

Avoiding The Pitfalls Of Pleading Civil RICO

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**Civil RICO is a dangerous weapon. It can misfire.
Or even explode in your own hands.**

THE CIVIL SIDE of Federal Racketeer Influenced and Corrupt Organizations Act (“Civil RICO”) has endured perennial popularity with business tort plaintiffs, despite equally long-lived judicial disquiet. Its enticing provisions for treble damages and attorneys’ fees are a siren. As wire and mail fraud can support a Civil RICO claim, a significant swath of business activity can fall within the ambit of a Civil RICO action. Some are afraid that criminal lawyers are best suited to the task. Not so—civil RICO is a species of tort that any litigator can construct. Other business litigators believe that adding a civil RICO claim is little more than “bringing out the big guns.” This view is equally misguided.

Judicial reluctance alone is a formidable barrier to such claims. Courts' hostility to Civil RICO claims stems, in part, from the fear that every tort action will morph into a civil RICO claim. To some extent, overzealous litigants who have garnered the opprobrium that attaches to RICO claims have spoiled the pot by bringing civil RICO actions for such things as overcharges by credit card companies, in which a normal class action would suffice. Also, there is plain judicial distaste for perceived "misuse" of a remedy that was, at least originally, intended for action against organized crime of the "Sopranos" variety. A lawyer considering bringing a civil RICO suit must, therefore, jump through quite a few judicial hoops.

Just as crucial, however, and far more overlooked, is the need to traverse an equally treacherous statutory and procedural minefield, requiring careful planning and consideration of the terrain ahead. This article will address both the procedural and strategic concerns in bringing a Civil RICO suit.

CHOOSING A FORUM • The first issue to confront is the choice of forum. RICO claims arise under federal law, thus can be brought at a federal level, but some states will entertain them. *See Tafflin v. Levitt*, 493 U.S. 455 (1990) (holding that RICO is not exclusively federal). Several states also have their own "little RICO" statutes, creating explicit state causes of action. These come with their own pitfalls, of course. The biggest danger, from the plaintiff's perspective, is that the dearth of case law about state "little RICO" statutes may create something of a Catch-22: When courts want to, they can draw on federal case law by analogy to justify ruling against a claim, but none of the favorable law is binding authority that can protect a complaint.

While the federal forum is a natural first choice for most plaintiffs, particularly in states with strict pleading rules, there are also disadvantages worth weighing. To begin with, most federal courts have adopted local rules with strict pleading require-

ments for RICO far in excess of the usual notice pleading. When local rules do not make such provisions, the "local local" rules or standing orders often do. Typically, a RICO Pleading Statement must accompany the complaint. A plaintiff must look for these local rules and seek to comply, or Rule 12 (and 11) motions can fly quickly. For example, the Southern District of New York requires a plaintiff to file and serve a RICO Pleading Statement within 20 days of filing the complaint, containing all of the following:

- The identity of each defendant and the alleged misconduct and basis for liability for each defendant;
- A list of all alleged wrongdoers who are not defendants, and the misconduct of each wrongdoer;
- A list of all alleged victims and how each was allegedly injured;
- A list of all the predicate acts being relied on;
- All dates, participants, and other surrounding facts for each predicate act;
- The time, place, and contents of the representations for wire and mail fraud claims, and an explanation of how they form a pattern of racketeering activity;
- A description of the alleged RICO enterprise in detail, with names of all individuals, corporations, and partnerships that comprise it;
- A description of the "structure, purpose, nature, and course of conduct of the enterprise."

And there about a two dozen more specific requirements for each subsection of RICO, requiring specific pleading about damages. All of this must be done without discovery. Moreover, the New York rule explicitly invokes Rule 11's "reasonable inquiry" requirement as its justification—indicating that Rule 11 sanctions may come quickly for a plaintiff who cannot meet that high burden. Rules such as these substantially diminish the normal pleading advantage of resorting to federal courts.

Because state courts play host to RICO claims less frequently, they may lack the special pleading requirements for civil RICO in federal courts. In the many states whose civil procedure is based on the federal rules, then, state suits may actually be more attractive if the plaintiff does not yet have all of the details.

The great difficulty with meeting such pleading requirements is in the nature of the “pattern of racketeering activity.” It normally includes pleading acts against others, in which the plaintiff was not involved, where factual discovery may be needed before a sufficiently detailed pleading can be drafted. Pleading a pattern of activity is always difficult, for while a plaintiff knows of its own injury, it can have great difficulty pleading other acts—against others—with specificity. By way of contrast, plaintiffs pressing employment discrimination claims often have to prove a pattern of discrimination against others. They start by making barebones allegations of a pattern of behavior, then use discovery to ferret out the details. They do not have to collect the details before pleading. Under civil RICO, unions have brought suit in friendlier jurisdictions against employers who hire undocumented workers, alleging that hiring them costs jobs and lowers wages of union members. Such suits have survived motions to dismiss, although damages will not be easy to calculate. However, it would be very difficult to maintain such suits if all the information about illegal hiring were required in advance of discovery.

On the other hand, state court unfamiliarity with civil RICO has one glaring downside. Those courts may have even greater difficulty in coming to terms with the breadth of activity encompassed by the RICO statute. As noted above, one of the features of RICO is that the pattern of racketeering activity will consist of a set of allegations about actions by defendants against various third parties. Thus, a plaintiff is often seeking discovery about injuries to third parties and acts unrelated to the plaintiff except insofar as they form a “pattern” of

activity. Courts often take a dim view of discovery regarding certain (often quite salacious) transactions that did not cause the alleged damage to the plaintiff, believing such investigation is intended merely to cause embarrassment (which may not be far off the mark). The advantage of circumventing the federal “pleading statements” for civil RICO is substantially mitigated if discovery is blocked.

The plaintiff’s job, then, is to remind the court that the purpose of RICO was to create liability in parties for acts that otherwise might not meet all the elements of a tort. It is not necessary, indeed highly unlikely, that a plaintiff can match up each RICO defendant with each act of racketeering alleged, or match each pleaded act with damages to itself. The likelihood that discovery regarding third parties may be blocked is a reminder of the key to all civil RICO pleadings: At all stages, the civil RICO plaintiff must focus the court on the whole conspiracy—the web of relationships and wrongdoing—and avoid being bogged down in details as long as possible.

Finally, it is worth remembering that federal subpoena power is more cumbersome than state subpoena power in large western states. California, for example, allows a subpoena to be served anywhere in the state, regardless of where the action is pending, in contrast to the 100-mile limit of Fed R. Civ. P. 45. Therefore, state courts should not be overlooked until a careful examination of the relative pleading requirements is made.

PLEADING THE PATTERN OF RACKETEERING •

The only acts of racketeering that can sustain a “pattern of racketeering” for civil RICO are spelled out in section 1961. These are known as “predicate acts.” It is a rather limited list of specific federal crimes. RICO emphatically does not “borrow” from other statutes beyond the specific crimes listed in section 1961. In general, violations of state law are irrelevant, unless specifically incorporated by section 1961 (e.g., bribery may in-

clude violations of state bribery statutes that carry substantial penalties). In addition, even where the claims involve wire and mail fraud, securities transactions are specifically exempted from this statute, and must be pursued, if at all, as shareholder derivative actions or other appropriate claims.

The most common predicate acts to plead are wire and mail fraud, which today encompass most fraud claims (as face-to-face fraud is increasingly rare). Regardless of forum, however, RICO mail and wire fraud claims are still fraud claims that must be pleaded with some particularity (under Fed R. Civ. P. 9(b) or the state equivalent).

The next hurdle is to establish that there is a pattern of such activity. The pattern of racketeering requires a plaintiff to demonstrate that the predicate acts alleged show “continuity plus relationship.” Single acts, no matter how egregious, cannot support a civil RICO claim. Nor can several diverse bad acts be stitched together to make a “pattern” unless there is some relationship between them, such as a common goal of market domination (other than, of course, the common identity of the actors).

If possible, a plaintiff should portray the predicate acts as a “regular way of doing business,” which has been accepted as a good definition of a pattern. Sometimes, the connection between predicate acts can be shown by pleading additional wrongful acts that are not predicate acts, in order to paint the picture of conspiracy. Unless there is really too little to go on, the plaintiff does best to view the “pattern” requirement as an opportunity to educate the court about defendants’ patterns of wrongdoing.

PLEADING THE SUB-PARTS OF RICO: 1962(a)-(d) • If there is a sufficient pattern of racketeering to meet the threshold of a civil RICO claim, the next issue after choosing a forum is to navigate the technical details of civil RICO’s four subparts. First, unlike its criminal cousin, civil RICO requires a plaintiff to have sustained dam-

ages to have standing. No injunctive relief is permitted to private plaintiffs.

Most importantly, there are four sub-parts to the RICO statute 18 U.S.C. 1962(a) – (d), each with its own standing requirement that hinges on a particular theory of damages. To put it mildly, the distinctions between these sections are opaque, and often result in strained pleading for civil RICO. The tendency to plead all four subsections and hope one sticks is understandable, particularly when key facts are unresolved, but better avoided. On the other hand, there will be extensive motion practice anyway in any Civil RICO action, so a plaintiff is unlikely to avoid motions to dismiss by eschewing extra RICO counts.

Section 1962(a)

Section 1962(a) permits a plaintiff to collect damages if it can show it has been financially injured by a defendant’s investment of income from racketeering in an enterprise that affects interstate commerce. For civil RICO purposes, section (a) is rarely applicable. A plaintiff cannot meet the standing requirement for section (a) merely by showing that a corporate defendant may have re-invested ill-gotten income in itself, in order to fund further acts of racketeering, however damaging that may, in fact, be. One of the few ways to apply this statute is where a defendant uses income derived from predicate acts to set up a network of subsidiaries or affiliates that then carry out harmful or damaging acts. Section 1962(a) can, therefore, be used to pin liability for corporate acts on the ultimate source directing them, if the corporate veil cannot be pierced.

Incidentally, the requirement that the targeted enterprise “affect interstate commerce” is not simply a hook to justify federal legislation in this area by invoking the commerce clause. It is a real requirement. The impact on interstate commerce should not be assumed, even with a particularly large corporation. The best practice is to think about the

link, then affirmatively plead it. If so pleaded, it is unlikely any court will dismiss on those grounds, because the definition of “interstate commerce” is so broad, and because “information and belief” allegations will create factual issues improper for Rule 12(b) resolution. Failure, however, to plead the effect of an enterprise on interstate commerce may invite dismissal, or at least the need to amend, giving a defendant the ability to define the scope of the enterprise as purely in-state before a court that likely is seeking grounds to dismiss.

Section 1962(b)

Section 1962(b) permits a plaintiff to collect damages if it can show it has been injured by a defendant’s use of income from racketeering to acquire control of an enterprise that affects interstate commerce. The distinction between sections (a) and (b) is slight, and the latter is often as little help to an injured plaintiff as the former. Both sections are directed at mobsters investing in legitimate businesses. As a practical matter, a private plaintiff is unlikely to know the connections before the FBI, and may be more likely to spill the beans to the proper authorities before commencing a civil suit.

Section 1962(c) And The RICO Enterprise

Section 1962(c) is usually the key to civil RICO claims, because it permits a plaintiff to collect damages if it can show it has been injured by a defendant conducting the affairs of an enterprise affecting interstate commerce through a pattern of racketeering. Under section (c), a plaintiff pleads that it was financially harmed directly by a predicate act—not the investment or use of ill-gotten gains. This is not only the most straightforward section to plead, but also the most likely. A particularly nasty act is the most likely genesis of the desire to bring a civil RICO action. For standing under section (c), then, a plaintiff must plead a pattern of racketeering acts, one of which, at least, caused it direct, financial harm.

Although more straightforward in the connection between act and injury, section (c) claims are fraught with pleading pitfalls. First and foremost, under section (c), pleading the “RICO enterprise” requires great care. Under sections (a) and (b), the RICO enterprise is often the mere instrumentality of the real defendants operating behind the scenes, also a nominal defendant. Under section (c), however, the RICO enterprise takes center stage.

Under section 1962(c), case authority holds that the RICO enterprise can not be named as a defendant, but is just the instrumentality by which named defendants injured the plaintiff. If pleading more than one RICO subsection, then, a plaintiff must be careful to make sure that the RICO enterprise is not named as a defendant for the section (c) claim, while simultaneously avoiding “blowing hot and cold” on the same set of facts. The typical private plaintiff will allege that a corporation is the section (c) RICO enterprise, while only naming the officers, directors, and affiliate companies as actual RICO defendants. For example, if a civil RICO plaintiff wants to bring a RICO claim against an insurance company for a pattern of mail fraud, the claim will be against the officers, directors, and affiliates of the insurance company, but the insurance company itself cannot be named as a defendant in the section (c) claim.

This pleading quirk can cause a dilemma. Plaintiffs are fond of big pockets. One obvious choice for a plaintiff would be to include a separate claim against the target company as a named defendant for ordinary fraud, but that may only serve to underscore the defendants’ position that the civil RICO action is just a fraud claim gussied up. Fraud claims do not come with treble damages and attorneys’ fees.

A RICO enterprise need not be a corporation, however. At its barebones, the RICO enterprise is some sort of organization or group, formal or informal, which has some purpose beyond merely committing the predicate acts. A RICO enterprise

has to have some *raison d'être* beyond criminality. However, it need not be incorporated, organized, or even anything more than an informal group that has some structure or relationship between the members. Remember: the archetypal RICO enterprise is a mob family.

The barest of barebones is the “association in fact” enterprise. If properly done, such a murky enterprise has a far more sinister look about it. It feels more like a RICO claim than just a tort claim in tarty clothing. For example, it may be that two cousins and a trusted employee collectively operate several legitimate businesses in a particular industry (say, auto repair) and regularly commit fraud on customers (say, by using junkyard parts rather than the factory OEM parts, then mailing or faxing bills claiming to have provided better parts). The complaint may name the cousins and their employee as an “association-in-fact” enterprise, because their association with one another, while informal, meets the requisite characteristics: (1) it has an independent existence beyond the fraud itself, in operating various repair shops; and (2) it contains some sort of structure or organization (big cheese, little cheese, gopher). Of course, going this route raises more proof and pleading issues than naming a clean entity (such as a corporation or partnership) as a RICO enterprise.

Theoretically, it is even possible to set forth a RICO claim against a single person who owns 100 percent interest in a corporation operating that corporation through acts of racketeering. “[I]f the enterprise was a corporation, the fact that there was but one stockholder would not shield that individual from suit, because such a corporate ‘one-man’ band does receive some legal protections..., [a] legal shield for illegal activity that Congress intended RICO to pierce.” *Sever v. Alaska Pulp Corp.*, 978 F.2d 1529, 1534 (9th Cir. 1992). As unlikely as it sounds, Internet businesses run out of the house (scammers and spammers) would seem to make such one-man-band suits more likely.

Section 1962(d)

Finally, section 1962(d) permits a plaintiff to bring suit if he or she has been injured by a conspiracy to violate subsections (a)-(c). Although the Supreme Court has yet to decide the issue, most circuits hold that this subsection cannot be pleaded unless a plaintiff can also plead an actual violation of another subsection of RICO. Normal conspiracy law would provide liability for the conspiracy alone, even if no criminal act actually results, because it is black letter law that conspiracy itself is an evil. For some reason, however, most courts reject that common-sense principle in civil RICO cases. Therefore, the law is that a section (d) claim cannot exist on its own. The corollary, however, is that any well-pleaded violation of subsection (a) – (c) can usually be accompanied by a section (d) claim without much difficulty.

Why bring a section (d) claim at all? One reason is to sweep in other defendants with a less clear nexus to the criminal activity. For example, it might be used to bring in a small web-hosting company that hosts high-bandwidth pornography sites (and which knows very well that the pornographic sites are just fronts for stealing credit card numbers) but which otherwise does not participate in RICO enterprise. Or, in the auto repair hypothetical mentioned earlier, it might provide a means to sweep in other persons not in the “inner circle” (such as junkyard suppliers) as conspirators. Another reason is that section (d) also is something of a freebie: inasmuch as it requires a violation of subsection (a) – (c) to be proven, it will probably survive until the end of the case, and most plaintiffs prefer to have more than one claim for relief.

Still another reason is that section (d) may help in handling federal RICO Pleading Statements. By allowing a plaintiff to separate defendants into two sets, one of which lacks a strong nexus in a separate claim for relief, it makes it more likely that the court will strike only that category of defendants, rather than all of them.

CONCLUSION • Drafting a well-pleaded civil RICO complaint requires careful assessment of numerous statutory and procedural issues. Some of the hurdles may seem irrational, or at least counter-intuitive. Many are traps for the unwary. It will take considerably more than just a few connected acts of wrongdoing to mount a civil RICO claim. Most often, a civil RICO claim becomes an expensive distraction that can end up harming the client, for the danger is that a plaintiff's injury can be shortchanged with all the judicial attention on the requisite intricacies of RICO pleading. A case that might be better pleaded, and easier won, as "mere" fraud may find itself against a much more hostile court if pleaded as civil RICO, with attendant consequences.

Therefore, plaintiffs who believe that RICO is a cheap and flashy way to draw attention and force a big settlement (to avoid embarrassment) are barking up the wrong tree. What you will get, instead, is lengthy and expensive motion practice, with many reversals along the way. A civil RICO case will definitely be farmed out to a large national law firm with substantial resources and a habit of drowning opponents in paperwork. Neither side should

expect federal limits on the number and length of depositions to be honored in a broad-ranging civil RICO case. The promise of treble damages and attorneys' fees is mitigated by the great cost and time it will take to prosecute the case, plus the higher than average likelihood of dismissal.

Also, good claims can be lost through careless pleading. Necessary discovery can be blocked, or truncated, by hostile courts. And, as a plaintiff, you will basically have the job of convincing the court that there is serious wrongdoing that could not be adequately addressed otherwise.

The primary reason to bring civil RICO claims is not, therefore, to increase the likelihood or size of a settlement. Rather, civil RICO best suited to a plaintiff for whom showing a pattern of racketeering activity is crucial to justifying redress for its own injury. It allows a plaintiff to discuss similar acts of wrongdoing, which matters most where the offense might not stand up in isolation, or where the offense is minor but the pattern is ugly. The statute was originally enacted to fight organized crime; a plaintiff would do well to consider foregoing civil RICO unless it can show there is, at least, a whiff of sulfur about the defendants.

PRACTICE CHECKLIST FOR Avoiding The Pitfalls Of Pleading Civil RICO

Courts are reluctant to entertain civil RICO claims and the procedural barriers are formidable.

- At the outset, it is essential to consider the forum. A RICO claim can be brought in federal court or in some jurisdictions, state court. (Several states also have their own "little RICO" statutes.) Many federal courts have adopted local rules with strict pleading requirements for RICO that are far stricter than the usual notice pleading standard. As an example, the Southern District of New York requires a plaintiff to file and serve a RICO Pleading Statement containing all of the following:
 - ___ The identity of each defendant and the alleged misconduct and basis for liability for each defendant;
 - ___ A list of all alleged wrongdoers who are not defendants, and the misconduct of each wrongdoer;
 - ___ A list of all alleged victims and how each was allegedly injured;
 - ___ A list of all the predicate acts being relied on;

- ___ All dates, participants, and other surrounding facts for each predicate act;
- ___ The time, place, and contents of the representations for wire and mail fraud claims, and an explanation of how they form a pattern of racketeering activity;
- ___ A description of the alleged RICO enterprise in detail, with names of all individuals, corporations, and partnerships that comprise it;
- ___ A description of the “structure, purpose, nature, and course of conduct of the enterprise.”
 - By contrast, states courts are less likely to have highly specialized requirements fro RICO pleading.
 - The great difficulty with meeting such pleading requirements is in the nature of the “pattern of racketeering activity.”
 - The only acts of racketeering that can sustain a “pattern of racketeering” for Civil RICO are spelled out in section 1961, and it is a rather limited list of specific federal crimes (“predicate acts”).
 - The next hurdle is to establish that there is a pattern of such activity. The pattern of racketeering requires a plaintiff to demonstrate that the predicate acts alleged show “continuity plus relationship.” Single acts, no matter how egregious, cannot state a Civil RICO claim:
- ___ Section 1962(a) permits a plaintiff to collect damages if it can show it has been financially injured by a defendant’s investment of income from racketeering in an enterprise that affects interstate commerce. For civil RICO purposes, section (a) is rarely applicable;
- ___ Section 1962(b) permits a plaintiff to collect damages if can show it has been is injured by a defendant’s use of income from racketeering to acquire control of an enterprise that affects interstate commerce. Both sections (a) and (b) are directed at mobsters investing in legitimate businesses;
- ___ Section 1962(c) is usually the key to civil RICO claims, because it permits a plaintiff to collect damages if it can show it has been injured by a defendant conducting the affairs of an enterprise affecting interstate commerce through a pattern of racketeering. Under section (c), the plaintiff claims it has been injured directly (and financially) by a predicate act. This is not only the most straightforward section to plead, but also the most likely. Under section 1962 (c), however, the RICO enterprise cannot be a named defendant.
- ___ Finally, section 1962(d) permits a plaintiff to bring suit if he or she has been injured by a conspiracy to violate subsections (a)-(c). One reason to bring a section 1962(d) action is to sweep in other defendants with a less clear nexus to the criminal activity.

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