. 1482 (D. Del. 1984) (hostile takeover target unsuccessfully alleged that its corporate adversary violated § 1961(5) of RICO).

37. Pit Pros, Inc. v. Wolf, 554 F. Supp. 284 (N.D. Ill. 1983) (tenant alleged that prospective landlord falsely represented through the mails that property was properly zoned).

38. Maxwell v. Southwest Nat'l Bank, 593 F. Supp. 250 (D. Kan. 1984) (court upheld a complaint stating a claim under RICO that defendant bank had defrauded a decedent and her heirs out of their estate).

39. Erlbaum v. Erlbaum, [1982 Transfer Binder] FED. SEC. L. REP. (CCH) § 98,772 (E.D. Pa. 1982) (under civil RICO wife claimed ex-husband defrauded her of interest in jointly-owned stock).

40. *See, e.g.*, Alcorn County, Miss. v. United States Interstate Suppliers, 731 F.2d 1160 (5th Cir. 1984) (Alcorn County recovered payments made to company furnishing office supplies under state bidding laws and was able to seek award of treble damages under civil RICO); Bennett v. Berg, 710 F.2d 1361 (8th Cir.) (RICO claims upheld in action against retirement community for loss of "life care" as well as 11 pendant causes of action for common law fraud under state law), *cert. denied*, 464 U.S. 1008 (1983).

41. While some may argue that a federal general fraud remedy would enhance oppor-

that the public interest requires a general federal fraud remedy, it is highly unlikely that a Congress that chooses to federalize common law fraud would do so through a device such as the one embodied in RICO. In addition to the lack of clear standards defining "mail fraud" and "wire fraud," RICO itself is, by congressional design, somewhat short on specific statutory standards.[42]

Recognizing that a broad range of activity could be viewed as technically violative of the statute, the Criminal Division of the United States Justice Department in 1981 promulgated "guidelines" in an effort to limit the Department's use of the statute to cases that fall within the Act's purposes, as well as its literal language.[43] The guidelines make clear that "not every case in which technically the elements of a RICO violation exist, will result in the approval of a RICO charge."[44] As a result, the Justice Department will not "approve 'imaginative' prosecutions under RICO which are far afield from the Congressional purpose of the RICO statute."[45] As the guidelines recognize, "the activity which Congress most directly addressed—the infiltration of organized crime into the nation's economy," is the essential objec-

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tunities for plaintiff recovery, it is apparent that in most cases where civil RICO has been used other remedies also exist. *See, e.g.*, Wilkinson v. Paine, Webber, Jackson & Curtis, 585 F. Supp. 23 (N.D. Ga. 1983) (investor claiming misrepresentation of material fact in suit against brokerage firm was able to maintain causes of action under § 9(a) of the Securities Exchange Act, § 12(2) of the Securities Act of 1933, § 17(a) of the Securities Act as well as civil RICO claims); Kimmel v. Peterson, 565 F. Supp. 476 (E.D. Pa. 1983) (plaintiff securities purchaser brought action against various brokerage firms through a 34-page complaint containing 12 counts under federal securities regulation statutes, various pendant state claims as well as claims under civil RICO); Austin v. Merrill Lynch, Pierce, Fenner & Smith, 570 F. Supp. 667 (W.D. Mich. 1983) (court upheld investors' claim under RICO where the complaint contained 11 other sufficient counts under federal and state securities laws and several common law theories). Indeed, in most instances where the plaintiff alleges loss at the hand of a financial institution or a securities dealer, a federal cause of action and jurisdiction are available under, respectively, the Truth in Lending Act and the 1933 and 1934 Securities Acts. Truth in Lending Act, 15 U.S.C. § 1601 (1982); Securities Act of 1933, 15 U.S.C. §§ 77a-77aa (1982); Securities Exchange Act of 1934, 15 U.S.C. §§ 78a-78hh (1982). *See generally Hearings on H.R. 2943 Before the Subcomm. on Criminal Justice of the House Judiciary Comm.*, 99th Cong., 1st Sess. ____ (1985) (forthcoming 1986) (testimony of Public Citizens' Congress Watch Witnesses and accompanying discussion).

42. The RICO statute does not define mail fraud, wire fraud, or embezzlement; instead it refers the reader to the applicable sections of the United States Code. 18 U.S.C. § 1961 (1982).

43. UNITED STATES ATTORNEYS' MANUAL §§ 9-110.200 to -110.500 (Mar. 9, 1984). The Department of Justice gives a detailed outline of RICO's use in federal prosecutions. *Id.* The Manual has a broad scope, covering both the duties of the prosecutor involved in RICO litigation, *id.* § 9-110.211, and the anticipated defenses, *id.* § 9-110.409.

44. *Id.* § 9-110.200.

45. *Id.*

tive that guides the Department's use of RICO's criminal provisions.[46] Unfortunately, there is no device available to limit similarly the discretion of private litigants, who are now utilizing the statute to its fullest extent.

The result is that it is virtually impossible for ordinary businesspeople to anticipate the limits of acceptable business activity under RICO. Businesspeople are routinely called upon to make decisions concerning whether to assume the risk of failure to perform under contracts, to deny insurance claims, and to engage in other activity that may result in litigation under state contract or tort law. Civil RICO arbitrarily triples that risk, adds the possibility of the award of attorney's fees, and, unlike state fraud, contract, or tort law, provides little in the way of guidance to individuals and businesses in assessing the risk of exposure.

In the context of securities litigation, RICO produces other troublesome effects. As noted, the ABA Task Force data indicates that forty percent of RICO claims involve allegations of securities fraud.[47] The nation's securities markets are regulated under a carefully tailored system of statutes, regulations, and precedent, which governs in a systematic and relatively clear and predictable fashion, the conduct of securities business in the United States.[48] Through this evolution, the Congress, the Securities and Exchange Commission, and the courts have structured standards considered most appropriate for balancing the private and public rights and remedies available for resolution of disputes involving securities transactions. The availability of and limitations on private rights of action for resolution of disputes in securities transactions have been clearly defined by this process.[49] Congress

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46. *Id.*

47. RICO TASK FORCE REPORT, *supra* note 25, at 55.

48. In order to protect the securities investor, Congress has enacted statutes governing the sales of corporate securities and guaranteeing truthful disclosure. *See* Securities Act of 1933, 15 U.S.C. §§ 77a-77aa (1982) (governing investor information and proper representation of securities offered for public sale); Securities Exchange Act of 1934, 15 U.S.C. §§ 78a-78hh (1982) (requiring disclosure and corporate reporting of securities). The Securities and Exchange Commission is an independent, quasi-judicial agency of the federal government created by Congress to enforce federal securities laws. *Id.* Those areas not governed by federal statutes are often policed by state laws. For instance, the General Corporation Law of the State of Delaware, DEL. CODE ANN. tit. 8, §§ 101-398 (1979), specifies what will be considered sufficient legal consideration for stocks, *id.* § 153, and when additional stock may be issued, *id.* § 161.

49. Courts have held that an implied private right of action exists under rule 10b-5 of the Securities Exchange Act of 1934. Superintendent of Ins. v. Bankers Life & Gas Co., 404 U.S. 6 (1971); Kardon v. National Gypsum Co., 69 F. Supp. 512 (E.D. Pa. 1946) (first decision to hold that an implied cause of action was available under the 1934 Act). This private cause of action, however, has been specifically limited to actual purchasers and sellers of securities. Birnbaum v. Newport Steel Co., 193 F.2d 461 (2d Cir.), *cert. denied*, 343 U.S. 965 (1952). The "Birnbaum" rule was adopted by the Supreme Court as the

has taken no action to disturb these evolved standards. RICO, without any record basis or apparent thought on the part of its framers, exposes securities transactions to actions by a broad class of litigants specifically excluded under current law. In the words of Justice Thurgood Marshall, the availability of civil RICO as a remedy in securities cases "virtually eliminates decades of legislative and judicial development of private civil remedies under the federal securities laws."[50]

RICO is an inappropriate weapon in civil commercial disputes for another intangible but nevertheless very important reason. A civil action brought under RICO involves an allegation of racketeering. This is, in our society, an extraordinary opprobrium, connoting criminal, and frequently violent, actions. In reality, the overwhelming majority of RICO claims involve allegations of activity that would never be prosecuted as RICO violations under the Justice Department guidelines.[51]

As a consequence, RICO defendants bear the stigma of criminal allegation without the protection that would, under Justice Department guidelines, be afforded even to those who could be reasonably suspected of engaging in truly criminal activities. Many appearing before Congress in favor of RICO reform have argued that this stigma forces settlements of claims of doubtful merit and subjects legitimate businesses to damage to reputation and standing in the community vastly out of proportion to the action alleged to have occurred.[52]

Finally, it is apparent that left unchecked, civil RICO will flood the federal courts with cases that arise under state tort and contract law and that properly belong in state forums. Forty-three percent of all reported RICO decisions were handed down in 1984,[53] notwithstanding the fact that the statute has been available for about one-and-a-half decades. This statistic suggests that the plaintiffs' bar has only recently begun to utilize civil RICO in a broad range of commercial disputes, and that a geometric progression of the RICO caseload can be expected. The new awareness of civil RICO arising from the *Sedima*

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best means for limiting this judicially-created cause of action. Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 730 (1975).

50. 105 S. Ct. at 3295 (Marshall, J., dissenting).

51. The Justice Department specifies that RICO prosecutions are to be aimed at organized crime figures. UNITED STATES ATTORNEYS' MANUAL § 9-110.200 (Mar. 9, 1984). However, only nine percent of the civil RICO suits have contained allegations of this type of criminal activity. RICO TASK FORCE REPORT, *supra* note 25, at 56.

52. Judge Abner J. Mikva, of the United States Court of Appeals for the District of Columbia Circuit, testified that defendants in civil RICO suits are forced to "pay out for frivolous disputes under pain of having to defend against being labeled a 'racketeer.' " *Hearings on H.R. 2943 Before the Subcomm. on Criminal Justice of the House Judiciary Comm.*, 99th Cong., 1st Sess. ____ (1985) (forthcoming 1986) (statement of Judge Abner J. Mikva).

53. RICO TASK FORCE REPORT, *supra* note 25, at 53.

decision,[54] which renders the courts powerless to restrict the reach of the statute, as well as numerous professional seminars educating lawyers regarding its broad scope, will further exacerbate the problem.

III. The Amendment of Civil RICO

Congress currently has before it a number of proposals for amending RICO. In my view, two objectives should be met in structuring an appropriate revision to the civil provision of the statute. First, Congress should restore the original purpose of the remedy: protecting victims of organized criminal activity. Civil RICO should remain a viable remedy for private individuals and firms injured by racketeering activity. Second, it is important to preserve, without amendment, the criminal law enforcement mechanism, which has been used effectively by the Justice Department to combat organized crime during the past fifteen years.

Congress should amend the civil side of the statute to require that civil RICO only be available when the defendant has been convicted of racketeering activity or of a violation of RICO. Under this formulation, only a person who has been convicted, under state or federal law, of a predicate offense such as murder, arson, extortion, kidnapping, or other activities, or someone who has been convicted of a violation of RICO itself, would be an appropriate defendant for a civil RICO claim. This amendment would not affect the criminal side of RICO.

While no solution to this problem is perfect, there are a number of reasons why the prior criminal conviction requirement appears to be the most appropriate and equitable means for curing the problems created under the current civil RICO law. It is a direct and simple solution, that does not stray into provisions of the statute essential to the law enforcement task and that preserves the civil remedy for those who suffer loss from true racketeering activity.

Under a prior criminal conviction requirement, a person injured as a result of a proven violation of these statutes would be free to pursue financial redress through the treble damage provisions. Yet such a requirement would not in any manner disturb the criminal law enforcement mechanism established in RICO.[55] The Justice Department

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54. 105 S. Ct. at 3287. As the Court noted,

> [i]t is true that private civil actions under the statute are being brought almost solely against such defendants (respected businesses), rather than against the archetypal, intimidating mobster. Yet this defect—if defect it is—is inherent in the statute as written, and its correction must lie with Congress. It is not for the judiciary to eliminate the private action in situations where Congress has provided it . . . .

Id. (footnote omitted).

55. *See* 18 U.S.C.A. §§ 1961-1963 (1984 & West Supp. 1985). The civil RICO statute

would be able to reach all criminal activity now subject to its prosecutorial discretion. For that reason, the "prior criminal conviction" requirement is preferable to other solutions that would cure the problem with civil RICO by eliminating mail fraud, wire fraud, or securities fraud from the list of predicate acts, or that would restrict the definition of "pattern of racketeering." Both of these latter approaches would render the criminal side of the statute less effective than the current law.

IV. CONCLUSION

RICO's treble damage remedy has significantly altered the balance of plaintiffs' and defendants' interests in civil litigation. The Supreme Court's decision in *Sedima* eliminated any possibility that judicial interpretation would constrain the use of civil RICO in ordinary business disputes. As a result, one must expect that RICO claims will proliferate and that defendants will find themselves faced with the threat of punitive damages and the stigma of charges of racketeering. Quite properly, the Supreme Court has advised Congress that it must correct its own error.[56] The imposition of the "prior criminal conviction" requirement would appropriately narrow the scope of the civil RICO remedy to those plaintiffs who have suffered injury at the hands of organized criminals.

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provides that a defendant who has been convicted of a criminal offense is estopped from denying those allegations in any subsequent action brought by the United States. *Id.* § 1964(d).

56. *See supra* note 54.