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Authority to Bring Private Treble-Damage Suits under RICO Should be Reformed, Hearings on RICO, June 10, 1985

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THE AUTHORITY TO BRING PRIVATE TREBLE-DAMAGE SUITS UNDER "RICO" SHOULD BE REFORMED

This memorandum details some of the serious problems that have arisen with the authorization for private treble-damage suits under the Racketeer Influenced and Corrupt Organizations ("RICO") title of the Organized Crime Control Act of 1970, 18 U.S.C. § 1961 et seq. It explains why reform of those provisions is necessary now.

I. INTRODUCTION

With little discussion, Congress in 1970 added the provision for private civil suits to a bill that was primarily designed to give the Department of Justice new criminal enforcement tools to attack "the mob." The language of the statute was drafted broadly to give the Justice Department adequate latitude in prosecuting persistent offenders, even if they are not members of traditional criminal syndicates. Congress expected, however, that the Justice Department, in exercising its enforcement discretion, would be faithful to the expressed congressional purpose to direct the new criminal sanctions against "organized crime," as experienced prosecutors understand that term. The Justice Department, in fact, has adopted formal guidelines to avoid abusive or excessive use of the broad language of RICO, and has exercised discretion in selecting cases for prosecution under RICO.

The provision for private civil suits was added very late in the legislative process and was intended to have the same focus: protecting legitimate businesses from incursions

by professional criminals. However, Congress did not include any specific mechanism to confine private civil suits to cases involving the activities of "organized crime."

Private claimants invoking the broadly phrased statute have not shown any of the discipline exercised by the Justice Department in its selective use of this powerful new weapon. As a result, inventive private lawyers seeking treble damages are successfully arguing for the most sweeping interpretation of RICO's broad language and are attempting to apply RICO in contexts far removed from those conceived by the statute's supporters. RICO claims are now added as a matter of course in virtually all cases challenging securities transactions or alleging some type of commercial fraud. RICO also crops up in landlord-tenant and real estate disputes, attorney-client conflicts, and even divorce battles. By contrast, only a tiny handful of the hundreds of cases alleging private civil claims under RICO involve either the people or the conduct that supporters of the bill sought to attack.

Without any of the restraint and responsibility that governs the decisions of public prosecutors, private lawyers are invoking civil RICO on behalf of private clients to level charges of "racketeering" against reputable businessmen and professionals such as investment bankers, brokers, and accountants. Although RICO was intended to protect legitimate business, the statute is now primarily being used to attack established businesses and firms. The threat to bring a

"racketeering" charge sometimes coerces settlements before the filing of a RICO complaint, while the actual filing of a RICO complaint exposes businessmen to continuing embarrassment and expense.

Some judges have attempted to restrict the uses of the civil RICO provision to the kinds of case that Congress contemplated. Most appellate courts, however, have rejected these limitations, explaining that they feel obliged to apply the sweeping phrasing of the statute as it is written. Several appellate courts have explicitly stated that relief from the overly broad coverage of RICO must come from Congress.

II. THE STRUCTURE OF THE STATUTE PERMITS OVERLY BROAD USE

The private civil RICO statute is 18 U.S.C. § 1964(c). Under that provision, a person may file a civil RICO action if he claims to have been "injured in his business or property by reason of" the defendant's "pattern of racketeering activity." The plaintiff may recover treble damages as well as costs and attorney's fees. The private civil claim under RICO involves three components.

A. The Predicate Offenses: "Racketeering Activity"

Because Congress doubted that it could adequately define "organized crime" in a criminal statute, it chose instead to focus on the types of conduct in which organized crime figures engage. The key to RICO coverage is an extensive list of "predicate" offenses that are defined as constituting

"racketeering activity." 18 U.S.C. § 1961. These include a variety of violent crimes, such as murder, kidnapping, extortion, and arson -- crimes that one normally associates with organized crime. In addition, because of some indications that organized crime was involved in trafficking in stolen or counterfeit securities and similar kinds of activity, the list of predicate offenses was expanded to include mail fraud, wire fraud, and "fraud in the sale of securities."

B. A "Pattern" of Racketeering Activity

The commission of any two predicate acts within a ten year period is defined to be a "pattern" of racketeering activity. The initial step in a plaintiff's civil RICO claim is to assert that a "person" -- including the whole spectrum of legitimate business corporations, associations, partnerships, and their executives -- committed two predicate acts within ten years and thus engaged in a "pattern of racketeering activity."

Unfortunately, this sweeping coverage makes virtually any businessman or business organization a potential target of a RICO claim. Since the two predicate offenses need not be separated in time or involve different transactions, a single commercial transaction that generates a dispute can be alleged to constitute a "pattern of racketeering." For example, an investor may allege simply that a securities transaction consisting of two steps involved fraud. This allegation would make out a "pattern of racketeering activity" involving "fraud

in the sale of securities" and would allow the claimant to circumvent various procedural and substantive limitations on damage suits under the securities laws. Similarly, a would-be RICO plaintiff may assert that two separate copies of a financial statement, bill, contract, advertisement or other document involved in a "fraudulent" transaction were sent through the mails. An accusation of this type effectively creates a private civil claim for "mail fraud," which before RICO had never been the basis for a civil suit under federal law. See, e.g., Ryan v. Ohio Edison Co., 611 F.2d 1170, 1177-79 (6th Cir. 1980).

C. The "Enterprise" Requirement

RICO also requires that the person commit the predicate acts in a particular relationship to an "enterprise." Under the statute, it is unlawful to obtain any interest in an "enterprise" through a pattern of racketeering activity, or to control an enterprise through such activity, or to conduct the affairs of an enterprise through racketeering activity. 18 U.S.C. § 1962. Depending on the facts, a plaintiff can easily satisfy the "enterprise" requirement in actions against legitimate businesses or businessmen by alleging that, for example, the defendant corporation or professional partnership is the "enterprise" that is conducting its affairs improperly.

III. THE LEGISLATIVE DEVELOPMENT OF CIVIL "RICO" SHOWS A PURPOSE TO PROTECT LEGITIMATE BUSINESSES

The bill that became the 1970 Organized Crime Control Act, including the RICO title, originated in the Senate. The Senate report stated unambiguously the objective of the legislation:

> "[T]he 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) (emphasis added).

In this vein, Senator McClellan, the bill's chief sponsor and a longtime foe of organized crime, focused his arguments for the bill on the insidious activities of "La Cosa Nostra." 116 Cong. Rec. 585-86 (1970). In particular, his sponsorship reflected awareness that, when "organized crime moves into a business, it usually brings to that venture all the techniques of violence and intimidation which it used in its illegal businesses." 115 Cong. Rec. 5874 (1969).

The Senate RICO bill contained no provision for civil suits when introduced or when initially passed by the Senate. The possibility of providing a private civil remedy had surfaced as part of other bills. The purpose of those proposals was, just as with RICO itself, to protect legitimate businessmen who are victimized by the infiltration of their businesses by organized crime or are subjected to unfair competition from

mob-controlled businesses. Drawing on the language and concepts used in the treble-damage section of the Clayton Antitrust Act, the civil remedy proposed in those bills reflected the intent:

> "[T]o apply the antitrust or civil features of our law to the invasion of legitimate businesses by members of the organized crime community." Measures Relating to Organized Crime: Hearings before the Subcommittee on Criminal Laws and Procedures of the Senate Committee on the Judiciary on S. 30, etc., 91st Cong., 1st Sess. 150 (1969) (statement of Senator Hruska on S. 1623 and S. 1861).

The Senate wanted to provide a mechanism to respond to reports that "organized crime has begun to penetrate" some legitimate businesses, such as securities firms from which it was stealing securities. See S. Rep. No. 617, supra, at 77; 116 Cong. Rec. 591 (1970) (remarks of Sen. McClellan).

The House shared this concern about the infiltration of organized crime into businesses across the nation. Thus, Congressman Poff, a leading proponent of the legislation, pointed to the takeover of a jukebox business by "a mafia boss" as an illustration of the general understanding that RICO was meant to protect legitimate business people injured by organized crime. 116 Cong. Rec. 6709 (1970).

A private civil remedy finally was added to the RICO legislation in the House Judiciary Committee at the urging of Representative Steiger, who submitted the draft of the language that ultimately became law. In submitting the amendment, Representative Steiger explained that his proposal

was designed to add a private remedy to help in the fight "to deal with organized crime." Organized Crime Control: Hearings Before Subcommittee No. 5 of the Committee 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). He carefully emphasized his understanding that RICO was designed "to prevent and reverse the corrupt infiltration of legitimate commercial activities by ruthless organized criminals." Id. at 519. So as to leave no room to doubt that he expected that the new statute, including his civil damage remedy, would be directed against "ruthless, organized criminals," Representative Steiger described examples of penetration of legitimate businesses by various "families" of "La Cosa Nostra" -- the Mafia. Id. In the sparse debate on the civil damage provision when the bill reached the House floor, the Chairman of the House Judiciary Committee, Representative Celler, explained that the addition of a treble-damage remedy was to be one of the tools "designed to inhibit the infiltration of legitimate business by organized crime." 116 Cong. Rec. 35,196 (1970).

The Senate accepted the House version of the bill, including the new provision for private civil suits, without any suggestion that the focus of congressional concern -- protection of legitimate businessmen -- had been shifted in the slightest. Indeed, Senator McClellan described the House amendments, including the addition of the civil provision, as

relatively minor changes. 116 Cong. Rec. 36,292-96 (1970). At no time did anyone ever suggest that the private civil remedy was intended for use against legitimate business people, corporations, or partnerships of licensed professionals, or was to be used in commercial disputes having nothing whatever to do with the activities of the people who were and are commonly recognized as "organized crime."

IV. THE USE OF THE PRIVATE CIVIL DAMAGE PROVISION HAS ACTUALLY UNDERMINED THE CONGRESSIONAL OBJECTIVE

In light of the unambiguous congressional focus, civil RICO actions should closely parallel criminal prosecutions and should attack similar kinds of conduct. Instead, almost none of the uses of the civil remedy has involved organized crime figures or the kinds of offense committed by organized crime figures.

Rather, civil RICO is used almost exclusively in commercial disputes. The statute is now being invoked in every kind of litigation where the predicate offense of "fraud" can possibly be alleged. Virtually all of these claims are either covered by specific federal regulatory laws such as the securities laws or do not belong in the federal courts at all. In the vast majority of cases, civil RICO claims are being used as weapons against the very people Congress was seeking to protect: legitimate business people. Not only have these developments distorted congressional expectations, but they also present widely recognized and increasing opportunities for abuse.

A. The Ability Of A Private Lawyer To Charge A Person With Criminal "Racketeering" Is Easily Abused

RICO is unprecedented in authorizing private lawyers who are representing purely private clients to invoke the judicial process by charging another private person with crimes. Under RICO, the private lawyer exercises power that normally is reserved to public officials and grand jurors: the power to lodge a formal accusation of crime. Those public officials and grand jurors, of course, have a duty of fairness and restraint in deciding whether to make that kind of accusation. As the Supreme Court once described the special responsibilities of prosecutors:

> "The United States Attorney is the representative not of an ordinary party to a controversy, but of a sovereignty whose obligation to govern impartially is as compelling as its obligation to govern at all; and whose interest, therefore, in a criminal prosecution is not that it shall win a case, but that justice shall be done. As such, he is in a peculiar and very definite sense the servant of the law, the twofold aim of which is that guilt shall not escape or innocence suffer." Berger v. United States, 295 U.S. 86, 88 (1935).

A private lawyer, by contrast, owes allegiance to his client's private interest, not to a higher sense of justice. His interest is not in impartiality, but in partisan advocacy. He is his client's servant, not the servant of the law. His client's interest is not that "justice" be done, but that he obtain money from the defendant.

Because of these fundamental differences, our system surrounds the exercise of prosecutorial power with many legal

and ethical restrictions. The officials who exercise prosecutorial discretion are accountable to the public for their judgments. As a further shield against overzealousness, the Constitution interposes grand jurors who, like the prosecutor himself, are sworn to secrecy while the prosecutor is attempting to demonstrate that there is substantial evidence to justify a proposed criminal charge. None of these restrictions, however, applies to a private lawyer who is considering filing a civil lawsuit in order to promote his client's financial interests.

As construed by most courts, RICO effectively licenses private parties to go into federal courts to level formal and explicit charges that other citizens have engaged in serious federal and state crimes and, by allegedly doing so, have made themselves "racketeers." The private claimant's power to brand a businessman or firm a "racketeer" may cause almost as much irreversible injury to the legitimate businessman as may an unwarranted criminal charge. Business rivals may use this power to gain economic advantage without actually having to go beyond the threat to file a civil RICO suit. The people who are monitoring the actual use of civil RICO know that this is the reality, not mere speculation. Ironically, civil RICO thus creates an opportunity to engage in a form of extortion, even though the criminal features of the statute are geared to prevent similar exactions.

In creating the civil remedy as a virtual afterthought, Congress failed to give any real attention to the

enormous power being delegated to private lawyers and clients. Nor did it consider how to safeguard this power or to protect the innocent against abuse. This basic flaw in the design of civil RICO created great potential for costly and damaging misuse. As discussed below, experience in recent years has shown that this regrettable potential has become the reality.

B. Civil RICO Suits Are Directed Mostly At Well Established Businesses, Not Organized Crime

The American Bar Association's special RICO Task Force recently collected comprehensive data about 118 private civil RICO cases, almost all of which were reported in the last three years.[1/] Only one civil case involved a kind of violent offense traditionally associated with organized crime: arson. One other alleged a usurious loan, one alleged extortion and four alleged bribery or commercial bribery. In dramatic contrast, 93 involved simply some form of alleged business "fraud", more than half of which were described as dealing with "securities fraud" and "tender offer" disputes; the balance were mainly "commercial fraud" cases and three were "antitrust" cases. Without question, this pattern has little to do with the perceived need for a new private civil remedy to attack organized crime.

[1/] See "The RICO Questionnaire Results", remarks by John K. Tabor before ABA Committee on Federal Regulation of Securities, RICO Program, April 6, 1984 (hereafter "ABA RICO Task Force Report".)

Another recently completed private survey located 132 civil RICO cases in which opinions have been published. According to the descriptions of allegations contained in those cases, they fall into the following categories:

Securities transactions	57
Commercial and contract disputes	38
Commodities trading	6
Bank loans	6
Antitrust price fixing	3
Religious disputes	2
Divorce	1
Union affairs	3
Commercial bribery/kickbacks	2
Political corruption (including official extortion and bribery)	9
Theft (by cleaners from apartment dwellers)	1
Violent crimes (murder, arson, extortion)	3

Thus, cases that could fairly be characterized as having anything to do with aiding the war on organized crime are a tiny minority.

Congress did not express any expectation that the prospect of treble damages would induce citizens injured by organized crime to come forward to supplement the resources of federal and local law enforcement officers by bringing suit against offenders whom the prosecutors had not charged. If there had been any such assumption, it would have proven to

be illusory. Apparently, the only three civil RICO cases involving allegations of gangster-like conduct -- murder, arson and extortion -- were tag-along cases filed after the authorities had obtained criminal convictions. See Anderson v. Janovich, 543 F. Supp. 1124 (W.D. Wash. 1982) (tavern owner claimed that convicted competitors tried to control local tavern business through threats of murder and arson); State Farm Fire and Casualty Co. v. Estate of Caton, 540 F. Supp. 673 (N.D. Ind. 1982) (insurance company sought to recover fraudulently obtained proceeds after convictions in arson-for-hire case); City of Milwaukee v. Hansen, No. 77-C-246 (E.D. Wis. January 13, 1981) (city sought to recover costs incurred in fighting fires started by convicted arsonists). In addition, nine other civil RICO cases also followed criminal convictions, generally for some form of political corruption.

In most civil RICO cases, however, the public authorities have not found a basis to proceed with any criminal charges. There has been, therefore, no careful screening by publicly accountable officials before those defendants have been charged with criminal "racketeering." This is not surprising, because public officials would not have considered it fair or accurate to brand the defendants in these cases "racketeers." Indeed, one commentator who maintains a computerized database of all published civil RICO decisions (which he calculates as consisting of 40% alleged securities fraud cases and 40% other kinds of alleged commercial fraud) concluded

that, "realistically speaking, the likelihood of state or federal prosecutors seeking indictments in the vast majority of these types of cases is as close to zero as anything could be." Weissman, "Circuit Aims To Curb Private Civil RICO Actions", Legal Times, August 20, 1984, at 12. Thus, these civil cases are not supplementing the enforcement efforts of prosecutors who simply lack the resources to deal with all the offenses deserving prosecution. Instead, these cases involve, with rare exceptions, disputes that no responsible prosecutor would brand as criminal, much less as the manifestations of "organized crime" or "racketeering."

Congress added the civil treble-damage provision to RICO in the expectation that this fearsome new weapon would be directed at the forces of organized crime. The members of Congress who voted for RICO would surely be startled to learn that RICO is actually being used almost entirely against the very people who were intended to be its beneficiaries: legitimate business people. Although not limited to those in the financial community and in related professional services, the burden has become especially severe for these people because they are viewed as vulnerable "deep pockets" whenever an investment or a commercial transaction goes sour. As the New York Times reported, despite the expectation that civil RICO would focus on "mobster deals," "legitimate businesses such as Morgan Stanley, American Express, E.F. Hutton and Lloyd's of London found their names smeared with racketeering charges. . . ." N.Y. Times, September 4, 1984, at D2. A partial roster of

defendants in civil RICO suits includes the following established and respected entities that private claimants have charged with a "pattern of racketeering":

Investment bankers and brokers

Bache Halsey Stuart Shields, Inc.
Bear Stearns & Co.
Merrill Lynch, Pierce Fenner & Smith, Inc.
Morgan Stanley & Co., Inc.
Oppenheimer & Co.
Paine Webber Jackson & Curtis, Inc.
Shearson/American Express, Inc.

National Accounting Firms

Alexander Grant & Company
Arthur Andersen & Co.
Coopers & Lybrand
Laventhol & Horwath
Price Waterhouse

Banks

Citibank, N.A.
Continental Illinois National Bank & Trust Co.
First Interstate Bank of Oregon
First National Bank of Atlanta
First National Bank of Maryland
Ford City (Illinois) Bank & Trust Co.
Hunter Savings Association
Marine National Bank (Wisconsin)
National Republic Bank of Chicago
Pacific Western Bank
Sierra Federal Savings & Loan Association
State Bank of India

Insurance Companies

Prudential Insurance Co. of America
Underwriters at Lloyd's, London
USLIFE Corp.

These firms have been named as defendants in dozens of RICO suits, even though the Justice Department has not seen merit enough even to file a criminal charge against them, much less to obtain a conviction. Of course, the enormous expenses

associated with defending against unchecked civil RICO claims become a cost of doing business that ultimately taxes the consumers of the goods and services provided by these firms and by their customers and clients.

C. Civil RICO Is Used Most Extensively In Ordinary Commercial Disputes

As the figures demonstrate, the vast bulk of private civil RICO cases have come in commercial contexts -- hardly in the settings that Congress (or the Department of Justice) thought needed bold new weapons and special incentives to sue. These cases fit within the language of RICO because the commercial activities allegedly involved "mail fraud," "wire fraud," or "fraud in the sale of securities."

The most extensive use of civil RICO at present is in actions involving securities trading and other commercial transactions. All three recent comprehensive surveys of reported decisions under RICO have ascertained that at least 80% of RICO claims appear in cases that involve sales of securities or commodities or relate to contract disputes or other ordinary commercial transactions. The cases reveal that RICO is being applied to federalize simple common-law fraud, or to add the threat of treble damages to cases already governed by federal securities laws. That latter use allows a plaintiff to circumvent the carefully crafted limitations on the remedies provided by the securities laws. See, e.g., Ernst & Ernst v. Hochfelder, 425 U.S. 185, 195, 206-211 (1976). In neither category of case, of course, is there any impact on "organized crime."

Claims based on "mail fraud" and "wire fraud" predicate offenses are easy to plead in many commercial disputes. They are also likely to survive motions to dismiss made at early stages. This is so because the underlying law in this area has been developed in criminal prosecutions under broadly worded criminal statutes. Courts have been willing to allow public officials to use broad prosecutorial discretion in determining which transactions are properly prosecutable:

> "The crime of mail fraud is [broad] in scope. The fraudulent aspect of the scheme to 'defraud' is measured by a non-technical standard. Law puts its imprimatur on the accepted moral standards and condemns conduct which fails to match the 'reflection of moral uprightness, of fundamental honesty, fair play and right dealing in the general and business life of members of society.' This is indeed broad." Blachly v. United States, 380 F.2d 665, 671 (5th Cir. 1967) (citations omitted).

In almost any instance where a venture has lost money, or a stock has fallen in value, a disappointed investor can allege that the businessman's behavior was not a "reflection of moral uprightness" and "fair play." Although Congress has never authorized private civil suits under the mail fraud statute, the inclusion of that offense as one of the predicates for a civil suit under RICO has now given this vast discretion to private claimants.

This system presents direct risks to the enforcement discretion of the Department of Justice. As we discuss in more detail below, various trial and appellate courts have been searching for some way to protect against the abusive use

of civil RICO. One way to do that would be to begin to narrow the kind of conduct that constitutes "mail fraud." The emergence of civil precedents that narrow the scope of RICO's predicate offenses would deprive the Department of its traditional discretion, not because federal prosecutors are distorting the mail fraud statute but because private lawyers and claimants are.

Similarly, private plaintiffs find it easy to level allegations of "securities fraud." Since the federal courts are reluctant to dismiss complaints before a plaintiff has had a chance to pursue substantial discovery in a search for evidence to support his allegations of "fraud," these cases withstand initial challenges. Even if the predicate offense that a plaintiff must ultimately prove in a civil RICO case is criminal securities fraud, a plaintiff may not even have to allege -- much less prove -- a deliberate intent to defraud him. For example, in United States v. Natelli, 527 F.2d 311 (2d Cir. 1975), cert. denied, 425 U.S. 934 (1976), the court upheld the conviction of a partner in a major accounting firm. On the basis of a finding that he had "recklessly" conducted a corporate audit, he was convicted of assisting in the corporation's filing of a false proxy statement in violation of 15 U.S.C. § 78ff(a). The trial judge in sentencing the accountant indicated that no finding of actual knowledge of falsity was necessary for conviction:

> "I think you are absolutely sincere when you say that you do not believe that you did anything wrong in this audit or audits. . . . But the tragedy is that the jury found that this was an audit or audits done with reckless disregard for what was really involved." United States v. Natelli, 74 Cr. 43 (S.D.N.Y.), Transcript of sentencing at 12.

Thus, a plaintiff may be able to assert a viable RICO claim based on alleged "fraud in the sale of securities" simply by claiming that the defendants were reckless in their actions, and that, as a result, a "fraudulent" filing or similar securities law violation occurred. This, in turn, permits the private claimant to brand the defendant a racketeer.

All its sponsors expressly agreed that RICO was aimed at preventing the infiltration of legitimate business by organized crime. The draftsmen certainly did not intend, for example, to have RICO become a device for challenging corporate takeover bids or to add a new level of regulation of those hotly contested deals. Yet, according to the ABA RICO Task Force Report, there have been at least six reported "tender offer" cases in which RICO claims were asserted by at least one of the contestants for corporate control. In Dan River, Inc. v. Ichan, 701 F.2d 278 (4th Cir. 1983), the court of appeals recently expressed concern about attempts to use RICO to block a takeover bid through a public tender offer, pointing out that this is simply one illustration of the unintended and excessive use of civil RICO:

> "Finally, we note the mounting controversy in the federal courts over the proper limits, if any, upon the use of RICO in cases far removed from

> the context which Congress had in mind when it enacted the statute. Congress was out to attack the problem of organized crime, not the problem of corporate control and risk arbitrage. We of course make no attempt to resolve the dispute here and now. We do not propose to enter the fray. We only note that the reach of RICO is itself a troubling issue. . ." Id. at 291.

See also, Tyson & August, The Williams Act After RICO: Has The Balance Tipped In Favor Of Incumbent Management?, 35 Hastings L.J. 53, 111-12 (1983) ("By giving target management a powerful new weapon in the takeover battle, the judicial approval of RICO suits predicated on Williams Act violations undermines the careful policy of evenhandedness that the Williams Act Congress sought so hard to attain".)

The treble-damage weapon of RICO and the "racketeering" label are also being used to challenge the ways banks set up their loan procedures and terms. For instance, in Morosani v. First National Bank of Atlanta, 703 F.2d 1220 (11th Cir. 1983), the 11th Circuit has allowed a case to proceed on the claim that the "prime rate" used in computing the interest on the plaintiff's loan was not the bank's true prime rate. In Lode v. Leonardo, 557 F. Supp. 675, 681 (N.D. Ill. 1982), the court explained why it, too, had to entertain a RICO suit involving alleged misrepresentations relating to a commerical loan:

> "Congress may not have envisioned that the civil remedies it supplied in RICO would find the widespread use that they have in commercial fraud cases. And such use of RICO's remedies may well be somewhat undesirable. But, when a plaintiff makes allegations which appear to state a claim under the statute as it is written, it is not the

> function of this Court to reject that claim on the ground that Congress must have meant something other than what it said in the statute."

This thoroughly unanticipated use of civil RICO has lead several sections of the American Bar Association to establish "yet another group to study RICO litigation . . . primarily in response to the prime rate RICO cases now about six-months-old. . . ." BNA, Securities Reg. & Law Rep. 1393 (Aug. 17, 1984).

RICO counts have already appeared in many other cases involving disputed commercial transactions, including churning of stock,[2] representations about a broker's expertise,[3] projections used in real estate syndication,[4] disputes between landlord and tenant,[5] disallowance of insurance claims,[6] alleged overcharges by a printer,[7] and failure to publish a medical journal according to a contractual agreement.[8]

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[2] See, e.g., Harper v. New Japan Securities International, Inc., 545 F. Supp. 1002 (C.D. Cal 1982).

[3] See, e.g., Noland v. Gurley, 566 F. Supp. 210 (D. Colo. 1983).

[4] Gordon v. Terry, 684 F.2d 736 (11th Cir. 1982), cert. denied, 103 S. Ct. 1188 (1983).

[5] Pit Pros, Inc. v. Wolf, 554 F. Supp. 284 (N.D. Ill. 1983).

[6] Barker v. Underwriters at Lloyd's, London, 564 F. Supp. 352 (E.D. Mich. 1983).

[7] Estee Lauder, Inc. v. Harco Graphics, Inc., 558 F. Supp. 83 (S.D.N.Y. 1983).

[8] American Society of Contemporary Medicine, Surgery & Opthalmology v. Murray Communications, Inc., 547 F. Supp. 462 (N.D. Ill. 1982).

Because Congress included open-ended "fraud" predicates, there is ample room for transforming even more commercial disputes into RICO cases.

It should be of special concern to the Department of Justice that the mail fraud and wire fraud predicates are so broad that at least one federal court has held that those predicates support a civil RICO claim for damages against FBI agents who orchestrated an undercover "sting" operation. Lightner v. Tremont Auto Auction, (N.D. Ill.), RICO Litigation Reporter 317 (September 1984). It is hard to imagine a more glaring illustration of the point that civil RICO is now being used against the very people it was designed to aid.

Although the "fraud" predicates are the easiest to abuse by artful pleading, they are not alone. In one of the most recent appellate decisions, the Fourth Circuit ordered reinstatement of a civil RICO case brought by a condominium developer who alleged that the purchasers of an office condominium unit were trying to "extort" an unreasonably high price from him in connection with the developer's effort to repurchase the condo unit in order to include it in a block of units the developer wanted to sell to IBM. Although the district court found that this was "at best a garden-variety commercial breach of contract" case, the Fourth Circuit concluded that the allegations might make out a claim of "extortion" under state law and, therefore, the plaintiff could press the case under RICO. Battlefield Builders, Inc. v. Swango, (4th Cir. No. 83-1797) (opinion filed September 20,

1984). The two businessmen who originally bought the condominium unit -- and their wives as co-defendants -- now stand accused of being racketeers and must defend themselves against a statute that Congress believed would protect business people from, in Representative Steiger's words, "ruthless organized criminals."

D. Most Courts Have Disclaimed Responsibility For Reforming Civil RICO's Overbreadth.

Several trial judges have attempted to restrain the use of civil RICO in ordinary commercial disputes. They have, for example, tried to treat the statute as requiring an allegation of some actual connection with "organized crime." E.g., American Savings Ass'n v. Sierra Federal Savings & Loan Ass'n, No. 83-JM-1889 (D. Colo. June 7, 1984); Richardson v. Shearson/American Express Co., 573 F. Supp. 133, 137 (S.D.N.Y. 1983); Noland v. Gurley, 566 F. Supp. 210 (D. Colo. 1983).

Other trial courts also have tried to give some sensible limit to the scope of RICO by requiring a showing of some special "racketeering injuries." For example, Alton v. Alton, 82 Civ. 0795 (S.D.N.Y. July 9, 1982), involved a RICO claim prompted by a dispute over division of property in a divorce suit. While the judge acknowledged that the plaintiff's complaint "may perhaps fit within the literal language of the statute," he dismissed the RICO claim, because:

> "[t]his action concerns a matrimonial dispute with claims of fraudulent inducement of a separation agreement and fraudulent acts in the administration of that agreement during the course of which the mails and telephone wires were used. To extend the treble damage provision of Section 1964 of the criminal statute to marital disputes setting forth individual claims of common law fraud, would

> produce a result not in conformity with the intent of the drafters of the statute. To allow such a remedy in this action would, in effect, establish a federal law of fraud, a treble damage remedy for any two instances of fraudulent conduct where the mails or wires are used." Id. at 8-9.

Several other recent RICO cases illustrate the full range of the distortion to which the present language of the civil RICO provision lends itself and the difficulties the courts are having in applying the statute sensibly. In at least two instances RICO has been invoked in religious squabbles, and the trial judges have struggled to make RICO inapplicable. In Van Schaick v. Church of Scientology, Inc., 535 F. Supp. 1125 (D. Mass. 1982), the district court was faced with a claim brought by a disaffected former adherent of the Scientologists alleging fraudulent misrepresentations. In dismissing the RICO counts the court stated:

> "We do not believe Congress intended § 1964(c) to afford a remedy to every consumer who could trace purchase of a product to a violation of § 1962. . . . Such an interpretation would open the federal courts to frequent RICO treble damage claims by federalizing much consumer protection law and by inviting plaintiffs to append RICO claims for consumer fraud to nonfederal claims thereby achieving treble damage recovery and a federal forum. . . . Absent a clear statement that Congress intended such a result, we believe courts should confine § 1964(c) to business loss from racketeering injuries." Id. at 1137.

The RICO claim in Congregation Beth Yitzhok v. Briskman, 566 F. Supp. 555 (E.D.N.Y. 1983), turned on a dispute about the proper succession to the "Skolyer Rebbe", a Chassidic Jewish leadership position. The plaintiffs invoked "mail fraud" and other predicate offenses based on alleged

misrepresentations by the defendants about their right to administer the congregation. In considering the propriety of a RICO claim, the court pointed to the lack of an alleged link to organized crime:

> "a line must be drawn somewhere, lest every garden variety dispute become a matter of federal concern. . . . No matter how expansive a view of RICO jurisdiction one is inclined to take, this case should fall beyond the pale. After all, it must be recalled that the statute was designed to 'rid the American economy and the channels of interstate commerce from the influences of organized crime' (citations omitted)." Id. at 557.9/

The recent trend in the courts of appeals, however, has been to disapprove all of these judicial efforts to reform RICO. For example, after the Beth Yitzhok decision the Second Circuit specifically rejected the limiting principle proposed there, the absence of an alleged link to "organized crime." Noting that the language of the statute is very broad, the Second Circuit stated that the courts may not insert what Congress failed to include: some specific language that would limit RICO's application to persons or offenses involved in organized crime. See Moss v. Morgan Stanley Inc., 719 F.2d 5, 21 (2d Cir. 1983), cert. denied, 104 S. Ct. 1280 (1984). The Seventh Circuit, too, has ruled in another commercial case that the statute does not require the plaintiff to show that the defendant has any connection with "organized crime". Sutliff, Inc. v. Donovan Cos., 727 F.2d 648, 654 (7th Cir.

9/ The ultimate dismissal of the claim was based on a finding that the religious issues raised were non-justiciable, 566 F. Supp. at 558.

1984). The other circuits that have addressed this issue have similarly rebuffed efforts by trial judges to confine the expansive statutory language of civil RICO within sensible limits that would direct it at the evil -- and the evil-doers -- Congress had in mind. See, e.g., Alcorn County v. U.S. Interstate Supplies, Inc., 731 F.2d 1160 (5th Cir. 1984) (rejecting requirement of link to organized crime); Owl Construction Co., v. Ronald Adams Contractor, Inc., 727 F.2d 540 (5th Cir. 1984) (same); Bennett v. Berg, 685 F.2d 1053, 1058-59 (8th Cir. 1982), modified en banc, 710 F.2d 1361, cert. denied, 104 S. Ct. 527 (1983) (reinstating RICO claims against insurance company and others based on alleged mismanagement of retirement community); Morosani v. First Nat'l. Bank of Atlanta, supra, (reinstating RICO claims against banks based on allegedly excessive interest rates charged to certain customers).

For the most part, other attempts at judicial solution of the problem also have been unavailing. In another massive RICO case, for example, Schacht v. Brown, 711 F.2d 1343 (7th Cir.), cert. denied, 104 S. Ct. 508, 509 (1983), the State Insurance Commissioner is alleging that an insurance company fraudulently under-estimated the necessary "loss reserves" that it should have maintained. The suit is being pressed under RICO on the ground that the use of the mails to circulate the company's financial statements constituted numerous separate acts of mail fraud. The defendants include three national accounting firms as well as the former officers and directors of the insurance company. In allowing the

action to proceed, the court of appeals expressed its concern about RICO's "vast impact upon the federal-state division of substantive responsibility for redressing" allegedly illegal conduct. 711 F.2d 1353. Nevertheless, the court rejected arguments that RICO should apply only where the defendants caused some "competitive injury" to the plaintiff; the court held that the courts are simply "without authority to restrict the application of the statute." Id. The Eighth Circuit has rejected restrictions based either on "competitive injury" or "racketeering injury." See Alexander Grant & Co. v. Tiffany Industries, Inc., (8th Cir. No. 83-1608) (opinion filed August 20, 1984) (RICO suit by accounting firm against its audit client); Bennett v. Berg, 685 F.2d 1053, 1059 (8th Cir. 1982), aff'd in part, rev'd in part, 710 F.2d 1361 (en banc), cert. denied, 104 S. Ct. 527 (1983).

Quite recently, a bitterly divided Second Circuit released a series of decisions in which three panels disagreed over the gloss that the courts may place on the terms of civil RICO. One panel decided by 2-1 vote (with one retired judge in the majority) that a private civil RICO case requires allegation and proof of both (1) criminal conviction under RICO or on the predicate offenses and (2) injury from the "racketeering enterprise" distinct from injury flowing from the predicate acts. Sedima, S.P.R.L. v. Imrex Co., (2d Cir. No. 83-7965) (opinion filed July 25, 1984). A second panel, also by 2-1 vote, decided to apply a requirement of a "distinct RICO injury" without also addressing the "prior conviction" issue.

Bankers Trust Co. v. Rhoades, (2d Cir. No. 83-7636) (opinion filed July 26, 1984). A third panel, however, rejected all of the approaches adopted by the two prior panels but was nevertheless bound to apply them in the absence of en banc reconsideration. Furman v. Cirrito, (2d Cir. No. 84-7113) (opinion filed July 27, 1984).

Even within the Second Circuit it is difficult to discern the status of civil RICO cases, but the disarray promises more years of confused litigation. The approach endorsed by the panel in Furman more accurately reflects the attitude of appellate courts in other circuits: "We think that any restrictions of RICO along the lines urged by defendants must come from Congress, not the judiciary." Slip op. at 5656. Moreover, since that recent trilogy, two other circuits have reinstated civil RICO complaints, declining to apply the limitations fashioned by two panels in the Second Circuit. Alexander Grant & Co. v. Tiffany Industries, Inc., supra; Butterfield Builders, Inc. v. Swango, supra.

E. Civil RICO Claims Against Legitimate Businesses Are Burgeoning

It is likely that, in light of the judicial unwillingness or inability to correct the overbreadth of the statute, RICO suits simply alleging securities fraud, commercial fraud, or other "imaginative" claims will continue to grow. The situation is already out of hand and destined to get worse.

Relatively few private RICO cases have progressed all the way to judgment, because intensive use of the statute

in civil cases only began to blossom a few years ago. The ABA RICO Task Force Report found that, although the statute was enacted in 1970, there was at most one reported opinion in a civil RICO case in each year up through 1979. In 1980, there were opinions in three civil RICO cases. The number grew to 22 in 1981, to 25 in 1982 and to 58 in 1983.

Of course, published decisions are only the tip of the iceberg. Lawyers and businessmen have reported that the mere threat to file a RICO suit has led to handsome settlements; this use of RICO never shows up in judicial statistics or in reported judicial decisions. Moreover, many complaints are doubtless at a procedural stage well before any rulings that would appear in published opinions. It is reasonable to infer, therefore, that several hundred formal RICO claims have been filed in the last few years. Virtually all of them accuse well-established and generally respected business people; few, if any, take on the affiliates of organized crime. And the numbers are increasing steadily and substantially.

The invocation of RICO against legitimate businesses in kinds of dispute never contemplated by Congress when it passed RICO is almost certain to accelerate. The decisions by four courts of appeals (the Fifth, Seventh, Eighth, and Eleventh Circuits), which have reluctantly adopted a broad, literal reading of the statute's sweep, all appeared in the last year and a half. Civil RICO claims are, therefore, far more likely to survive, and hence to be utilized, than they were even 18 months or two years ago.

In addition, there is rapidly spreading publicity about the utility of RICO as a device for getting a local commercial dispute into federal court or as a tactic for dramatically increasing the stakes in a case otherwise covered by the traditional single-damage feature of other, specific federal laws, such as the securities laws. Legal and business journals are filled with articles discussing the statute. See, e.g., Skinner and Tone, "Recent Developments in RICO Litigation", National Law Journal, February 13, 1984, at 20; Skinner and Tone, "Civil RICO and the Corporate Defendant", National Law Journal, January 30, 1984, at 22; Flaherty, "Private RICO Damages Awarded", National Law Journal, December 26, 1983 at 8; Sylvester, "Civil RICO's New Punch", National Law Journal, February 7, 1983 at 1; Weissmann, "'Moss' Makes RICO Statute the Darling of Plaintiffs' Bar", Legal Times, December 19, 1983 at 24; Murphy, "RICO -- A Federal Treble Damage Fraud Statute?", New York State Bar Journal, July 1983 at 18; "Business is Picking Up An Anticrime Weapon", Business Week, February 20, 1984, at 85.

So too, law reviews are focusing a great deal of attention on the statute, debating the extent of its flaws and the proper methods of correcting them. See, e.g., Tyson & August, The Williams Act After RICO: Has The Balance Tipped In Favor Of Incumbent Management, 35 Hastings L.J. 53 (1983); Note, RICO and Securities Fraud: A Workable Limitation, 83 Colum. L. Rev. 1513 (1983); Note, Civil RICO: The Temptation and Impropriety of Judicial Restriction, 95 Harv. L. Rev. 1101

(1982); Campbell, Civil RICO Actions in Commercial Litigation, 36 Southwestern L.J. 925 (1982).

Numerous how-to-do-it courses are being offered nationwide to acquaint lawyers with RICO's possibilities. For example, the ABA already has held three "continuing legal education" National Institutes on RICO, two in New York City in September 1983 and February 1984, and one in Los Angeles in November 1983. With ominous accuracy the ABA has titled these sessions "RICO: The Ultimate Weapon in Business and Commercial Litigation." The popularity of the presentations is great; the mailing for the February 1984 course pointed out that the two earlier meetings were sold out, with over 600 lawyers in attendance. One of the programs held at the ABA's annual convention in August 1984 was entitled "RICO: The Current Status of Baby Huey." The ABA is planning to hold another National Institute on RICO in New York in October 1984 entitled "RICO - The Second Stage." Among the featured topics are discussions of RICO and its impact on states and municipalities, RICO suits by and against unions, and RICO suits against financial institutions.

The Practicing Law Institute ("PLI") also held RICO sessions in June of this year both in New York City and in San Francisco, with topics including the use of RICO in "antitrust cases", "commercial bribery and faithless employee cases," "unfair competition cases," "securities and commodities cases," and "corporate takeover cases." In addition, Law & Business, Inc., offered RICO programs in Chicago in June and in San

Francisco in July. The volume of RICO litigation is expected to be so heavy that a special reporting service called the "RICO Litigation Reporter" began regular publication in May 1984 with a first issue containing over 200 pages of articles and reports on RICO decisions.

This almost frantic preoccupation with RICO as the "ultimate weapon" in commercial litigation reflects the view that, in light of the actual, even if unintended, scope of civil RICO:

> "a plaintiff's attorney zealously protecting the rights of his client, as he is charged to do, is obligated to bring RICO claims where they can reasonably be interposed." Brodsky, "RICO", New York Law Journal, February 15, 1984, at p. 1, Col. 1.

The bonanza for lawyers in RICO cases is widely and candidly recognized. Indeed, when the Los Angeles Times recently did a series of articles on "the litigation explosion," it devoted a front page article just to private civil RICO suits, entitling the feature, "'RICO' Running Amok in the Board Rooms", and subtitling the piece, "Law aimed at Mafia becomes popular in private suits." Siegel, Los Angeles Times, February 15, 1984. The article quoted one RICO lawyer as explaining that when he recently set up his private law practice he "was looking for a way to develop business," and he "studied RICO and saw the potential for lots of civil litigation."

Thus, it is unrealistic to expect that private lawyers selecting claims that may "appropriately" be brought

under RICO will show the kind of restraint and discipline manifested by the Justice Department. As long as the statute remains worded as broadly as the courts have viewed it, lawyers will have every incentive to continue pushing its use to the outer limits of the statutory language.

As the Los Angeles Times article accurately reported, the "most general response by trial judges to these suits has been dismay," but, as discussed above, most appellate courts have said that the judiciary must take the law as written and apply it. The dismay of trial judges is understandable, since these circuit holdings do more than legitimize creative lawyering, they allow cases to proceed that are attempting to shift hundreds of millions or billions of dollars. In Schacht v. Brown, supra, for example, the plaintiff demands more than one hundred million dollars in actual damages from the accounting firms and insurance company officials who are defendants. Complaint at ¶ 81. With trebling, the claim is for over 300 million dollars. So too in Bennett v. Berg, supra, the plaintiffs are seeking several million dollars even before trebling. Thus, the total sums claimed in all RICO cases represent an effort to redistribute huge amounts. The drag on the economy from all these contingent liabilities must be substantial.

Of course, in addition to multiple damages the plaintiffs in these actions seek attorneys fees. While there are few civil RICO cases that have progressed far enough to have reached the fee-determination stage, the amounts at issue

are substantial.[10/] Awards of hundreds of thousands or even millions of dollars are not uncommon under other statutes that contain similar "fee shifting" provisions. The prospect of such handsome awards is a powerful stimulus to press RICO to even newer frontiers.

Furthermore, at least two decisions hold that state courts also may entertain RICO claims. See, Greenview Trading Co., Inc., v. Hershman & Leicher, P.C., 24999-83 (N.Y. Sup. Ct., New York County), printed in New York Law Journal, March 13, 1984 at 5; and LaVay Corp. v. First National Bank of Maryland, 83-1020 (Md. Cir. Ct., Prince George's County, March 5, 1984) [both discussed in "Two States Lay Claim to RICO", National Law Journal, May 7, 1984 at 3]. Thus, even in a circuit where the federal courts have tried to place some limits on civil RICO, a plaintiff may simply bring a RICO complaint in the state courts. A state tribunal is not bound by the interpretation given RICO by the lower federal courts. See United States ex rel. Lawrence v. Woods, 432 F.2d 1072, 1075-76 (7th Cir. 1970), cert. denied, 402 U.S. 483 (1971); Seatec International, Ltd. v. Secretary of the Treasury, 525 F. Supp. 980, 982 (D.P.R. 1982). Hence, forum shopping will

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[10/] For example, in Schacht v. Brown, supra, the lead counsel for the plaintiff Insurance Commissioner reported billings of $363,737.00 through September of 1982. "Insurance Liquidations a Legal Bonanza", Chicago Tribune, September 12, 1982, § 5 at 1. This may include expenses for some items in addition to the Schacht litigation itself, but the vast majority is almost certainly for that civil RICO action, in a period before any significant discovery had commenced.

almost certainly occur, and plaintiffs will attempt to convince state courts to adopt the broadest possible construction of RICO. This involvement of state courts simply adds another level of expense and confusion for legitimate businesses facing RICO suits and undermines any hope that litigation and judicial rulings are a practical route to solving the problems with RICO.

V. REFORM OF CIVIL "RICO" SHOULD REFLECT THE JUSTICE DEPARTMENT'S CAREFUL SCREENING PROCESS

A. The Administration, The Courts, And Others Have Recognized The Need For Reform

The explosion of unjustified civil RICO cases is already at hand, and the adverse effects of this development on the courts and on legitimate business are direct, palpable, and unwarranted. It would be difficult to overstate the in terrorem effect of civil RICO on legitimate businesses, even though relatively few companies, so far, actually have been ordered to pay treble damages in these cases. As Business Week reported:

> "Lawyers say the number of court awards under RICO is not an accurate measure of the problem, because few cases go to trial: The mere threat of a headline suggesting a connection with organized crime often induces a settlement." February 20, 1984 at 85.

In addition, the scope of the permissible allegations permits wide-ranging pre-trial discovery: "That gets very, very expensive," one securities lawyer was quoted as explaining, "and the cost tends to result in settlements." Id.

In urging reform, the American Bar Association has recognized:

> "When RICO is combined with mail fraud predicate offenses, the effect is to federalize all torts involving business transactions in which a party thinks deceitfully and uses the mails. This result is undesirable in two respects: (1) the efficient operation of federal courts will be significantly impaired, if not crippled, by a tidal wave of RICO civil actions when plaintiffs become aware of the attractions of treble damages and recovery of attorney's fees; and (2) the balance between state and federal power will be substantially disrupted. If future RICO statutes are to include civil remedies, use of mail fraud as a predicate offense must be limited." Reports with Recommendations to the House of Delegates, ABA, 1982 Annual Meeting, August 1982, Report No. 112C at 8, adopted by the House of Delegates August 1982.

According to the recent ABA RICO Task Force Report, fully 74% of all lawyers with actual experience with RICO claims, either as counsel for plaintiffs or for defendants, believe that the statute should be amended, and only 8% see no need for reform.

From his unique vantage point as a regulator of securities industry and the accounting profession, SEC Commissioner Charles L. Marinaccio recently expressed his view that civil RICO has "gone awry in the execution," is being used against "the very legitimate corporations and businesses that were intended to be protected," to undermine the "carefully crafted structures" of express and implied remedies under state and federal securities laws. See BNA, Daily Report for Executives A-6 (September 21, 1984). As a result the SEC Commissioner concluded:

> "In my judgment, Congress needs to revisit the RICO statute. It should specifically make clear in

> the statute that before a civil claim may be filed under RICO the predicate of a criminal charge by the government is a necessity. It should further make clear that a 'racketeering' type injury needs to be shown. That is, that more than injury arising from the individual violations need be shown. What should be required is an injury which results from a pattern of racketeering to the competitive position of the enterprise alleging the harm. Perhaps the Supreme Court will do the job. But I believe it is the responsibility of the Congress to take RICO off its head and stand it on its feet."

Federal judges, acting in their capacity as commentators on what they are witnessing, also have spoken out in public about the problem. Thus, District Judge Milton Pollack of New York recently said:

> "one of the proliferating developments in civil litigation has been the use of RICO, the Racketeer Influenced and [Corrupt] Organizations Act, in civil claims, in routine commercial disputes, including those arising under the Federal Securities Laws. I think that the proliferation of those claims and the use of a law that was designed to eliminate organized crime is a very bad influence on the commercial community". "Symposium Highlighting Developments in Securities Law Over Past Century," New York Law Journal, January 30, 1984 at 52.

And Judge Abner Mikva of the United States Court of Appeals in Washington, who had warned against the overbreadth of the proposed RICO bill when he was in Congress in 1970, has seen RICO outstrip his worst fears. He warned then that placing a treble-damage remedy under so broadly worded a statute would provide an "invitation" to the "disgruntled and malicious" to "harass innocent businessmen. . ." H. R. Rep. No. 1549, 91st Cong., 2d Sess., reprinted in 1970 U.S. Code Cong. & Ad. News 4007, 4083. As he predicted, "What a protracted, expensive trial may not succeed in doing, the adverse

publicity may well accomplish -- destruction of the rival's business." Judge Mikva was quoted in a recent interview as expressing regret that these problems were not avoided by complete deletion of the civil provision, which "was not an important element of the legislation." Los Angeles Times, February 15, 1984.

In their formal opinions as well, many courts have warned about these dangers and abuses, even while deciding that they are obliged to apply the expansive language of the statute as originally written. For example, in allowing a mail fraud allegation to proceed as a RICO case, the Seventh Circuit in Schacht ruefully observed that Congress inadvertently "may well have created a runaway treble damage bonanza for the already excessively litigious." Schacht v. Brown, supra, 711 F.2d at 1361.

In another Seventh Circuit case, the court observed that RICO "is constructed on the model of a treasure hunt," Sutliff, Inc. v. Donovan Companies, Inc., 727 F.2d 648, 652 (7th Cir. 1984), and went out of its way to comment:

> "[w]e must abide by Congress's decision, made at a time of less sensitivity than today to the workload pressures on the federal courts and to the desirability of maintaining a reasonable balance between state and federal courts, however much we may regret not only the burdens that the decision has cast on the federal courts but also the displacement of state tort law into the federal courts that it has brought about." Id. at 654.

There is a consensus in the appellate courts that it is up to Congress, not the courts, to remedy the undesirable effects of the way RICO was originally drafted:

> "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 combating organized crime." Schacht v. Brown, supra, 711 F.2d at 1361.
>
> "[W]e are cautioned by the Supreme Court that broad Congressional action should not be restricted by the courts in the name of federalism. . . . It is beyond our authority to restrict the reach of the statute." Bennett v. Berg, supra, 685 F.2d at 1064 (panel opinion).
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> "Complaints that RICO may effectively federalize common law fraud and erode recent restrictions on claims for securities fraud are better addressed to Congress than to courts." Moss v. Morgan Stanley Inc., supra, 719 F.2d at 21.

In the words of former District Court Judge Simon Rifkind:

> "I have a feeling about RICO in the civil world, not in the criminal side, as being the most conspicuous case I know of legislation requiring Congressional attention for revision." "Symposium Highlighting Developments in Securities Law Over Past Century," New York Law Journal, January 30, 1984 at 52.

The Administration has heard these calls for reform and has decided that they are well founded. The Vice President's Task Group on Regulation of Financial Services, whose members include the Attorney General, recognized in its final report adopted on July 2, 1984, that civil RICO is being abused. The Task Group found that

> "a statute designed to control organized crime through both criminal and civil penalties against racketeering . . . has increasingly been utilized by imaginative lawyers in suits against banks, securities firms, accountants and other perfectly legitimate businesses without even any alleged connection to organized crime."

The Report continued:

> "This litigation increases the backlog in federal courts, undermines the structure of the substantive banking and securities laws enacted by Congress, and creates totally unnecessary costs for the affected firms and, ultimately, their customers."

Accordingly, one of the Task Group's recommendations (number 5.15) calls for "Elimination of Nuisance Litigation Under RICO." Without defining precisely how RICO should be amended, the Task Group states as a goal the formulation of amendments "to ensure that its civil liability provisions are not misused by private parties in litigation involving financial institutions."

B. The Justice Department's RICO Guidelines Point The Way To Reform

In 1981, the Criminal Division of the United States Department of Justice promulgated "Guidelines" for the exercise of the Department's power to initiate criminal prosecutions under RICO. See 9 United States Attorney's Manual, Ch. 110 (1981). The Guidelines were promulgated because the Department recognized the great possibility for abuse if RICO is applied to every set of circumstances that may conceivably be covered by the broad statutory language.

Many of the concerns reflected in the Justice Department Guidelines apply with equal force to private civil litigation under RICO. These internal Guidelines, however, do not regulate the activity of private plaintiffs. Therefore, legislation is necessary in order to erect similar safeguards around the private civil RICO mechanism and in that way to

minimize its great potential for abuse. Both the policies reflected in the Guidelines and the screening process that they establish suggest some approaches to reform of civil RICO.

1. Private Civil RICO Claims Should Be Permitted Only After The Defendant Has Been Convicted Of A Related Crime.

In their "Preface," the Guidelines state that, despite the statutory provision that RICO is to be "liberally construed to effectuate its remedial purpose," it is the policy of the Department of Justice that RICO should only be used "selectively." The Guidelines are designed to assure "that not every case, in which technically the elements of a RICO violation exists, will result in the approval of a RICO charge." The Justice Department will not "approve 'imaginative' prosecutions under RICO which are far afield from the Congressional purpose of the RICO statute." As the Guidelines recognize, "the activity which Congress most directly addressed -- the infiltration of organized crime in the nation's economy" -- is the touchstone for determining whether a RICO charge is warranted. This is the same limiting principle that a number of federal trial judges have attempted to impose on civil RICO claims but that appellate courts have said would require legislative change.

In addition, Guideline V states that, in order to constitute a violation of RICO, the "pattern of racketeering activity" should have "some relation to the purpose of the

enterprise." This sensible interpretation is not followed in the civil cases that have been filed under RICO, where allegedly fraudulent activities conducted by legitimate businesses such as investment banking houses, brokerage firms, accounting firms, law firms, and others are -- even if true -- aberrational rather than related to the purpose of those "enterprises."

Moreover, the overall theme of the Guidelines, as stated in their preface, is that "the consequences for the accused" require "particularly careful and reasoned application" of RICO's purposes before making the decision to charge a RICO violation. Accordingly, the Guidelines insist on careful monitoring and centralized control over the Government's filing of any RICO charge. This centralized monitoring guarantees that the Guidelines will be effectively enforced by officials who are charged with public accountability. In dramatic contrast, the decision whether to file a private RICO claim under the broadly worded statute is currently left wholly to the discretion of entrepreneurial private lawyers. Their sole loyalty is to their private clients, and they have no public responsibility for the consequences of any extravagant allegations.

There is one straight-forward amendment to civil RICO that would eliminate the existing abuses, refocus the statute on its intended targets, and adapt the Justice Department's Guidelines to the civil use of RICO. That would be

to permit civil claims to proceed under RICO only after the defendant has been convicted of a RICO offense or of at least one of the predicate offenses. This amendment would effectively curb the abuse of the discretionary power to bring private claims against legitimate business people involved in ordinary commercial activities. It would confine the circumstances in which suits can be filed to those in which public prosecutors have screened those people who may fairly be charged with being involved in "organized crime" or "racketeering" from those who should not be subject to such accusations. This is the kind of protection that a panel of the Second Circuit read into RICO in the Sedima case and that SEC Commissioner Marinaccio called upon Congress to write into the statute.

2. Civil RICO Claims Should Not Overlap Federal Statutes That Specifically Regulate Commercial Transactions

The Justice Department Guidelines highlight another problem with civil RICO as it currently stands. The Preface states that the Department ordinarily will not add a RICO charge "which merely duplicates the elements of proof of a traditional" statute that specifically covers the conduct in question. One of the major criticisms of the current civil RICO provision, however, is that it creates a general, private federal claim for treble damages even where federal law already provides a carefully crafted set of prohibitions and remedies.

The most notable example of this unnecessary and disruptive overlap involves the federal securities laws. Those laws, which Congress and the courts have carefully shaped over fifty years, define the responsibilities of various categories of persons, prescribe the procedures to be followed in maintaining civil suits, establish the time limits applicable in asserting those claims, and tailor the remedies available. By including as a predicate the open-ended offense of "fraud in the sale of securities," however, RICO allows private claimants to duplicate -- but for treble damages -- the rights already granted by the federal securities laws or allows them to circumvent the limitations that Congress has deliberately fashioned for civil suits under those laws. In neither type of situation is there any justification for tolerating the substantial mischief that civil RICO permits. Since federal law comprehensively regulates securities transactions, a person should be allowed to press a civil damage suit only under the circumstances and only to the extent permitted under those specific statutes.

When Congress decided to add securities fraud as a RICO predicate, it referred to only one significant kind of misconduct that was not already covered by the federal securities laws but was attracting organized crime: trafficking in stolen or counterfeit securities. Experience has shown, however, that civil RICO is not being used against schemes of that type. In any event, it is possible to include

that kind of criminal activity in civil RICO without also embracing every other conceivable "fraud in the sale of securities."

3. RICO Should Not "Federalize" Purely State Law Claims

The Justice Department's Guideline III expressly directs that, except in extraordinary circumstances, a RICO count will not be asserted "where the predicate acts consist solely and only of state offenses." Reflecting important considerations of federalism, the commentary explains that this guideline is designed "to underscore the principle that prosecution of state crimes . . . is primarily the responsibility of state authority."

Similar observations apply to the use of the federal courts to litigate civil disputes governed by state law. Nevertheless, the inclusion of "mail fraud" and "wire fraud" in RICO has been used by private plaintiffs as a device for bringing into federal courts what are essentially local commercial or property disputes. This use of RICO has "federalized" state commercial and tort cases. Moreover, as one former federal prosecutor recently wrote in calling for legislation to delete "the mail fraud and wire fraud statutes from the list of predicate acts required to bring a private civil RICO action":

> "[A] general problem with RICO, that the constraints of prosecutorial discretion and guidelines which limit its application in the criminal sphere are no bar to its private civil application . . ., is most acute when the underlying predicate statutes are

> mail fraud and wire fraud, since it is the breadth of these statutes, both actual and potential, that forms the basis for most of the recent expansion of civil RICO litigation." Rakoff, RICO Litigation Reporter 206-07, 211 (September 1984).

Continued inclusion of "mail fraud" and "wire fraud" as predicates for civil RICO claims allows private plaintiffs to disregard these concerns about federalism and to transform local disputes into federal cases simply because one of the parties used the mail or the telephone.

4. RICO Should Not Apply To A Single Episode Or Transaction

The statute makes any two occurrences of a predicate violation within ten years sufficient to show a "pattern of racketeering activity." Guideline IV recognizes that this definition is subject to abuse and provides that no RICO count will be charged "based upon a pattern of racketeering activity growing out of a single criminal episode or transaction."

Most of the private civil cases that have been filed under RICO, by contrast, relate to allegedly fraudulent activity in connection with a single episode or transaction, such as the sale of stock in a single company or the structuring of a particular venture that includes a number of parties. Since each mailing of, for example, a copy of an allegedly misleading financial statement constitutes a separate violation, it is easy for the artful pleader to allege a "pattern" of racketeering in connection with a single commercial episode or transaction. This usage, however, has little to do with the congressional goal of cracking down on racketeers who make

their living by engaging in a continuous pattern of illicit activity over a long career.

VI. CONCLUSION

The need for reform is clear. The nature of the reform is clear. And the responsibility for reform is clear. The Justice Department, implementing the recommendation of the Vice President's Task Group, should urge Congress to amend the civil provisions of RICO to focus the private remedy on its original purpose of aiding the war against organized crime, while curing its capacity to bludgeon innocent business people.