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Statement of Ray J. Groves, Chairman, before the Criminal Justice Subcommittee of the Committee on the Judiciary U.S. House of Representatives, June 12, 1985

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Mr. Chairman, Members of the Subcommittee, I am Ray J. Groves, Chairman of the American Institute of Certified Public Accountants. Accompanying me are Philip B. Chenok, President of the Institute, Theodore C. Barreaux, AICPA Vice President in charge of our Washington office and AICPA Special Counsel Phillip A. Lacovara of the firm of Hughes, Hubbard and Reed.

The AICPA is the national professional organization of certified public accountants (CPAs) in the United States. Its service to the profession and to the public spans almost one hundred years. Today, membership consists of over 230,000 CPAs in public practice, in industry, in education and in government. The Institute is widely recognized as the authoritative voice of the accounting profession.

The purpose of these hearings is to consider H.R. 2517, a bill introduced by the distinguished Chairman of this Subcommittee to amend the Racketeer Influenced and Corrupt Organizations Act (RICO). As you know, the bill would alter the criminal provisions of the RICO statute. The AICPA has neither experience nor any claim of expertise with respect to such matters. Consequently, we cannot offer the Committee any counsel on the wisdom of the proposed changes to the criminal aspects of RICO. Rather, our purpose here today is to ask the Committee to broaden its focus to examine the civil RICO portion of the statute, specifically Section 1964(c) of Title 18. On this matter, we have considerable first-hand knowledge that reform is urgently required.

The civil RICO remedy was incorporated in the original legislation in 1970 with little discussion or apparent analysis. It allows any victim of so-called "racketeering" to sue in federal court and recover three times damages, plus attorney's fees. With increasing frequency, this seemingly meritorious device for redressing the wrongs of organized crime has been turned against ordinary businesses -- the very people the act intended to protect. Among those who have found themselves targeted by racketeering allegations -- and please remember it only needs to be alleged that criminal violations have occurred -- have been this nation's leading and most respected accountants, banks, insurance companies, securities firms, and many other legitimate business people.

This Subcommittee is well aware of the nature of a RICO claim and it would serve no useful purpose to detail all of its elements. To put our statement in the proper context, it should merely be noted that the commission of any two proscribed acts within a ten-year period triggers the statute and the availability of the treble damage claim. Some of these so-called "predicate" offenses are those of a hard-core nature often associated with organized crime: murder, kidnapping, extortion and arson. But also included are some offenses subject to broad interpretation such as mail and wire fraud and fraud in the sale of securities. Allegations of fraud can be easily framed in almost any business transaction gone awry.

And this is exactly what has happened in the RICO arena. The statute is now being invoked in every kind of litigation where "fraud" can possibly be alleged. In fact, the use of civil RICO becomes more ludicrous every day, encompassing breach of contract actions, commonplace landlord-tenant or real estate disputes, product liability actions, wrongful discharge from employment cases, matrimonial controversies and even religious disputes.

Moreover, the mere allegation of pervasive criminality, as the statute requires, is damaging. Few professionals or businesses dependent on maintaining a reputation for integrity dare risk the harm that may result from publicity about those allegations, even if you are confident that the litigation will prove unsuccessful. Being innocent is not enough. The ability to label a defendant "a racketeer" by the initiation of litigation, coupled with the legal costs of defending against such a case and the potential of treble damages, exerts powerful pressures to induce a settlement. These pressures would not be significantly lessened, we fear, if the "racketeering" label is simply changed to a "pattern of criminality."

It should be noted that in 1970, when the House Judiciary Committee reported the Organized Crime Control Act (P.L. 91-644), the chairman of this subcommittee, along with then Representatives Mikva (D-Ill.) and Ryan (D-N.Y.), opposed

the treble damage section of the civil RICO provisions in the 1970 legislation as follows:

> ...[S]ection 1964(c)...provides invitation for disgruntled and malicious competitors to harass innocent businessmen engaged in interstate commerce by authorizing private damage suits....what a protracted, expensive trial may not succeed in doing, the adverse publicity may well accomplish -- destruction of the rival's business. (House of Representatives Rep. No. 1549, 91st Cong. 2d Sess. (1970), at 187.)

With hindsight, Mr. Chairman, we all regret that your colleagues in the House and those in the Senate failed to heed this admonition.

The bill from which the Organized Crime Control Act of 1970 (including the RICO title) was derived, had originated in the Senate and contained no civil provision when introduced or when initially passed by the Senate. The object of the legislation was to enhance the government's arsenal in the war against organized crime, not to create new remedies for commercial disputes. The Senate Report on the bill clearly stated the bill's precise purposes:

> The eradication of organized crime in the United States by strengthening the legal tools in the evidence gathering process, by establishing new penal prohibitions, and by providing enhanced sanctions and new remedies to deal with the unlawful activities of those engaged in organized crime. (S. Rep. No. 90-617, 91st. Cong. 1st Sess. at 2 (1969)).

In this vein, Senator McClellan, the chief sponsor, focused his arguments for the bill on the activities of "La

Cosa Nostra." In particular, he was concerned that when "organized crime moves into a business, it usually brings to that venture all the techniques of violence and intimidation which is used in its illegal business." 115 Cong. Rec. 5872 (1969). However, Congress was concerned that any attempt to define "organized crime" per se in the statute -- as Senator McClellan had attempted to do in earlier legislation introduced in the 90th Congress -- would encounter constitutional difficulties. Accordingly, Senator McClellan instead endorsed an approach that would create a broad list of predicate offenses, including various types of fraud, because organized crime had shown great flexibility in branching into additional illegal activities and "if we name one crime they will commit another". Congress, the Senator explained, could not "anticipate everything"; it would "have to make a statute general" 116 Cong. Rec. 845-846 (1970). The Department of Justice, which was to have exclusive authority to enforce the statute, would thus have to channel the statute to its intended target: organized crime. These broad provisions could not have been intended to invite civil litigation against legitimate businessmen, since the Senate bill did not even authorize private suits.

With little discussion, the private civil remedy, with its provision for treble damages and attorneys' fees, was later added to the legislation in the House Judiciary Committee and

as noted previously, was opposed by several prominent members of the Committee. No one involved in proposing the amendment suggested that it was to revolutionize Federal law applicable to business or securities transactions or was to federalize local commercial disputes. Vividly illustrating the view that this addition did not alter the essential nature of the bill, the Committee's report devoted only a single, bland sentence to the new provision:

> The title, as amended, also authorizes civil treble damage suits on the part of private parties who are injured. (H.R. Rep. No. 1549, 91st Cong., 2d Sess. (1970), at 58).

In the House debates that led to passage of the bill as reported, the Members gave scant attention to this aspect of the bill. Instead, the debate was dominated by controversy over the breadth of the enforcement powers being conferred upon the government, not only in the Rico title but in other provisions. See generally 116 Cong. Rec. 35, 191-217, 287-363 (1970). For the House, too, was mainly concerned with the infiltration of organized crime figures into businesses across the nation. Thus, Congressman Poff, a leading proponent of the legislation, pointed to the takeover of a jukebox business by "a mafia boss" as an illustration of the general understanding that RICO was meant to prevent organized crime from injuring legitimate business people. 116 Cong. Rec. 6709 (1970).

The Senate accepted the House version of the bill, including the new provision for private civil suits, without any suggestion that the focus of Congressional concern had been shifted in the slightest from the goal of punishing hard-core criminals through federal prosecution. Indeed, Senator McClellan described the House amendments, including the addition of the provision for private civil suits, as relatively "minor changes." 116 Cong. Rec. 36,292-96, at 36,293 (1970). At no time did any sponsor or supporter of the RICO bill ever suggest that the private civil remedy was intended for use <u>against</u> legitimate business people, corporations, and licensed professional partnerships, or was to be used in commercial disputes having nothing whatsoever to do with the activities of what was and is commonly understood as "organized crime." Only you, Mr. Chairman, Judge Mikva and a few others seemed to recognize this potential. But I am afraid your dissenting views were somewhat lost in the rush to complete work on the legislation at the end of the session.

In fact, as we now know, civil RICO has been used and is today being used with increasing frequency, to harass all sorts of legitimate business enterprizes. According to comprehensive data recently collected on hundreds of civil RICO cases by the American Bar Association's Special RICO Task Force, 91% of all civil RICO cases rely primarily or solely on the securities fraud or mail fraud predicates of this organized crime statute.

Only 9% of all civil RICO cases involve underlying allegations of criminal activity of the type generally associated with professional criminals.

In his recent testimony before the Senate Judiciary Committee on the need for civil RICO reform, Assistant Attorney General Trott of the Department of Justice reported that the Department's own survey of private RICO cases confirmed this pattern of massive abuse. He estimated that, as a result of the increasing use of civil RICO in commercial disputes, the actual number of private cases filed already exceeds 500. According to the Justice Department's calculations, only about 7% of these cases involve either actual organized crime figures or the kinds of criminal conduct common to organized crime syndicates.

As these figures indicate, the statute has become a tool for civil litigants to avoid the carefully crafted limitations of the federal securities laws and to federalize a wide variety of local commercial disputes. As Assistant Attorney General Trott concluded:

> "Experience has shown . . . that the instances of private civil RICO's use against traditional organized crime activities are far outweighed by example of its application as a general federal anti-fraud remedy against seemingly reputable businessmen."

The invocation of RICO against what Mr. Trott called "conduct bearing little resemblence to organized crime activity in the traditional sense" is almost certain to accelerate. Decisions by appellate courts permitting the broad use of the statute first appeared in late 1982 and continue to the present time. Civil RICO counts are, therefore, far more likely to survive and hence to be utilized.

The one exception to this trend is in the Second Circuit, where, in the case of Sedima, S.P.R.L. v. Imrex Co., 741 F.2d 482 (2nd Cir. 1984), cert. granted, 53 U.S.L.W. 3506 (January 14, 1985), the court held that a private civil RICO action requires a prior criminal conviction of either a RICO offense or of the predicate offenses. The Supreme Court has heard arguments in both the Sedima case and in Haroco v. American National Bank & Trust Co., 747 F.2d. 384, 390 (7th Cir. 1984), cert. granted, 53 U.S.L.W. 3496 (Jan. 15, 1985), an appellate decision that rejects any requirement that any injury beyond injury from the predicate acts be alleged, thus opening the way to an especially broad application of the statute to virtually any commercial dispute.

The Supreme Court's decisions in those cases may not be dispositive of the issues presented and may not close the door in a definitive manner to the abuse of civil RICO. In any event, it is decidedly within the province of the Congress to correct the statute's patent deficiencies. In fact, the

Supreme Court may well adopt the position of many lower courts that Congress must undo the misuse of RICO that has flowed from its ambiguous language:

> "The legislature having spoken, it is not our role to reassess the costs and benefits associated with the creation of a dramatically expansive, and perhaps insufficiently discriminate tool for combating organized crime." Schact v. Brown, 711 F.2d 1343, 1361 (7th Cir. 1983).
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> "[W]e are cautioned by the Supreme Court that broad Congressional action should not be restricted by the courts in the name of federalism . . . . It is beyond our authority to restrict the reach of the statute [Civil RICO]." Bennett v. Berg, 685 F.2d 1053, 1064 (panel opinion) (8th Cir. 1982).
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> "Complaints that RICO may effectively federalize common law fraud and erode recent restrictions on claims for securities fraud are better addressed to Congress than to courts." Moss v. Morgan Stanley, 719 F.2d 5, 21, quoting Note, Civil RICO: The Temptation and Impropriety of Judicial Restriction, 95 Harv. L. Rev. 1101, 1121 (1982) (2nd Cir. 1983).

To eliminate existing abuses and refocus the statute on its intended targets, Congress should permit civil claims under RICO to proceed only after the defendant has been convicted of a RICO offense or of at least the predicate offenses. Such an amendment, which would basically codify the decision of the Second Circuit in the Sedima case, would confine the circumstances in which suits can be filed to those in which public prosecutors have screened those people who may fairly be charged with being involved in "organized crime" or a "pattern

of racketeering" (or "criminal activity") from those who should not be subject to such accusations.

We believe that the prior criminal conviction standard is a viable and meaningful standard which should govern civil RICO actions. The decision to lodge an accusation of a crime is the exclusive responsibility of the Executive Branch. It should not be left to private plaintiffs to invite federal courts and juries to find that persons have committed crimes for which they had not been successfully charged by public prosecutors.

Indeed, we are encouraged to observe that this guiding principle of the screening function obtained through the exercise of prosecutorial discretion and the discipline of a grand jury proceeding appears to be a facet of the Chairman's bill. Although no direct amendment is made to change Section 1964(c), the change in the definition of a "pattern of criminal activity" would appear to have at least a salutary effect with respect to RICO's civil remedy. By tying the "pattern of criminal activity" upon which civil liability is to be based to predicate crimes for which an "indictment is found or [an] is instituted," the amended definition would appear to require that an indictment or an information must issue before a civil damages action could be instituted. Thus, the change would allow private plaintiffs to pursue the special civil RICO remedy only after the Dartment of Justice has determined that the circumstances warrant the special enforcement remedies of the statute and a grand jury has approved that determination.

We continue to believe, however, that the requirement for prior conviction is a more appropriate and effective condition precedent to civil remedy. For example, we are concerned that once an indictment or information is returned, for private litigants to proceed with a civil case might jeopardize defendants' rights or complicate the prosecution's case. Moreover, it would be a somewhat troublesome result if a civil court found in favor of the plaintiff only to have the criminal court subsequently exonerate the defendant. Or worse yet, to have the criminal court dismiss the government's case and have the civil court subsequently find in plaintiff's favor. Because we are dealing with two different standards of proof in civil and criminal cases, either result is possible. It is for these reasons that, as we have deliberated on these matters, AICPA has decided to recommend "prior conviction" as the triggering event for civil liability. Nevertheless, as I noted earlier, we would acknowledge that the requirement for prior indictment or information does provide the requisite screening of RICO claims which we seek.

Mr. Chairman and members of the Subcommittee, we believe that the need for reform is clear. We respectfully urge you expand the scope of this inquiry so that you might consider and adopt amendments to the civil provisions of RICO which will restore the private remedy to its original purpose as an additional weapon against organized crime, while curing its

current capacity to inflict grievous harm and unreasonable costs on legitimate businesses.

We thank you for the opportunity to testify. To further assist the Subcommittee, we would ask that our more detailed paper on this subject be included in the record. We would be pleased to respond to any questions.