

1994

RICO and the "Operation or Management" Test: The Potential Chilling Effect on Criminal Prosecutions

Ira H. Raphaelson

Michelle D. Bernard

Follow this and additional works at: <http://scholarship.richmond.edu/lawreview>

 Part of the [Antitrust and Trade Regulation Commons](#), and the [Criminal Law Commons](#)

Recommended Citation

Ira H. Raphaelson & Michelle D. Bernard, *RICO and the "Operation or Management" Test: The Potential Chilling Effect on Criminal Prosecutions*, 28 U. Rich. L. Rev. 669 (1994).

Available at: <http://scholarship.richmond.edu/lawreview/vol28/iss3/4>

This Article is brought to you for free and open access by the Law School Journals at UR Scholarship Repository. It has been accepted for inclusion in University of Richmond Law Review by an authorized editor of UR Scholarship Repository. For more information, please contact scholarshiprepository@richmond.edu.

RICO AND THE "OPERATION OR MANAGEMENT" TEST: THE POTENTIAL CHILLING EFFECT ON CRIMINAL PROSECUTIONS

*Ira H. Raphaelson**

*Michelle D. Bernard***

I. INTRODUCTION

For more than two decades, prosecutors, plaintiffs' lawyers, the civil and criminal defense bar, and the courts have struggled with the coverage of the Racketeer Influenced Corrupt Organizations Act ("RICO" or the "Act").¹ The Supreme Court has interpreted the Act many times in both criminal and civil cases.² For the most part, the high Court has applied the man-

* The authors are attorneys with the law firm of Shaw, Pittman, Potts & Trowbridge in Washington, D.C., who concentrate their practices on corporate compliance matters, civil litigation and the defense of complex white collar criminal cases.

Mr. Raphaelson joined Shaw Pittman in January 1993 after a fifteen year career as a state (1978-1980) and federal (1980-1993) prosecutor. Mr. Raphaelson worked in the U.S. Attorney's Office in Chicago where he concentrated on the prosecution of complex white collar crimes. While an Assistant United States Attorney, Mr. Raphaelson successfully prosecuted six Racketeer Influenced and Corrupt Organizations (RICO) matters before juries. He also supervised RICO prosecutions in a district that brought more cases and convicted more defendants than any other district in the country using the RICO statute. Between 1991 and 1993, Mr. Raphaelson served as the Bush Administration's Special Counsel for Financial Institutions Crime within the Justice Department as well as Counselor to then Attorney General William P. Barr.

** Ms. Bernard is an associate at Shaw Pittman, practicing in the areas of white collar criminal defense, litigation, financial institutions and corporate compliance and government relations. She is a member of the American Bar Association's White Collar Crime Committee and Section of Business Law, Committee on Criminal Law, and is co-chair of its Subcommittee on Financial Institution Fraud.

The authors wish to thank J. Mark Gidley, Esquire, counsel with Shaw Pittman, whose editorial comments were invaluable. The authors also wish to recognize and thank summer associates Kevin Broyles, Andrew Miller and Ian Walker for their indispensable research and assistance in this endeavor.

1. Pub. L. No. 91-452, § 901, 84 Stat. 922, 941 (1970) (codified at 18 U.S.C. §§ 1961-1968 (1988)).

2. *E.g.*, *Reves v. Ernst & Young*, 113 S. Ct. 1163 (1993); *H.J. Inc. v. Northwestern Bell Tel. Co.*, 492 U.S. 229 (1989).

datory "liberal" interpretation language of the law³ to expand the scope of the statute in criminal cases.⁴ However, in the civil cases considered, the Supreme Court has generally restricted the scope of the Act.⁵

The restriction of RICO in the face of a statutory mandate to interpret it broadly is particularly surprising for a Court which has expressed disdain for judicial activism.⁶ Some commentators have described RICO as favoring the prosecution.⁷ This Article will attempt to examine the recent trend whereby the Supreme Court restricts RICO as a function of the Court's dislike of the Act, rather than its traditional method of statutory construction. Congress created a private cause of action in RICO hoping to assist prosecutors by creating an economic incentive and mechanism to involve private citizens in the "war on crime."⁸ The net result of the private bar's use of RICO and the Supreme Court's result-oriented narrowing of RICO's scope will ultimately be an unintended limitation on government use of the statutory tool.⁹

Recently, the Supreme Court considered the meaning of the word "conduct," as a noun and as a verb in the RICO prohibition provision most often used by prosecutors, 18 U.S.C. § 1962(c).¹⁰ The commonly understood English definition of the word "conduct," when used as a verb, means to "carry on."¹¹ As a noun, it normally means "the way a person acts; behav-

3. Organized Crime Control Act, Pub. L. No. 91-452, § 904(a), 1970 U.S.C.C.A.N. (84 Stat.) 1104 ("The provisions of this title [RICO] shall be liberally construed to effectuate its remedial purposes."). *Id.*

4. *See, e.g.,* *Russello v. United States*, 464 U.S. 16 (1983); *United States v. Turkette*, 452 U.S. 576 (1980).

5. *See, e.g.,* *H.J. Inc.*, 492 U.S. at 229.

6. *See, e.g.,* *Harper v. Virginia Dep't of Taxation*, 113 S. Ct. 2510 (1993).

7. *See, e.g.,* Gerard E. Lynch, *RICO: The Crime of Being a Criminal*, 87 COLUM. L. REV. 661, 719-23 (1987) (stating that prosecutorial discretion is important to prevent abuse of RICO's broad prohibiting provisions).

8. Norman Abrams, *A New Proposal for Limiting Private Civil RICO*, 37 UCLA L. REV. 1, 2-3 (1989).

9. Despite the difference between the Court's interpretive approach in criminal and civil cases, the holdings from the civil RICO cases extend to criminal cases and vice versa. The substantive provisions defining RICO violations, 18 U.S.C. § 1962 (1988), is shared for civil and criminal RICO. Civil RICO is, however, enforced through 18 U.S.C. § 1964 (1988) and criminal RICO through 18 U.S.C. § 1963 (1988).

10. *Reves v. Ernest & Young*, 113 S. Ct. 1163, 1169 (1993).

11. THE AMERICAN HERITAGE DICTIONARY 307 (2d ed. 1987).

ior"¹² The definition and use of the word "conduct" under § 1962(c) is critical to criminal RICO prosecutions because virtually every act proscribed by § 1962(c) as a verb and a noun is defined by one of these two uses of the word "conduct."¹³ Thus, a restrictive definition of the word "conduct" affects the government's ability to enforce the Act.¹⁴

In *Reves v. Ernst & Young*,¹⁵ the Supreme Court considered application of the "operation or management" test,¹⁶ whereby a party is liable under § 1962(c) only if he or she has participated in the operation or management of the enterprise itself.¹⁷ By construing the phrase "to conduct or participate, directly or indirectly, in the conduct of such enterprise's affairs" as importing a degree of direction or control into § 1962(c),¹⁸ the Supreme Court has created a defense to actions brought under the Act that unduly restricts the scope of RICO and that will deter bringing criminal prosecutions under the Act.

Imagine a federal prosecutor evaluating two cases for prosecution post-*Reves*. In the first case, a bank president lied to regulators, bribed Congressmen, defrauded investors, and received kickbacks on real estate loans. In the second case, a soldier in an organized crime family committed murder, arson, and engaged in numerous extortionate credit transactions.

Passed in 1970 as title IX of the Organized Crime Control Act of 1970,¹⁹ RICO prohibits (1) the use of money gained from

12. *Id.*

13. The word conduct appears twice in 18 U.S.C. § 1962(c) (1988), first as a verb, then as a noun. § 1962(c) provides:

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

Id.

14. *See, e.g.*, Brief for the United States as Amicus Curiae Supporting Petitioners at 6, *Reves v. Ernst & Young*, 113 S. Ct. 1163 (1993) (No. 91-886) ("[T]he Court of Appeals' holding that the defendant must have participated in operating or managing the enterprise in order to be held liable under Section 1962(c) is unfounded and threatens to impede the government's enforcement of the RICO statute.") *Id.*

15. 113 S. Ct. 1163 (1993).

16. *See Bennett v. Berg*, 710 F.2d 1361, 1364 (8th Cir. 1983).

17. *Reves*, 113 S. Ct. at 1172-73.

18. *Id.* at 1169-70.

19. Organized Crime Control Act, Pub. L. No. 91-452, § 901, 84 Stat. 922, 941

a "pattern of racketeering activity" in acquiring or operating any "enterprise" engaged in interstate commerce;²⁰ (2) the acquisition of such an enterprise through a pattern of racketeering activity;²¹ (3) the running of such an enterprise through a pattern of racketeering activity;²² and (4) the conspiracy to commit any of these activities.²³ Consequently, on its face, the Act provides that almost any connection between a pattern of racketeering activity and an enterprise engaged in interstate commerce constitutes a RICO violation.

After ten years of relatively little use, RICO became an important and harsh tool in the hands of prosecutors during the 1980's and beyond. Hotly contested prosecutions produced reams of pages of judicial interpretation. Given the power of the Act, the Justice Department implemented strict guidelines for centralized review and approval of the Act's use.²⁴ The civil component of the Act, however, produced pleadings by the private bar which had not undergone rigorous review like that attendant to the government's use of the Act. The courts, including the Supreme Court, repeatedly expressed concern over the private misuse of the Act and the federalizing of routine contract matters through overly creative pleadings.²⁵ Scholars debated both sides of the issue with the plaintiff and defense

(1970) (codified at 189 U.S.C. §§ 1961-1968 (1988)).

20. § 1962(a).

21. § 1962(b).

22. § 1962(c).

23. § 1962(d).

24. Unlike private RICO actions, all government actions are subject to strict internal review and controls. The Criminal Division of the U.S. Department of Justice established a system whereby every proposed RICO action by the government, criminal or civil, is submitted to the Organized Crime and Racketeering Section for review and approval. See CRIMINAL DIV., THE DEPT OF JUSTICE MANUAL, ORGANIZED CRIME AND RACKETEERING § 9-110.320 (Supp. II 1993) [hereinafter MANUAL]. The Organized Crime and Racketeering Section modifies most of these cases before the charges are filed. *Id.* § 9-110.210. As a result of the review process, very few of the Justice Department's RICO prosecutions have failed because of defective pleadings or legal justification. Arguably, the lack of such controls over private civil actions has caused much of the controversy surrounding the private use of RICO. Obviously, this has a negative impact upon governmental actions.

25. See, e.g., L. Gordon Crovitz, *Two Cheers for This Bill to Reform RICO*, WALL ST. J., June 27, 1990, at A13 (praising a 1990 House Bill that restricted use of RICO in civil cases); *Wounding the RICO Beast*, WASH. TIMES, Nov. 27, 1989, at F2 (stating that Judge Sentelle of the D.C. Circuit has labeled RICO "the monster that ate jurisprudence").

bars predictably on opposite sides of the call for civil RICO reform.²⁶

Whether § 1962(c) of the Act is used properly by the private bar or not, the Supreme Court has repeatedly articulated its suspicion that because abuses occur, the scope of the Act needs redefinition.²⁷ Nevertheless, any proposed change in RICO must be measured not only in terms of its perceived abuses, but also in terms of the negative impact that it may have on desirable law enforcement efforts. For this reason alone, any restriction on the reach of RICO should come from Congress rather than the Supreme Court. Notwithstanding this reasoning and an intellectual tradition which abhors judicial activism, the Burger and Rehnquist Supreme Courts acted based on their perception and redefined RICO in ways that are inconsistent with both its plain meaning and congressional intent. The result is that the ability of government prosecutors to use the Act effectively has diminished due to limitations imposed through private litigation. After *Reves*, the absurd result of the two hypotheticals previously offered may well be that the bank president is clearly within the scope of the Act while the mafia foot soldier may not be.

This Article argues that the Supreme Court's decision in *Reves* was incorrect on the merits and that the decision invites legislative reversal. Part II traces the history of RICO and the calls for civil RICO reform. Parts III, IV, and V trace the Supreme Court's expansive approach to RICO in its criminal and criminal forfeiture analyses. In this regard, the Supreme Court's liberal construction of the Act enabled the government to secure numerous important convictions under RICO and made RICO one of the most effective tools for prosecuting orga-

26. See, e.g., Abrams, *supra* note 8, at 1; G. Robert Blakey & Thomas A. Perry, *An Analysis of the Myths that Bolster Efforts to Rewrite RICO and the Various Proposals for Reform: "Mother of God—Is this the End of RICO?"* 43 VAND. L. REV. 851 (1990); Susan Getzendanner, *Judicial "Pruning" of "Garden Variety Fraud" Civil RICO Cases Does Not Work: It's Time for Congress to Act*, 43 VAND. L. REV. 673 (1990); Michael Goldsmith, *Judicial Immunity for White Collar Crime: The Ironic Demise of Civil RICO*, 30 HARV. J. ON LEGIS. 1 (1993); William J. Hughes, *RICO Reform: How Much Is Needed?* 43 VAND. L. REV. 639 (1990); Adam F. Ingber, *10b-5 or Not 10b-5? Are the Current Efforts to Reform Securities Litigation Misguided?*, 61 FORDHAM L. REV. 351 (1993) (arguing that reform of RICO is preferable to reform of Rule 10b-5).

27. See, e.g., *Sedima, S.P.L.R. v. Imrex Co.*, 473 U.S. 479 (1985).

nized crime, drug trafficking and official corruption. Part VI discusses the Supreme Court's warning concerning RICO's reach. Parts VII, VIII and IX argue that by importing an "operation or management" test into § 1962(c), the Supreme Court further limited the reach of RICO and potentially, the government's ability to use the Act for its intended purpose.

II. THE EVOLUTION OF RICO

In 1970, Congress enacted the Organized Crime Control Act, of which Title IX is known as RICO.²⁸ Congress enacted the 1970 Act to "strengthen the legal tools in the evidence-gathering process, by establishing new penal prohibitions and, by providing enhanced sanctions and new remedies . . ."²⁹ In 1980, the private bar finally began to bring civil RICO suits.³⁰ Since that time, the number of civil RICO suits brought by the private bar has increased dramatically,³¹ causing many to believe that RICO is overused and that civil RICO should be reformed.

For example, a former federal judge has commented:

My RICO perspective comes from my years as a federal district court judge in Chicago from 1980 to 1987, when I witnessed the real birth and growth of civil RICO. I am told . . . that for a time I had written more RICO opinions than any other judge in the country As I dealt with these cases, it became clear to me that most civil RICO cases simply should not be in federal court. The majority of civil RICO cases involve commonplace commercial controversies, the facts of which reveal an ordinary business relationship gone sour. These mercantile melees are recharacterized

28. Pub. L. No. 91-452, § 901, 84 Stat. 922, 941 (1970) (codified at 18 U.S.C. §§ 1961-1968 (1988)).

29. § 901, 84 Stat. at 923.

30. See A.B.A. SEC. CORP., BANKING & BUS. LAW, Report of the Ad Hoc Civil RICO Task Force 55 (1985).

31. For example, although RICO was enacted in 1970, the *civil* provisions were not used extensively until the early 1980's. As reported by a RICO task force of the American Bar Association, of approximately 270 trial court decisions between 1970 and 1985, only 3% were decided before 1980, 20% in 1980, 7% in 1981, 13% in 1982, 33% in 1983, and 43% in 1984. *Id.*

by resourceful attorneys to conform with the requirements of RICO: adding a few allegations of the use of the mails or wires in furtherance of a fraudulent scheme, describing how the mail or wire fraud offenses form a pattern, and explaining how the defendants conducted the affairs of an appropriate enterprise. Thus transmogrified, the ordinary state law fraud or contract action becomes a federal "racketeering" case, threatening treble damages, costs, and attorney's fees. Not only is this transformation unfair to the typical commercial defendant, but it also burdens the dockets of the federal courts and multiplies the legal costs for both sides in otherwise straightforward litigation.³²

At the same time the private bar increased its use of RICO, the Act became the prosecutor's tool of choice in organized crime, political corruption, white collar crime, terrorism, and hate group prosecutions.³³ Also, the Department of Justice began enforcing the civil provisions of the Act.³⁴ Nevertheless, the clogging of the judicial docket by the private bar's perceived and often actual misuse of civil RICO has stimulated the Supreme Court's efforts to limit the reach of the Act. Thus, as in the area of habeas corpus, the Court created a measure of docket control for itself in the absence of congressional action.³⁵ In both areas, the Court appears to believe it is acting merely to protect the caseload of the lower federal courts.

32. Getzendanner, *supra* note 26, at 674.

33. See *Oversight on Civil RICO Suits: Hearings Before the Senate Comm. on the Judiciary*, 99th Cong., 1st Sess. 109-11 (1985) (statement of Assistant Attorney General Stephen S. Trott) [hereinafter *Oversight Hearings*]; see also *United States v. Yarbrough*, 852 F.2d 1522 (9th Cir.) (RICO prosecution of a white-hate group, for robbery, murder and other crimes), *cert. denied*, 488 U.S. 866 (1988); *United States v. Angiulo*, 847 F.2d 956 (1st Cir. 1988) (RICO prosecution of a Boston organized crime family); *United States v. Marubeni Am. Corp.*, 611 F.2d 763 (9th Cir. 1980) (RICO prosecution of a Japanese corporation for mail fraud and bribery).

34. See Karen Tumulty, *U.S. Files Suit to Oust Mob from N.Y. Waterfront*, L.A. TIMES, Feb. 15, 1990, at A1 (reporting a civil RICO suit by the Justice Department against the International Longshoremen's Association alleging extortion, embezzlement, bribes, mail fraud, assault and murder; quoting the Attorney General's statement that a "hidden tax of payments to organized crime" was imposed that cost the consumers millions of dollars; and noting the opposition by more than 250 members of Congress as well as former Gov. Michael S. Dukakis to the use of civil RICO against unions).

35. See, e.g., Yale L. Rosenberg, *Kaddish for Federal Habeas Corpus*, 59 GEO. WASH. L. REV. 362 (1991).

III. EXPANDING RICO'S REACH: CRIMINAL ENTERPRISES

Beginning with its decision in *United States v. Turkette*,³⁶ the Supreme Court's interpretation of § 1962(c) allowed the government to expand use of the Act in a manner that was not only appropriate, but served legitimate law enforcement purposes. In *Turkette*, the Supreme Court endorsed "illegitimate enterprise" prosecution.³⁷ The indictment in *Turkette* concerned a number of arson-for-profit schemes.³⁸ After conviction, and on appeal, respondent argued that "RICO was intended solely to protect legitimate business enterprises from infiltration by racketeers and that RICO" did not prohibit "participation in an association which performed only illegal acts and which" did not "attempt to infiltrate a legitimate enterprise."³⁹ The First Circuit agreed with the respondent's position, reversing his conviction.⁴⁰ However, the Supreme Court reversed, holding that the term "enterprise" encompassed *both* legitimate and illegitimate enterprises.⁴¹ As the Supreme Court reasoned, "[t]he common thread to all counts was [Turkette's] alleged leadership of this criminal organization through which he orchestrated and participated in the commission of the various crimes."⁴²

Both the prosecution and the Supreme Court found Turkette's and his co-conspirators' conduct a "criminal organization":

[A] group of individuals associated in fact for the purpose of illegally trafficking in narcotics and other dangerous drugs, committing arsons, utilizing the United States mail to defraud insurance companies, bribing and attempting to bribe local police officers, and corruptly influencing and attempting to corruptly influence the outcome of state court proceedings⁴³

36. 452 U.S. 576 (1981).

37. *Turkette*, 452 U.S. at 580-81.

38. The Supreme Court opinion itself offers few of the facts of the case; however, the opinion of the First Circuit discusses the evidence supporting the charges in some detail. See *United States v. Turkette*, 632 F.2d 896, 908-09 (1st Cir. 1980), *rev'd*, 452 U.S. 576 (1981).

39. *Turkette*, 452 U.S. at 579-80.

40. *Id.* at 580.

41. *Id.* at 593.

42. *Id.* at 579.

43. *Id.* (quoting the indictment).

In response to the appellate court's contention that expanding RICO to illegitimate enterprises would merge the enterprise requirement into a pattern of racketeering requirement,⁴⁴ the Court found that while the evidence used to prove the two elements may overlap, *both* elements must be proved. Thus, the Court stated that "[i]n order to secure a conviction under RICO, the Government must prove both the existence of an 'enterprise' and the connected 'pattern of racketeering activity.'"⁴⁵ The Court then stated that a RICO enterprise must be an "entity" proven "by evidence of an ongoing organization, formal or informal, and by evidence that the various associates function as a continuing unit."⁴⁶

The Supreme Court's broad interpretation of the word "enterprise" in *Turkette* allowed prosecutors to use the Act effectively in carrying out the aims of Congress. As one commentator has stated:

The advantages to the prosecution in indicting this sort of case under RICO . . . are considerable. Crimes that otherwise could not have been joined in the same indictment could be amalgamated, crimes over which the federal government would ordinarily not have jurisdiction could be proved, and defendants who were involved in only a small part of the operation could be tied into the same indictment. In addition, greatly enhanced penalties would be available, without the need for procedurally cumbersome mechanisms such as those of the Dangerous Special Offender statute.⁴⁷

Thus, the interpretation of § 1962(c) adopted in *Turkette*

turn[ed] RICO from a probably redundant prohibition of acts of infiltration into precisely the sort of prohibition against membership in a criminal organization that seemed as problematic earlier. After *Turkette*, RICO makes it a crime not only to infiltrate or corrupt legitimate enterprises,

44. United States v. *Turkette*, 632 F.2d 896, 899 (1st Cir. 1980), *rev'd*, 452 U.S. 576 (1981).

45. *Turkette*, 452 U.S. at 583.

46. *Id.*

47. Lynch, *supra* note 7, at 706.

but *also* to be a gangster, whether in the Mafia or in a much more loosely affiliated criminal combine.⁴⁸

IV. EXPANDING RICO'S REACH: FORFEITURE

Arguably, the Supreme Court's decision in *Russello v. United States*,⁴⁹ represents the culmination of the Supreme Court's acceptance of the government's efforts to use RICO as an effective weapon. The target was not only organized crime infiltration of legitimate business, but also the existing criminal organizations in general.

Russello, like *Turkette*, involved an arson-for-hire ring. The arsonists were convicted of RICO violations, among other crimes, and, in addition to fines and prison sentences, various forfeitures were ordered. The issue before the Supreme Court was whether the profits earned by one of the arsonists were subject to forfeiture as part of the RICO judgment.⁵⁰

The forfeiture provision of RICO as it stood in 1983 provided that any person convicted of violating RICO forfeited to the United States "any interest he [had] acquired or maintained in violation of" RICO.⁵¹ *Russello* argued in support of a narrow construction of the forfeiture provision such that money or profits acquired through criminal conduct could not constitute an "interest" within the meaning of § 1963(a)(1) because an "[i]nterest," by definition, includes of necessity an interest *in* something.⁵² That is to say, an interest, as opposed to profits or proceeds, should be defined as an interest in the enterprise itself.

The Supreme Court unanimously rejected *Russello's* arguments, stating as follows:

We note that the RICO statute's definition of the term "enterprise" in § 1961(4) encompasses both legal entities and illegitimate associations-in-fact. Forfeiture of an interest

48. *Id.* (citations omitted) (emphasis added).

49. 464 U.S. 16 (1983).

50. *Russello*, 464 U.S. at 17.

51. 18 U.S.C. § 1963(a)(1) (1982).

52. *Russello*, 464 U.S. at 22 (citing Brief for Petitioner at 9) (emphasis added).

in an illegitimate association-in-fact ordinarily would be of little use because an association of that kind rarely has identifiable assets; instead, proceeds or profits usually are distributed immediately. Thus, construing § 1963(a)(1) to reach only interests in an enterprise would blunt the effectiveness of the provision in combatting illegitimate enterprises, and would mean that "[w]hole areas of organized criminal activity would be placed beyond" the reach of the statute.⁵³

Thus, the Supreme Court took an expansive view of the forfeiture provisions in *Turkette*.

As Professor Lynch has noted,⁵⁴ whether or not *Russello* was consistent with the congressional intent behind the Organized Crime Control Act of 1970, it is clearly consistent with the spirit of the congressional intent behind the expanded reach of RICO which occurred in the 1980's. For example, in the Comprehensive Crime Control Act of 1984,⁵⁵ Congress expressly adopted the *Russello* holding and elaborated on the forfeiture provisions of the Act.⁵⁶ Thus, one may argue that the 1984 forfeiture provisions enacted by Congress represent an implicit endorsement not only of the expanded reach of RICO, but also of its use of RICO against illegitimate associations. *Russello* clearly suggests that Congress is satisfied with the Supreme Court's expansive interpretation of RICO in the area of crime.⁵⁷

53. *Id.* at 24 (quoting *United States v. Turkette*, 452 U.S. 576, 589 (1981)).

54. *See Lynch, supra* note 7, at 710-13.

55. Pub. L. No. 98-473, 98 Stat. 1976 (1984) (codified in various sections of the U.S.C.).

56. § 302, 98 Stat. at 2040 (codified at 18 U.S.C. § 1963).

57. *Cf. United States v. Horak*, 833 F.2d 1235, 1241-44 (7th Cir. 1987) (discussing the Seventh Circuit's analysis of pre- and post-amendment forfeiture).

V. EXPANDING RICO'S REACH: STANDING AND THE "PATTERN" CONCEPT

In *Sedima, S. P. R. L. v. Imrex Co.*,⁵⁸ Sedima, a Belgian corporation, filed an action in a New York federal district court. Sedima's complaint set forth claims under § 1964(c) of RICO,⁵⁹ supported by alleged violations of § 1962(c) based on predicate acts of mail and wire fraud.⁶⁰ A third count alleged a conspiracy to violate § 1962(c).⁶¹

The United States District Court for the Eastern District of New York held that "for an injury to be 'by reason of a violation of § 1962,' " as required by § 1964(c), it must somehow be different in kind from the direct injury resulting from the predicate acts of racketeering activity.⁶² In an attempt to limit RICO's scope, the district court held that a complaint must allege a "RICO-type injury," which was either a "racketeering enterprise injury," or a "competitive injury." In *Sedima*, the district court found "no allegation . . . of any injury apart from that which would result directly from the alleged predicate acts of mail fraud and wire fraud," and accordingly, dismissed the RICO counts for failure to state a claim.⁶³

The Second Circuit affirmed,⁶⁴ holding that Sedima's complaint was defective in two ways. First, the Second Circuit found that Sedima's complaint failed to allege an injury "by reason of a violation of § 1962."⁶⁵ In the Second Circuit's view, the language of the sections was clearly a limitation on standing, reflecting congressional intent to compensate victims of "certain specific kinds of organized criminality, [and] *not* simply to provide additional remedies for already compensable injuries."⁶⁶ Analogizing to the Clayton Act, which was the model for § 1964(c), the Second Circuit concluded that just as an anti-

58. 473 U.S. 479 (1985).

59. *Id.* at 483-85.

60. *Id.*

61. *Id.* at 484.

62. See *Sedima S.P.R.L. v. Imrex Co.*, 574 F. Supp. 963, 965 (E.D.N.Y. 1983) (citation omitted), *aff'd*, 741 F.2d 482 (2d Cir. 1984), *rev'd* 473 U.S. 479 (1985).

63. *Id.*

64. 741 F.2d 482 (2d Cir. 1984) *rev'd*, 473 U.S. 479 (1985).

65. *Id.* at 494.

66. *Id.* (emphasis added).

trust plaintiff must allege an "antitrust injury," a RICO plaintiff must allege a "racketeering injury"—an injury "*different* in kind from that occurring as a result of the predicate acts themselves, or not simply caused by the predicate acts, but also caused by an activity which RICO was designed to deter."⁶⁷ In addition, the Second Circuit found the complaint defective for failure to allege that the defendants had *already* been criminally convicted of the predicated acts of mail and wire fraud or of a RICO violation.⁶⁸

In reversing the Second Circuit's opinion, the United States Supreme Court poignantly stated:

In response to what it perceived to be misuse of civil RICO by private plaintiffs, the court below construed § 1964(c) to permit private actions only against defendants who had been convicted on criminal charges, and only where there had occurred a "racketeering injury." While we understand the court's concern over the consequences of an unbridled reading of the statute, we reject both of its holdings.⁶⁹

After a lengthy review of the legislative history of the private action for treble damages, the Supreme Court held that there was no support in

the statute's history, its language or considerations of policy for a requirement that a private treble-damages action under § 1964(c) can proceed only against a defendant who has already been criminally convicted. To the contrary, every indication is that no such requirement exists. Accordingly, the fact that Imrex and the individual defendants have not been convicted under RICO or the federal mail and wire fraud statutes does not bar Sedima's action.⁷⁰

Moreover, in considering the Second Circuit's prerequisite for a private civil RICO action "injury . . . caused by an activity which RICO was designed to deter"⁷¹—the Supreme Court adopted a *less restrictive* construction of the Act, holding that

67. *Id.* at 496 (emphasis added).

68. *Id.*

69. *Sedima, S.P.R.L. v. Imrex Co.*, 473 U.S. 479, 481 (1985).

70. *Id.* at 493.

71. 741 F.2d 482, 496 (2d Cir. 1984) *rev'd*, 473 U.S. 479 (1985).

[w]here the plaintiff alleges each element of the violation, the compensable injury necessarily is the harm caused by predicate acts sufficiently related to constitute a pattern for the essence of the violation is the commission of those acts in connection with the conduct of an enterprise. Those acts are, when committed in the circumstances delineated in § 1962(c), "an activity which RICO was designed to deter." Any recoverable damages occurring by reason of a violation of § 1962(c) will flow from the commission of the predicate acts.⁷²

Finally, with respect to judicial attempts to limit RICO's reach, the Court stated the following:

We nonetheless recognize that, in its private civil version, RICO is evolving into something quite different from the original conception of its enactors. Though sharing the doubts of the Court of Appeals about this increasing divergence, we cannot agree with either its diagnosis or its remedy. The "extraordinary" uses to which civil RICO has been put appear to be primarily the result of the breadth of the predicate offenses, in particular the inclusion of wire, mail and securities fraud, and the failure of Congress and the courts to develop a meaningful concept of "pattern." We do not believe that the amorphous standing requirement imposed by the Second Circuit effectively responds to these problems, or that it is a form of statutory amendment appropriately undertaken by the courts.⁷³

This judicial philosophy represents the Supreme Court's analysis of RICO's scope in the mid-1980's.⁷⁴

72. *Sedima*, 473 U.S. at 497 (citation omitted).

73. *Id.* at 500 (citations omitted).

74. See also *American Nat'l Bank & Trust Co. v. Haroco, Inc.*, 473 U.S. 606, 608-09 (1985) (rejecting the Seventh Circuit's formulation of a requirement of a distinct RICO injury and holding that a civil claim for treble damages under RICO does not require that the plaintiff have suffered damages by reason of defendant's violation through proscribed predicate offenses; rather, injury from those offenses alone is sufficient).

VI. LIMITING RICO'S REACH: RELUCTANTLY ABANDONING THE "MULTIPLE SCHEMES" TEST WITH A WARNING

Six years after its decision in *Sedima*, the Supreme Court, in *H.J. Inc. v. Northwestern Bell Telephone Co.*,⁷⁵ rejected the judicial philosophy it espoused in *Sedima*, and, like the lower federal courts that it had once admonished, began to limit the reach of RICO as a remedy in response to its perception that RICO had evolved into something beyond the scope of Congress' original intent. Considering the meaning of the phrase "pattern of racketeering" in *H.J., Inc.*, the Supreme Court faced the results of litigation over its earlier dicta in *Sedima*. In *Sedima*, the Court had stated that by requiring "at least two acts of racketeering," Congress had implied "that while two acts are necessary, they may not be sufficient."⁷⁶ As a result of this interpretation, the circuits split in their analyses of RICO cases predicated on mail fraud schemes.⁷⁷ The Eighth Circuit developed a "multiple schemes" test for resolving the dilemma where a pattern could not be established by multiple mailings in furtherance of a single mail fraud scheme.⁷⁸ While noting that the presence of multiple schemes were significant in establishing a requisite pattern, the Court nonetheless rejected the Eighth Circuit's mechanical test.⁷⁹ However, this apparent victory for pro-RICO advocates was illusory.

In *H.J. Inc.*, the petitioners filed a class action suit alleging violations of § 1962(a), (b), (c) and (d), seeking an injunction and treble damages under RICO's civil liability provisions, § 1964(a) and (c). The district court dismissed the complaint pursuant to Rule 12(b)(6) of the Federal Rules of Civil Procedure for failure to state a claim upon which relief could be granted because each of the fraudulent acts alleged was "committed in furtherance of a single scheme" rather than multiple illegal schemes.⁸⁰ The Eighth Circuit affirmed the district

75. 492 U.S. 229 (1989).

76. *Sedima*, S.P.L.R. v. *Imrex Co.*, 473 U.S. 479, 496 & n.14 (1985).

77. *H.J. Inc.*, 492 U.S. at 235 & n.2.

78. *H.J. Inc. v. Northwestern Bell & Tel. Co.*, 829 F.2d 648, 650 (8th Cir. 1987), *rev'd*, 492 U.S. 229 (1989).

79. 492 U.S. at 240-41.

80. *H.J. Inc. v. Northwestern Bell Tel. Co.*, 648 F. Supp. 419, 425 (D. Minn. 1986), *aff'd*, 829 F.2d 648 (8th Cir. 1987), *rev'd*, 492 U.S. 229 (1989).

court's decision, holding that under precedent, a single scheme is insufficient to establish a pattern of racketeering activity.⁸¹ The Supreme Court reversed the Eighth Circuit's decision.⁸²

Rather than give the Act its broadest possible reach as Congress explicitly required, the Court formulated its own "continuity and relationship" test for establishing patterns by giving great weight to isolated remarks within the legislative history.⁸³ Though read as narrowing the scope of the Act, the test actually had little effect on prosecutions under § 1962(c). "Relationship" is almost inherent in RICO cases where the predicate acts are carried out as part of the enterprise's activities or in infiltrating the same. The "continuity" element is met either by the facts or through the use of § 1962(d) to allege that continuity is missing only because the plan was aborted, presumably due to outside factors such as law enforcement intervention or private sleuthing. Thus, the test itself did little to limit the Act's use.

Specifically, in *H.J. Inc.*, the Supreme Court defined relationship in terms of predicate acts "hav[ing] the same or similar purposes, results, participants, victims, or methods of commission, or otherwise [being] interrelated by distinguishing characteristics and . . . not isolated events."⁸⁴ In applying the relationship prong of the pattern requirement, the circuit courts have consistently followed the language of *H.J. Inc.*⁸⁵ In the aftermath of *H.J. Inc.*, the lower federal courts require prosecutors to prove that predicate acts are related and that the acts pose a threat of continued criminal activity.⁸⁶

Continuity has been interpreted by the circuit courts to be a

81. *H.J. Inc.*, 829 F.2d at 650.

82. *H.J. Inc.*, 492 U.S. at 250.

83. *Id.* at 238-39.

84. *Id.* at 240.

85. *See, e.g.*, *Hughes v. Consol-Pennsylvania Coal Co.*, 945 F.2d 594, 609 (3d Cir. 1991) (following *H.J. Inc.* in defining "relationship" for proof of pattern of racketeering activity); *Terry A. Lambert Plumbing v. Western Sec. Bank*, 934 F.2d 976, 979-80 (8th Cir. 1991) (quoting language of *H.J. Inc.* in defining "relationship").

86. *See, e.g.*, *United States v. Dischner*, 974 F.2d 1502, 1509 (9th Cir. 1992) (stating that a relationship plus continuity "formula" has been adopted to prove pattern of racketeering activity); *United States v. Pelullo*, 964 F.2d 193, 207 (3d Cir. 1992) (following *H.J. Inc.*, and stating that relationship and continuity are required to prove a pattern of racketeering activity).

temporal concept, referring either to a closed-ended period of continuous commission of predicate acts or to an open-ended period that, by its nature, will project into the future.⁸⁷ The circuit courts have not determined a specific length of time that is sufficient to fulfill the continuity requirement of closed-ended racketeering activity. For example, the First Circuit has held that commission of predicate acts over a period of six years is sufficient to establish continuity.⁸⁸ The Third Circuit, however, has found that predicate acts done within a limited time period of seven months is not sufficient for continuity.⁸⁹

The true significance of *H.J. Inc.* can be found not in the holding but in the concurring opinion of Justice Scalia, wherein he was joined by the Chief Justice, Justice O'Connor and Justice Kennedy. The concurring opinion criticized the continuity plus relationship test as being "about as helpful [to the lower courts in interpreting the Act] as 'life is a fountain.'"⁹⁰ Justice Scalia then wrote "[i]t is, however, unfair to be so critical of the Court's effort, because I would be unable to provide an interpretation of RICO that gives significantly more guidance concerning its application."⁹¹

87. See, e.g., *Pelullo*, 964 F.2d at 208 (holding that continuity is determined on a case-by-case basis considering whether the activity was closed- or open-ended); *United States v. Stodola*, 953 F.2d 266, 270 (7th Cir. 1992) (stating that continuity is a temporal concept).

88. *United States v. Ruiz*, 905 F.2d 499, 504-05 (1st Cir. 1990) (finding that continuity was proven by predicate acts of narcotics trafficking over a period of six years).

89. *Marshall-Silver Const. Co. v. Mendel*, 894 F.2d 593, 597 (3d Cir. 1990) (finding that an attempt, over a period of seven months, to ruin plaintiff's reputation by forcing him into bankruptcy did not satisfy continuity requirement). The Sixth Circuit has held that a prosecutor may also establish continuity by proving the threat of continued criminal activity in the future. *United States v. Busacca*, 936 F.2d 232, 237-38 (6th Cir. 1991). This threat may be established "by showing that the related predicates themselves involve a distinct threat of long term racketeering activity, either implicit or explicit, or by showing that the predicate acts or offenses are a part of an ongoing entity's regular way of doing business." *Id.* at 238. See also *United States v. O'Connor*, 910 F.2d 1466 (7th Cir. 1990) (finding police officer's acceptance of a number of bribes over a period of two months sufficient to fulfill the closed-ended continuity requirement). The racketeering activity does not necessarily have to be of a long duration if the threat of continued racketeering activity is projected into the future.

90. *H.J. Inc.*, 492 U.S. at 252 (Scalia, J., concurring).

91. *Id.* at 254-55 (Scalia, J., concurring).

Justice Scalia then sent a warning on behalf of four members of the Court. Relying on Justice Marshall's dissent in *Sedima*, Justice Scalia invited a constitutional challenge of RICO by suggesting that the pattern requirement may be impermissibly vague. Justice Scalia's frustration is evident from his statement, "[t]hat the highest Court in the land has been unable to derive from this statute anything more than today's meager guidance bodes ill for the day when that challenge is presented."⁹² This message sent shockwaves through the RICO plaintiff's bar. It was particularly unexpected given the Court's decision in *Fort Wayne Books, Inc. v. Indiana*,⁹³ where the Court rejected a constitutional vagueness challenge to the Indiana RICO statute which had been patterned on the federal law.⁹⁴

How could a statute once viewed as broad but clear suddenly be in danger of being held unconstitutionally vague? Though of the litigation will continue on the "vagueness issue" as a result of *H.J. Inc.*, the lower courts thus far have rejected such challenges.⁹⁵ The Supreme Court, however, had set the stage for giving legal significance to its displeasure with RICO.

VII. REVES V. ERNST & YOUNG: THE CHILLING EFFECT ON CRIMINAL PROSECUTIONS

A. *Facts of the Case*

The civil law suit in *Reves v. Ernst & Young*⁹⁶ was brought by the trustee in bankruptcy of the Farmer's Cooperative of Arkansas and Oklahoma, Inc. (the "Co-op") and certain noteholders against forty individuals and entities, including Arthur Young and Company,⁹⁷ the Co-op's accountant. The

92. *Id.* at 255-56 (Scalia, J., concurring).

93. 489 U.S. 46 (1989).

94. *Id.* at 57-58.

95. *See*, United States v. Ashman, 979 F.2d 469, 487 (7th Cir. 1992).

96. 113 S. Ct. 1163 (1993). Like the court at summary judgment, we do not consider likely the factual defenses presented by Arthur Young.

97. *Reves*, 113 S. Ct. at 1168. The Co-op hired Russell Brown and Company to perform its financial audit in 1981. On January 2, 1992, Russell Brown and Company merged with Arthur Young and Company. Arthur Young and Company later became respondent Ernst & Young. *Id.* at 1167. For clarity, we hereinafter refer to the respondent as "Arthur Young".

trustee's suit alleged, among other things, that Arthur Young's financial statements for the Co-op were fraudulent in violation of § 1962(c).⁹⁸

As the Co-op's auditor, one of Arthur Young's first duties was to determine the fixed asset value of White Flame Fuels, Inc. ("White Flame" or "the Company"), a company allegedly purchased by the Co-op in February of 1980.⁹⁹ Although the Co-op's 1980 financial statement gave no fixed asset value for White Flame,¹⁰⁰ Arthur Young "essentially invented"¹⁰¹ a figure identical to the fraudulent figure that the Company's prior, and now convicted, accountant had previously created.

Second, Arthur Young had to determine how the Company's value should be treated for accounting purposes.¹⁰² If the Co-op had owned the company from its formation in 1979, the Company's value for accounting purposes would have been its fixed-asset value of \$4.5 million.¹⁰³ If the Co-op had purchased the Company in February of 1980, it would have to be given its fair market value at the time of purchase: somewhere between \$444,000 and \$1.5 million.¹⁰⁴ If the Company was valued at less than \$1.5 million, the Co-op was insolvent.¹⁰⁵

Although the Co-op's 1980 financial statement *and* a local court consent decree indicated that the Co-op did not acquire White Flame until February of 1980, Arthur Young, on its own volition, made representations that the Co-op had acquired White Flame in May of 1979. Thus, for accounting purposes, Arthur Young represented that the Company's fixed asset value was \$4.5 million.¹⁰⁶

Basing the audit on these facts, not only did Arthur Young present its 1981 audit report to the Co-op's board, but it failed to tell the board of its conclusion that the Co-op had owned White Flame since its creation in 1979 and that, without that

98. *Id.* at 1168.

99. *Id.* at 1167.

100. *Id.* at 1176 (Souter, J., dissenting).

101. *Id.* (Souter, J., dissenting).

102. *Id.* at 1167.

103. *Id.*

104. *Id.*

105. *Id.*

106. *Id.*

conclusion, the Co-op was insolvent.¹⁰⁷ At the 1982 annual meeting of the Co-op, Arthur Young distributed condensed financial statements to the members.¹⁰⁸ These condensed financial statements included White Flame's contrived \$4.5 million asset value among its total assets. Once again, Arthur Young omitted relevant information as to the Co-op's real financial status.¹⁰⁹ Finally, in the 1982 audit report presented to the board, Arthur Young reported the value of White Flame as being approximately \$4.5 million and made representations that it was responsible for the Co-op showing a positive net worth.¹¹⁰ A condensed financial statement was distributed by Arthur Young at the Co-op's annual meeting in 1983. At the 1983 annual meeting, Arthur Young once again failed to state that the Co-op was in grave financial danger if White Flame were written down to its fair market value.¹¹¹

On February 23, 1984, the Co-op filed for bankruptcy.¹¹² On February 14, 1985, the trustee in bankruptcy filed suit.¹¹³

B. *The District Court Decision*

The district court granted summary judgment in favor of Arthur Young on the RICO claim. Applying the "operation or management" test established in *Bennett v. Berg*,¹¹⁴ the district court ruled that,

Plaintiffs have failed to show anything more than that the accountants reviewed a series of completed transactions and certified the Co-op's records as fairly portraying its financial status as of a date three or four months preceding the meetings of the directors and the shareholders at which they presented their reports. We do not hesitate to declare

107. *Id.*

108. *Id.*

109. *Id.* at 1167-68.

110. *Id.* at 1168.

111. *Id.*

112. *Id.*

113. *Id.*

114. 710 F.2d 1361, 1364 (8th Cir. 1983) (en banc), *cert. denied*, 464 U.S. 1008 (1983) (requiring "some participation in the operation or management of the enterprise itself").

that such activities fail to satisfy the degree of management required by *Bennett v. Berg*.¹¹⁵

Therefore, the district court found that because the conduct engaged in by Arthur Young did not meet the "operation or management" test of the Eighth Circuit, Arthur Young did not "conduct or participate, directly or indirectly, in the conduct of" the Co-op's affairs pursuant to § 1962(c).

C. *The Circuit Court Decision*

The United States Court of Appeals for the Eighth Circuit affirmed the district court's decision to grant summary judgment in favor of Arthur Young on the RICO claim.¹¹⁶ Ironically, the court of appeals characterized Arthur Young's conduct merely as being "limited to the audits, meetings with the Board of Directors to explain the audits, and presentations at the annual meeting."¹¹⁷ Thereafter, the court of appeals stated that "[i]n the course of this involvement it is clear that Arthur Young committed a number of reprehensible acts"¹¹⁸ Nevertheless, like the district court, the Eighth Circuit applied its "operation or management" test as articulated in *Bennett v. Berg* and held that Arthur Young's conduct "in no way . . . [rose] to the level of participation in the management or operation of the Co-op"¹¹⁹ required for a RICO violation.¹²⁰

115. *Reves v. Ernst & Young*, 113 S. Ct. 1163, 1168, (1993) (citing *Robertson v. White*, 113 F.R.D. 20 (W.D. Ark. 1986)).

116. *Arthur Young & Co. v. Reves*, 937 F.2d 1310, 1339-40 (8th Cir. 1991), *aff'd sub nom.*, *Reves v. Ernest & Young*, 113 S. Ct. 1163 (1993).

117. *Arthur Young & Co.*, 937 F.2d at 1324.

118. *Id.*

119. *Id.* (emphasis added). It is not clear, however, that the Eighth Circuit agreed with the test as articulated in *Bennett*. For example, in response to the plaintiffs' contention that the court of appeals should follow the Eleventh Circuit's decision in *Bank of Am. Nat'l Trust & Sav. Ass'n v. Touche Ross & Co.*, 782 F.2d 966, 970 (11th Cir. 1986), not imposing a requirement that a RICO defendant participate in the management or operation of the enterprise, the Eighth Circuit stated, "[w]e are aware of the inconsistencies between the circuits regarding the necessary level of participation for RICO liability But until the Supreme Court rejects our standard or this court en banc overrules *Bennett*, we are bound to follow that decision." *Arthur Young & Co.*, 937 F.2d at 1324.

120. *Arthur Young & Co.*, 937 F.2d at 1324.

D. *The Supreme Court Wrongly Decided Reves v. Ernst & Young*

The Supreme Court's conclusion in *Reves* that in order "to conduct or participate, directly or indirectly, in the conduct of" an enterprise's affairs under § 1962(c), one must participate in the operation or management of the enterprise itself is flawed in several respects. First, the Supreme Court's construction and use of the term "conduct" in § 1962(c) fails to recognize that the term is used twice, first as a verb and then as a noun. In terms of context, by failing to recognize these two uses of the term as they appear in the Act, the Court creates a nonexistent congressional limitation of liability under § 1962(c) for those who participate in the operation or management of an enterprise itself. Thus, the Supreme Court, rather than Congress, has in effect, amended § 1962(c) by importing an "operation or management test" into the statute. Second, even assuming *arguendo* that an "operation or management" test is appropriate, the Court clearly misapplies the test to the facts presented in this case. As a result, the floodgates of the federal courts are now open for use of this test as a defense in not only civil RICO litigation, but also criminal prosecutions brought under § 1962(c).

1. The Supreme Court's Analysis of *Reves*

The Supreme Court's analysis of Arthur Young's liability ignores alternative plain meanings of the words "conduct" and "participate" which mandated the opposite result of *Reves*' actual outcome. The majority concluded that the term "conduct," when used as a noun, signifies a high degree of direction or control in § 1962(c) sufficient for Arthur Young's allegedly fraudulent conduct to escape liability under the Act. In reaching this conclusion, the Supreme Court ignored the two uses of the term "conduct" in § 1962(c), that when read together, clearly import *no* degree of direction or control under the Act. Furthermore, the Court failed to consider the numerous acts of Arthur Young, which on their face, could arguably fall within the pur-

view of the "operation or management" test to which the Court has given birth.¹²¹

In *Reves*, the only portion of the appellate court's decision at issue was its affirmation of summary judgment granted to Arthur Young on the RICO claim. The Supreme Court took issue with the district court and the Eighth Circuit's application of the "operation or management" test articulated in *Bennett v. Berg*.¹²² The Court also attempted to resolve the conflict between the D.C. Circuit and the Eleventh Circuit in *Yellow Bus Lines, Inc. v. Drivers, Chauffeurs & Helpers Local Union 639*¹²³ and *Bank of America National Trust v. Touche Ross & Co.*¹²⁴ The issue as the Court stated, was "the meaning of the

121. The Court's application of its "operation or management" test to the alleged conduct engaged in by Arthur Young in *Reves* clearly recognized the negative impact that the undisciplined use of civil RICO against accounting firms can have on the relationship between an accounting firm and its clients. More likely than not, absent the knowing involvement of upper management, accounting firms such as Arthur Young should be shielded from the use of RICO for the very conduct at issue in *Reves*. However, that issue is not one which should have been resolved by the Supreme Court. Rather, it is a decision which should be made by the legislature. For this reason, the Supreme Court's conclusion regarding Arthur Young's conduct in *Reves* may have brought about the right result for the wrong reason, albeit a reason with unforeseen consequences to RICO's use in the future.

122. 710 F.2d 1361 (8th Cir. 1983).

123. 913 F.2d 948, 954 (D.C. Cir. 1990) (en banc), *cert. denied*, 111 S. Ct. 2839 (1991). The D.C. Circuit construed the "operation or management" test as follows:

Conduct is synonymous with "management" or "direction." The "conduct of [the enterprise's] affairs" thus connotes more than just some relationship to the enterprise's activity; the phrase refers to the guidance, management, direction or other exercise of control over the course of the enterprise's activities. In order to participate in the conduct of an enterprise's affairs, then, a person must participate, to some extent, in "running the show." . . . Section 1962(c) applies when a defendant, through a pattern of racketeering activity, exercises significant control over or within an enterprise, participating not merely in the enterprise's affairs, but in the conduct of the enterprise's affairs. Most often the participation requirement will be satisfied when a defendant either participates in directing the enterprise toward its preexisting goals or participates in exercising control over an enterprise so as to reset its goals.

Id. (alteration in original) (citations omitted).

124. 782 F.2d 966, 970 (11th Cir. 1986). The Eleventh Circuit construed the "operation or management" test as follows:

RICO does not require [a large] degree of participation [as] urged by the defendants. It is not necessary that a RICO defendant participate in the management or operation of the enterprise. On its face, the statute requires only that the defendant "participate, directly or indirectly in the conduct of [the] enterprise's affairs" . . . The word "conduct" in § 1962(c)

phrase 'to conduct or participate, directly or indirectly in the conduct of such enterprise's affairs.'¹²⁵ Obviously, the word "conduct" is used twice. However, the Court found that in using the word "conduct" first as a verb and second as a noun, it seemed more "reasonable to give each use a similar construction."¹²⁶ The Court found that as a verb, "conduct" means to "lead, run, manage, or direct."¹²⁷ Rejecting petitioner's request that the Court read "conduct" as "carry on," the Court found that "context is important, and the context of the phrase 'to conduct . . . [an] enterprise's affairs,' . . . indicates some degree of direction."¹²⁸

The Court stated that "[t]he more difficult question is what to make of the word 'participate.'¹²⁹ The Court found that in the context of § 1962(c), "participate" "appears to have a narrower meaning."¹³⁰ Thus the Court defined "participate" by stating:

We may mark the limits of what the term might mean by looking again at what Congress did *not* say. On the one hand, "to participate . . . in the conduct of . . . affairs" must be broader than "to conduct affairs" or the "participate" phrase would be superfluous. On the other hand, as we have already noted, "to participate . . . in the conduct of . . . affairs" must be narrower than "to participate in affairs" or Congress' repetition of the word "conduct" would serve no purpose. It seems that Congress chose a middle ground, consistent with a common understanding of the word "participate"—"to take part in."¹³¹

The Court ultimately found the "operation or management" test in § 1962(c) to mean that in order to participate, directly or indirectly, in the conduct of prohibited enterprises affairs,

simply means the performance of activities necessary or helpful to the operation of the enterprise.

Id. at 970. (citations omitted).

125. *Reves v. Ernst & Young*, 113 S. Ct. 1163, 1169 (1993).

126. *Id.* (citing *Sorenson v. Secretary of the Treasury*, 475 U.S. 851, 860 (1986)).

127. *Reves*, 113 S. Ct. at 1169 (citing WEBSTER'S THIRD NEW INTERNATIONAL DICTIONARY, 474 (3d ed. 1976)).

128. *Reves*, 113 S. Ct. at 1169.

129. *Id.* at 1170.

130. *Id.* (citations omitted).

131. *Id.* (citations omitted) (emphasis added).

one must have some part in directing those affairs.¹³² Because the Court could not conclude that Arthur Young “participated” in the operation or management of the Co-op itself, the accounting firm was not liable under § 1962(c).¹³³

2. The Souter Dissent

Interestingly, while the majority of the Court found a “clear” congressional mandate in the word “conduct” to limit § 1962(c) liability to participants in the operation or management of a RICO enterprise, Justice Souter, with whom Justice White joined in dissent, found the exact opposite.¹³⁴ Souter found the statute’s liberal construction clause “not irrelevant, but dispositive.”¹³⁵ Furthermore, even if he were to assume that the word “conduct” imports a degree of direction or control into § 1962(c), “[Justice Souter] would have to say that the majority misapplies its own ‘operation or management’ test to the facts presented here.”¹³⁶

Justice Souter correctly pointed out that the term “conduct” does not necessarily imply control because:

[t]he term, when used as noun, is defined by the majority’s chosen dictionary as, for example, “carrying forward” or “carrying out” . . . [Section] 1962(c) covers not just those “employed by” an enterprise, but those merely “associated with” it, as well . . . [A]ssociates (like employees) are prohibited not merely from conducting the affairs of an enterprise through a pattern of racketeering, not merely for participating directly in such unlawful conduct, but even from indirect participation in the conduct of an enterprise’s affairs in such a manner. The very breadth of this prohibition renders the majority’s reading of “conduct” rather awkward, for it is hard to imagine how the “operation or management” test would leave the statute with the capacity to reach the indirect participation of someone merely associated with an enterprise [T]his contextual examination

132. *Id.* at 1169-74.

133. *See id.* at 1174.

134. *See* Pub. L. No. 91-452, § 904, 84 Stat. 941 (1970) (“The provisions of this title shall be liberally construed to effectuate its remedial purposes.”).

135. *Reves*, 113 S. Ct. at 1174 (Souter, J., dissenting).

136. *Id.* (Souter, J., dissenting).

shows "conduct" to have a long arm, unlimited by any requirement to prove that the activity includes an element of direction. But at the very least, the full context is enough to defeat the majority's conviction that the more restrictive interpretation of the word "conduct" is clearly the one intended.¹³⁷

Nevertheless, even assuming *arguendo* that the majority's reading of § 1962(c)'s operation or management test is correct, Justice Souter correctly points out that even under the majority's view, Arthur Young violated the statute.¹³⁸ Several facts support this point:

1. Arthur Young did not confine itself in this case to the role traditionally performed by an outside auditor;
2. Arthur Young created the very financial statements it was hired to audit; and
3. Arthur Young took on management responsibilities by deciding, in the first instance, what value to assign to the Co-op's most important fixed asset, White Flame.

Under the American Institute of Certified Public Accountants' Code of Professional Conduct, Arthur Young arguably abandoned the normal activities of an auditor and took on responsibility in managing the Co-op's affairs by engaging in this conduct. Thus, even under the majority's "operation or management test," Arthur Young crossed the line separating outside

137. *Id.* at 1174-75 (Souter, J., dissenting) (citations omitted).

138. *Id.* at 1175-77 (Souter, J., dissenting). The American Institute of Certified Public Accountants' ("AICPA"), Code of Professional Conduct indicates that management has responsibility for the content of financial statements. The auditor "simply expresses an opinion on the client's financial statements." *Id.* at 1175-76 (Souter, J., dissenting) (citing Brief for Respondent at 30). The auditors' code provides as follows:

The financial statements are management's responsibility. The auditor's responsibility is to express an opinion on the financial statements. Management is responsible for adopting sound accounting policies and for establishing and maintaining an internal control structure that will, among other things, record, process, summarize, and report financial data that is consistent with management's assertions embodied in the financial statements The independent auditor may make suggestions about the form or content of the financial statements or draft them, in whole or in part, based on information from management's accounting system.

Codification of Accounting Standards and Procedures, Statement on Auditing Standards No. 1, § 110.02 AM. INST. OF CERTIFIED PUB. ACCOUNTANTS (1972).

auditors from inside financial managers and should have been held answerable under § 1962(c).¹³⁹

VIII. USE OF RICO BY THE JUSTICE DEPARTMENT AND THE EFFECT OF *REVES* ON CRIMINAL PROSECUTIONS

RICO is the most effective tool a prosecutor has in unraveling organized crime in the United States today.¹⁴⁰ The Justice Department effectively uses RICO to prosecute a broad range of crimes such as government corruption, white collar crime, labor corruption, and concerted criminal activity like narcotics trafficking and arson.¹⁴¹ RICO provides incentives to agents of the Federal Bureau of Investigation to conduct investigations into organized crime by assuring agents that a successful investigation will probably lead to a RICO prosecution that may effectively remove an entire crime family from operating in a city.¹⁴² For example, a successful RICO prosecution led to the demise of the Nicodemo Scarfo family in Philadelphia.¹⁴³

RICO has also been extremely effective in attacking government corruption. For example, the United States Attorney's Office for the Northern District of Illinois used RICO in "Operation Greylord" to successfully prosecute corrupt judges, attorneys, court clerks and police officers that were involved in schemes to fix cases in the Cook County state court system.¹⁴⁴ White collar crime is effectively prosecuted using RICO in insid-

139. *Reves*, 113 S. Ct. at 1178.

140. Paul E. Coffey, *The Selection, Analysis, and Approval of Federal RICO Prosecutions*, 65 NOTRE DAME L. REV. 1035, 1038 (1990) (describing method used in deciding to bring a RICO case by the Organized Crime and Racketeering Section, Criminal Division of the Department of Justice).

141. Lynch, *supra* note 7, at 735.

142. Coffey, *supra* note 140, at 1038.

143. *See* United States v. Pungitore, 910 F.2d 1084 (3d Cir. 1990) (affirming criminal RICO convictions of fourteen defendants, all members of the Scarfo crime family).

144. *See, e.g.*, United States v. LeFevour, 798 F.2d 977 (7th Cir. 1986) (convicting judge under RICO for taking bribes to fix traffic infractions and allowing attorneys to gain clients by soliciting potential defendants on the courthouse steps); United States v. Conn, 769 F.2d 420 (7th Cir. 1985) (holding a court clerk was guilty under RICO for soliciting and taking bribes to influence public officials); United States v. Murphy, 768 F.2d 1518 (7th Cir. 1985) (convicting judge for taking bribes in connection with cases involving drunk driving, battery and felony theft).

er trading cases and criminal fraud, such as mail, wire and securities fraud.¹⁴⁵ For example, Alfred Elliott, an attorney, was convicted under § 1962(c) of securities and mail fraud in *United States v. Elliott*.¹⁴⁶

Since RICO has become law, § 1962(c) has been, and remains, the most effective subsection the Justice Department has used in successfully prosecuting criminal RICO allegations.¹⁴⁷ According to officials at the Justice Department, of the 914 cases brought by the Department since 1984, 898, or ninety-eight percent of the indictments included § 1962(c) violations.¹⁴⁸ Forty-three percent of these RICO cases solely involved violations of § 1962(c).¹⁴⁹ Section 1962(d) prohibits a defendant from conspiring to commit any of the acts described in subsections (a),(b) or (c). The Justice Department has coupled subsection (d) with subsection (c) in 463 or fifty-one percent of all the RICO indictments since 1984.¹⁵⁰ The prosecutor normally alleges that the defendants conspired to violate subsection (c). The Justice Department has only coupled subsection (d) with either subsection (a) or (b) in nine cases since 1984.¹⁵¹

Prosecutors have simply found that bringing a RICO indictment under § 1962(c) is easier and more effective as compared to subsections (a) and (b). Subsection (a) is not often used because a prosecutor must prove that a defendant actually invested or used racketeering proceeds in an enterprise.¹⁵² As decided in *American National Bank & Trust Co. v. Haroco, Inc.*¹⁵³ and *Yellow Bus Lines, Inc. v. Drivers, Chauffeurs & Helpers Local Union 639*¹⁵⁴ a defendant cannot be charged *both* as the enterprise *and* as the person conducting the racketeering activi-

145. Edward S.G. Dennis, Jr., *Current RICO Policies of the Department of Justice*, 43 VAND. L. REV. 651, 653 (1990).

146. 727 F. Supp. 1131 (N.D. Ill. 1989).

147. Lynch, *supra* note 7, at 731.

148. Interview with the Office of Public Affairs, The United States Department of Justice, in Washington, D.C. (July 9, 1993).

149. *Id.*

150. *Id.*

151. *Id.*

152. See, e.g., *Busby v. Crown Supply, Inc.*, 896 F.2d 833, 837 (4th Cir. 1990) (holding that receipt of income from a pattern of racketeering activity and investment of this income in an enterprise must be proven under § 1962(a)).

153. 473 U.S. 606 (1985).

154. 913 F.2d 948 (D.C. Cir. 1990), *cert. denied*, 111 S. Ct. 2839 (1991).

ty. In *Yellow Bus Lines*, the District of Columbia Circuit stressed that the purpose of RICO is to prevent organized crime and other racketeering activity from infiltrating the legitimate business community.¹⁵⁵ Also, because subsection (a) is convoluted, instructing a jury on the elements of the subsection is difficult.

Subsection (b) is not often used because it is fact-specific. The prosecutor must prove ownership of the enterprise, an irrelevant element when prosecuting many RICO cases. In government corruption cases the enterprise is the government and a government official cannot own the government itself. Moreover, in circumstances in which a prosecutor proves that an enterprise is an association-in-fact, it is often difficult to prove actual ownership of that enterprise.

Under subsection (c), the prosecutor does not have to prove an investment or use of racketeering proceeds or actual ownership of an enterprise. The prosecutor must only prove that a person has conducted or participated, "directly or indirectly," in the racketeering affairs of an enterprise. This easier burden is the reason that subsection (c) has been the most effective subsection of § 1962 since its enactment in 1970. Since *Turkette* allows an enterprise to be considered an association-in-fact, the Justice Department has been able to bring additional cases under subsection (c).

Decisions in civil RICO affect governmental use of the statute.¹⁵⁶ Although the *Reves* case was a private civil RICO action, it will still affect the Justice Department's ability to bring criminal indictments because the RICO statute is an integrated whole.¹⁵⁷

155. *Id.* at 954 (stating that entire RICO statute is limited to prevention of corrupt acquisition of legitimate business).

156. Dennis, *supra* note 145, at 655. In deciding the civil RICO case, *H.J. Inc. v. Northwestern Bell Tel. Co.*, 829 F.2d 648 (8th Cir. 1987), *rev'd*, 492 U.S. 299 (1989), the Eighth Circuit held that a "pattern of racketeering activity" could only be proven by establishing the existence of multiple schemes. Although the standard was eventually reversed by the Supreme Court, the Justice Department virtually stopped its use of criminal RICO in the Eighth Circuit.

157. Michael Goldsmith, *RICO and Enterprise Criminality: A Response to Gerard E. Lynch*, 88 COLUM. L. REV. 774, 790 (1988).

IX. THE AFTERMATH OF *REVES*

Congress could easily look at the effect of *Reves* and *H.J. Inc.* and recognize that its intent is in danger of being frustrated. A corrective response is unlikely, however. For years, the Justice Department has unsuccessfully sought enhancement of the Hobbs Act,¹⁵⁸ and forfeiture authority in mail fraud cases. In fact, the most recent legislative fix undertaken on behalf of prosecutors was the 1988 passage of 18 U.S.C. § 1346 as a response to the Supreme Court's limitation of mail fraud prosecutions in *McNally v. United States*.¹⁵⁹

Though the circuits continue to affirm RICO convictions notwithstanding the dicta in *H.J. Inc.*¹⁶⁰ the practical effects of *Reves* have yet to be felt. Once again, imagine the prosecutor considering whether to bring charges against the bank president and the mafia foot soldier. The bank president's case is a fairly easy one to decide whether to prosecute. Congress has added § 1344 as a RICO predicate offense so that bank crimes are plainly within the intended reach of the Act. Selecting an appropriate enterprise to charge is however, made more difficult by *Reves*. The regulatory agency which is victimized by the misrepresentations is not an appropriate enterprise to charge because the bank president can hardly be said to exercise management or control of the regulatory agency. Similarly, the bank president does not control Congress.¹⁶¹ Yet, the president of a bank plainly manages and controls that institution so the bank may be charged as the enterprise. Thus, *Reves* is ultimately no impediment to this prosecution.

The mafia foot soldier, however, is more difficult to prosecute. *Turkette* taught us that RICO's scope includes illegitimate enterprises, encompassing as broad an array of racketeering activity as possible. The soldier's efforts to infiltrate a legitimate business will not be sufficient to give him control or manage-

158. 18 U.S.C. § 1951 (1988).

159. 483 U.S. 350 (1987).

160. See *United States v. Ashman*, 979 F.2d 469, 487 (7th Cir. 1992).

161. Indeed, one almost wonders whether Congress anticipated *Reves* with approval, as one could argue that no one manages or controls Congress. Thus, Congress, unlike several local and state legislative bodies, would never serve as a RICO "enterprise."

ment of the business until he is successful. It is unlikely that Congress intended for this type of criminal activity to succeed before it became actionable under RICO, but that may be the result of *Reves*.

The soldier in an organized crime family does not control or manage the affairs of the godfather's enterprise — the godfather does. The soldier follows orders. If the United States charged the "family" as the enterprise, the soldier would have a defense based on his absence of control under *Reves*. Charging the soldier as part of an "association-in-fact" enterprise will doubtless be the prosecutors' solution to this dilemma. Yet, it is an imperfect solution. Under *American National Bank & Trust Co. v. Haroco, Inc.*,¹⁶² the association-in-fact cannot be both defendant and enterprise (defendants merely conducting their own affairs). Consequently, the association-in-fact will need to become more than the sum of its parts to meet the required "entity" status. Moreover, it is curious that prosecutors will be forced to redefine their enterprises to satisfy *Reves*, where, as in the hypothetical case, the more obvious enterprise is hierarchical.

X. CONCLUSION

While creative prosecutors will no doubt find a way around this dilemma, one wonders why it had to become a problem at all. For years, bribe payers have been prosecuted under RICO for conducting the affairs of government enterprises whose affairs they never managed and only controlled at an insignificant level. The securities salesman who commits fraud in the sale of securities "carries-on" the affairs of his brokerage house but he does not manage or control the house. Given the breadth of RICO and the clear congressional directive to interpret it broadly, one has to conclude that the Court in *Reves* adopted the "management or control" test in order to limit RICO. Such a policy determination has generally been left by the Court to Congress. Justice Souter was correct in his analysis; perhaps some day the Court will reconsider its decision in *Reves*.

162. 473 U.S. 606 (1985).

