RICO and the Professionals

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Congress enacted the Organized Crime Control Act of 1970, including Title IX of the Act containing the Racketeer Influenced and Corrupt Organization (RICO) provisions, for the purpose of eradicating organized crime.1 This lofty goal has met with some success, especially with regard to the Act's criminal provisions. The Act also established a broadly worded civil remedy in favor of private plaintiffs. To put it mildly, it is questionable whether civil RICO has accomplished any of its drafters' lofty goals. Rather than being used as an effective tool in fighting organized crime, civil RICO has resulted in an avalanche of claims against legitimate businesses.

The purpose of this Article is three-fold. First, it will trace the development of RICO in the civil context in order to provide an understanding of the nature of the debate on this point. Second, it will comment on the significance of the Supreme Court's recent landmark decision in Sedima, S.P.R.L. v. Imrex Co.2 Finally, it will identify and discuss key issues that

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1. Pub. L. No. 91-452, 84 Stat. 922 (1970). Title IX has been codified at 18 U.S.C. §§ 1961-1968 (1982). Throughout this Article, the authors have assumed that the reader has a working knowledge of RICO's basic structure. Similarly, the authors have not attempted to cite all relevant cases or law review articles on RICO. Those sources include literally hundreds of cases and scores of articles, most of which at this point are of historical interest only. For an excellent overview of RICO, as well as thoughtful suggestions for legislative reforms, see Report of the Ad Hoc Civil RICO Task Force, 1985 A.B.A. Sec. Corp. Banking & Bus. L. Rep. [hereinafter cited as ABA RICO Report].

2. 105 S. Ct. 3275 (1985). On the same day, the Supreme Court handed down a companion decision in America Nat'l Bank & Trust Co. v. Haroco, Inc., 105 S. Ct. 3291 (1985), essentially based upon its ruling in Sedima. For ease of reference, this Article will refer
remain after *Sedima*. Throughout the discussion, the Article's primary emphasis will be on RICO's impact on professionals, specifically attorneys and accountants who frequently are the targets of civil RICO suits.

I. THE DEVELOPMENT OF RICO: THE ATTACK ON THE PROFESSIONS

There is no doubt that professionals in general, or "professional advisors" as the ABA Ad Hoc Civil RICO Task Force refers to them, have been active targets for RICO suits. In order to understand the risks faced by professionals in this area, it is useful to canvass the existing empirical data concerning the filing of these suits. Unfortunately, collecting meaningful data is exceedingly difficult. The most common source is simply a physical inventory of reported cases. While reliable, this method is hardly complete.

Reported cases do not tell the whole story, in part because many district court decisions are not reported. Moreover, suits may proceed for years without a formal court opinion. To complicate the process even further, litigants settle many actual or threatened RICO suits prior to any court review or even prior to suit being filed. Indeed, the spectre of RICO forcing large *in terrorem* settlements is a major criticism of RICO by its opponents.

The numbers that do exist tell a convincing, if incomplete, story. The ABA Task Force on RICO collected a database of over 270 RICO court decisions available in early 1985 showing twenty reported cases having been filed against attorneys and accountants, with another forty decisions concerning securities broker-dealers as defendants. Indeed, at the commencement of the study, three of only five substantive court of appeals' civil RICO decisions concerned claims against accounting firms.

The RICO decisions against professional advisors demonstrate that, rather than being an independent tort defining new patterns of liability, RICO claims have been used essentially as repetitions of other existing

solely to *Sedima* to identify the Supreme Court's position unless the context also requires a reference to *Haroco*.

3. ABA RICO REPORT, supra note 1, at 21.

4. ABA RICO REPORT, supra note 1, at 29. See The Authority to Bring Private Treble-Damage Suits Under "RICO" Should be Reformed, AICPA WHITE PAPER, at 11, 30 (June 10, 1985) [hereinafter cited as AICPA WHITE PAPER].

5. ABA RICO REPORT, supra note 1, at 30.

causes of action like alleged fraud in securities transactions. Indeed, RICO claims are commonly asserted in combination with more traditional state law claims filed either in the same case or as independent state court proceedings. Perhaps the best generalization that can be offered is that professionals are sued under RICO for the same types of problems for which they were sued prior to RICO's ascendancy. RICO claims against attorneys have been filed primarily for expressing opinions in stock transactions or partnership offerings. RICO cases against accountants have been defined somewhat more broadly, but in general have focused on problems arising in connection with audit examinations.

This observation is hardly earth-shaking, yet it is nonetheless significant. To the extent Congress believed that it was creating an important new tool for eradicating certain types of criminal activity, the results demonstrate that this goal has not been fulfilled, at least not as used in connection with suits against professionals. The behavior that is now being subjected to RICO's scrutiny was previously the subject of potential liability under existing laws. Moreover, no difference can be perceived in the type of plaintiff filing RICO suits against professionals. Primarily, the plaintiffs have been aggrieved creditors or investors who allegedly suffered losses, the standard pre-RICO plaintiff in complex litigation involving claims against professionals.

Until approximately 1980, RICO was not a major concern for professionals. Once RICO was recognized as a new civil litigation tool, however, its use spread like wildfire. The RICO explosion is well-documented. Before 1980, there were only nine reported district court civil RICO decisions. By 1984, the number had grown to 270, with courts handing down

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7. See AICPA White Paper, supra note 4, at 12-14.
12. ABA RICO Report, supra note 1, at 53a.
over 110 decisions in 1984 alone.\footnote{13} The pre-
Sedima\period, running approximately from 1981 until the end of 1984 when the Supreme Court agreed to review Sedima, was a period of full-scale war against RICO's application to legitimate businesses. Members of the legal profession, from the courts to practitioners and academicians, were occupied with trying to make sense of RICO's collection of exceedingly foreign terms and concepts. Perhaps the only analogy to the recent wave of legal energy expended on RICO was the collective efforts of the legal profession in connection with the development of rule 10b-5\footnote{14} in the securities area during the late 1960's.

Seemingly overnight, virtually every securities litigator had at least one, and usually more, RICO cases. The RICO allegations often would be a throw-in, but their consequences were immense. Clients resented being identified as racketeers, and although the criminal stigma element was probably overblown in court pleadings, the issue was real. While some defendants settled, perhaps an equal or greater number reacted in the opposite manner and authorized increased expenditures to vindicate themselves by fighting the RICO charge on all fronts. Certainly with respect to large institutional defendants, the message was clear: do whatever is necessary to defeat the broad application of RICO in civil litigation.\footnote{15}

Why was the reaction so strong? Certainly RICO's provisions for treble damages and attorneys' fees\footnote{16} were factors. Yet, many of the same defendants now subject to RICO had at least passing experience with antitrust suits encompassing the same array of remedies, or with securities laws that routinely allowed attorneys' fees to the successful plaintiff. Something beyond economic motivation was clearly involved. Certainly, the existence of actual losses was not a controlling factor; few if any civil RICO cases have resulted in a final judgment against a 'professional' defendant. The cause of the high emotional level exhibited by professional defendants is best understood as a combination of two elements: (1) the resentment and stigmatization associated with being branded a racketeer; and (2) the lack of understanding about what they supposedly had done to warrant the RICO claim.

The defense bar's creativity was proven several times over in its assault against RICO. RICO defendants had three levels of defense: (1) procedural; (2) definitional; and (3) substantive. On the procedural front, de-

\footnote{13} Id. at 30, 53a.\footnote{14} 17 C.F.R. § 240.10b-5 (1985).\footnote{15} See Berts, Pursuing a Business Fraud RICO Claim, 21 Cal. W.L. Rev. 246, 289 (1985) (noting potential negative effects on settlement possibilities from raising RICO claim).\footnote{16} 18 U.S.C. § 1964(c) (1982).
fendants challenged the sufficiency of RICO complaints with some successes during the early skirmishes. RICO's terminology was foreign to plaintiffs' attorneys and many RICO complaints simply did not articulate the statutory elements.\textsuperscript{17} The number of pleading defects decreased with time as various articles and seminars provided sufficient background to educate the drafters.

Another procedural tactic involved challenges under rule 9(b) of the Federal Rules of Civil Procedure.\textsuperscript{18} In a rare show of uniformity, virtually all courts have held that rule 9(b)'s more stringent pleading requirements apply in RICO cases.\textsuperscript{19} Beyond the fact of its applicability, however, rule 9(b) motions have not proven to be a major factor in RICO cases; as in other areas in which rule 9(b) applies, most courts read rule 9(b) in conjunction with the Federal Rules' liberal approach to pleading.\textsuperscript{20} While procedural objections served a limited purpose in rejecting some of the more outrageous applications of RICO, they did not offer any long range potential absent the development of substantive doctrines limiting RICO's application.

The only remaining procedural question offering any prospect for finding a meaningful limitation to RICO is the ultimate determination of the appropriate burdens of proof in RICO cases. The legislative history, to the extent that it addresses the subject, suggests that Congress intended to apply the usual civil standard permitting a plaintiff to prevail based upon a preponderance of the evidence.\textsuperscript{21} While the Second Circuit in \textit{Sedima, S.P.R.L. v. Imrex Co.}\textsuperscript{22} expressed concern that the preponderance standard would not adequately protect defendants, most courts to date have applied it nonetheless.\textsuperscript{23} The ABA RICO Report, however, makes a strong case that, while the preponderance standard should be applied on most issues, the existence of the criminal predicate acts should


\textsuperscript{18} Fed. R. Civ. P. 9(b).


\textsuperscript{21} See Sedima, S.P.R.L. v. Imrex Co., 741 F.2d 482 (2d Cir. 1984) (legislative history indicates that Congress assumed a preponderance standard was appropriate), \textit{rev'd on other grounds}, 105 S. Ct. 3275 (1986); ABA RICO Report, supra note 1, at 378-80 (canvassing legislative history on this issue).

\textsuperscript{22} 741 F.2d 482, 502 (2nd Cir. 1984), \textit{rev'd on other grounds}, 105 S. Ct. 3275 (1986).

require a heightened proof level.\textsuperscript{24}

RICO defendants also asserted a number of definitional arguments that largely fell on deaf ears. The most widespread argument, which was universally rejected by the courts of appeals, was the 'organized crime' theory that required the RICO defendant to be associated with traditional criminal elements.\textsuperscript{26} Other efforts were made to impose restrictive meanings to the 'enterprise' element; indeed, such efforts persist even after \textit{Sedima}.\textsuperscript{28} Finally, a number of courts were called upon to reject an argument defining RICO injuries as including only 'competitive' injuries as defined by the antitrust laws.\textsuperscript{27}

There also evolved over time a substantive attack against RICO that was formulated in numerous ways. The most common approach involved the 'racketeering enterprise' argument.\textsuperscript{29} According to this theory, a RICO claim was appropriate only in those cases that evidenced the type of illegal conduct that Congress must have intended when it enacted RICO. The questions presented transcended the statutory language and concerned whether RICO had any place at all in scrutinizing the affairs of law firms, accounting firms, brokerage companies, and the like. The concept had both a substantive liability component and a damage component. On occasion it was premised upon a reading of the "by reason of" language in section 1964;\textsuperscript{30} other times its statutory roots were left purposefully vague. While a number of courts accepted the limitation,\textsuperscript{31} the courts of appeals, with the exception of the Second Circuit in \textit{Sedima}, rejected the approach largely because of an inability on the part of RICO defendants to define how the concept could be meaningfully applied on a

\textsuperscript{24} ABA RICO Repott, \textit{supra} note 1, at 378-84.

\textsuperscript{25} See, e.g., Alcorn County v. United States Interstate Supplies, Inc., 731 F.2d 1160 (5th Cir. 1984); Schacht v. Brown, 711 F.2d 1343 (7th Cir.), \textit{cert. denied}, 464 U.S. 1002 (1983).

\textsuperscript{26} Courts have disagreed about whether the RICO 'person' can be the same as the RICO 'enterprise.' Compare United States v. Hartley, 678 F.2d 961 (11th Cir. 1982), \textit{cert. denied}, 459 U.S. 1170 (1983) (no separate enterprise required) with Bennett v. United States Trust Co., 770 F.2d 308 (2d Cir. 1985) (requiring separate enterprise).


\textsuperscript{28} Other terms for this concept include 'distinct injury,' 'special injury,' 'enterprise injury,' and 'racketeering injury.' See Comment, \textit{Civil RICO: The Resolution of the Racketeering Enterprise Injury Requirement}, 21 Cal. W.L. Rev. 364, 368 n.26 (1983) [hereinafter cited as \textit{Resolution of Racketeering Enterprise}].

\textsuperscript{29} 18 U.S.C. § 1964(c) (1982).

case-by-case basis. 31

The judicial approach to RICO evolved during the early 1980's. Decisions in the initial group were sometimes short and relatively nontechnical. Several courts made unsupported observations on RICO's purposes or limits. 32 Few opinions demonstrated a careful review of the legislative history or consideration of the substantive issues involved.

Perhaps recognizing the growing frequency of RICO cases, and undoubtedly spurred by increasingly lengthy and complex briefs by defense counsel, courts began approaching civil RICO with greater care. The decisions became not only longer but better. References to the legislative history increased. In general, defendants did better in this second stage. The overwhelming expenditure of resources by the defendants, often against less well-financed plaintiffs, resulted in some significant victories for defendants at the district court level. 33

The final pre-Sedima stage was characterized by complex and theoretical decisions. 34 Recognizing the actual or at least self-proclaimed RICO crisis, the courts focused tremendous resources in attempting to analyze the range of defenses being offered. RICO's amorphous structure offended many judges. The decisions included extensive discussion of the judiciary's power to impose meaningful limitations in the absence of any indication from Congress to do so. For the first time, the courts of appeals began regularly issuing civil RICO decisions. On balance, the courts of appeals ruled in favor of a broad reading of RICO. 35 Often this was accomplished with gnashing of teeth. Every major appellate decision came down in favor of RICO's broad application against 'legitimate' businesses, until the Second Circuit's Sedima trilogy in July 1984. 36


35. See, e.g., Battlefield Builders, Inc. v. Swango, 743 F.2d 1060 (4th Cir. 1984); Alcorn County v. United States Interstate Supplies, 731 F.2d 1160 (5th Cir. 1984); Schacht v. Brown, 711 F.2d 1343 (7th Cir.), cert. denied, 464 U.S. 1002 (1983).

36. See Sedima, 741 F.2d 482 (2d Cir. 1984), rev'd on other grounds, 105 S. Ct. 3275 (1985); Bankers Trust Co. v. Rhosedes, 741 F.2d 511 (2d Cir. 1984); Furman v. Cirrito, 741 F.2d 524 (2d Cir. 1984).
To say that the Second Circuit's decision was unexpected is an understatement. Most defense attorneys had rejected the 'prior conviction' defense early in the battle, usually replacing it with the far more promising 'racketeering enterprise injury' concept. Nonetheless, there it was—the influential Second Circuit holding that a prior conviction was required under RICO. It may be that no prior decision in the history of the courts of appeals resulted in the filing of so many motions to dismiss or reached such instant recognition among interested attorneys. Soon thereafter, the Seventh Circuit rejected the Second Circuit's requirement, and *Sedima* was destined for the Supreme Court.

II. THE SIGNIFICANCE OF *SEDIMA*

The most uncontroversial observation about the Supreme Court's decision in *Sedima* is that it will insure that RICO litigation will flourish. The philosophical thrust of *Sedima* at first glance seems incredibly proplaintiff. Focusing on the lamentations of the dissenters, the reader could conclude that RICO will inevitably become all that the 'legitimate' RICO defendants urged that it should not. Despite these harbingers of doom, the opinion hardly compels the ascendancy of RICO as the universal cause of action.

As presented to the Supreme Court, *Sedima* raised two issues: (1) the prior conviction theory, virtually without support in the legislative history; and (2) the racketeering enterprise theory, which had proven to be incapable of definition despite years of effort. The prior conviction defense was a minor, indeed previously discarded, defense that was transformed overnight into the White Knight. Yet, apart from philosophical agreement from the beleaguered defense bar, few believed that the prior conviction requirement held any promise. The ABA RICO Report, otherwise quite critical of RICO's application, disputed the applicability of the prior conviction theory. Regardless of how good an idea the prior conviction requirement may seem in retrospect, Congress simply did not appear to have such a barrier in mind when RICO was enacted. The Supreme Court's rejection was predictable.

The 'racketeer enterprise' or 'RICO injury' concept was more plausible.

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38. 105 S. Ct. at 3292 (Marshall, J., dissenting); 105 S. Ct. at 3288 (Powell, J., dissenting).
39. ABA RICO REPORT, supra note 1, at 209-38. The American Institute of Certified Public Accountants (AICPA) expressly called for the adoption or enactment of a prior conviction requirement in its 'White Paper' report filed with the Department of Justice. AICPA WHITE PAPER, supra note 4, at 42-44.
While articulated in several different and often inconsistent ways, it was best presented as an analogy to a similar limitation from the antitrust laws articulated in Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc. The comparison is appealing, just as the antitrust laws were intended to provide a remedy to those suffering an antitrust injury—an injury the antitrust laws were designed to prevent—so too should RICO be limited to those injuries which RICO was designed to prevent. The problem with applying Brunswick is that its logic, albeit somewhat circular, meant something in the antitrust context. The antitrust laws are not very precise; they are more like a constitution that requires fleshing out. Antitrust is intended to promote an economically fair and efficient marketplace. There are certain acts that injure competitors but do not injure competition; this is Brunswick’s primary focus.

On the RICO front, there is no need to adopt a similar conceptual limitation. RICO describes or defines what it seeks to prevent more precisely than do the antitrust laws. Behavior constituting the commission of the proscribed predicate acts, so long as they form a pattern, are always ‘illegal’ under RICO. It does not matter if just one competitor is hurt; unlike the antitrust laws, focus on the benefit to the economy as a whole, RICO seeks to prohibit all ‘racketeering activity.’ The private wrong is coextensive with the public policy.

Sedima’s rejection of a racketeering injury requirement is little more than an acknowledgment that any injury resulting from the commission of the proscribed criminal acts is an evil that Congress intended to punish. While the antitrust laws have a number of countervailing interests that interact with its prohibitions, such as efficient markets and lower prices, there are no such positive virtues lurking behind a RICO defendant’s commission of predicate acts.

Beyond the rejection of these two defenses, which if adopted might have stopped RICO dead in its tracks, what does Sedima say about RICO’s future? Plaintiffs will cite its language describing Congress’ far reaching purposes. Surely, they argue, if the Supreme Court so vehemently rejected the variety of standing limitations considered in Sedima, it must have intended RICO to be given a broad reading in other respects. Similarly, so the argument will go, one need not read further than the dissent to know that RICO now reigns supreme.

It is always dangerous to read a Supreme Court dissent as a comment on issues not decided by the majority. A dissent commonly presents a parade of horribles to suggest that the specific issue decided by the Court was improperly determined. In fact, the Court remains as free as ever to

41. Id. at 489.
consider the next question presented on its own merits. *Sedima* is no different. If anything, Justice White’s decision implicitly and explicitly suggests that the Court’s approach on the substantive contours of the RICO cause of action is far from determined. Rather than saying that the courts must now begin imposing RICO liability whenever possible, *Sedima* can be read as urging strict adherence to the statutory regime that includes a number of substantive limitations, each of which remains open to be explored. *Sedima*’s message, while certainly significant, is that RICO cannot be read to exclude broad categories of cases simply because some suits will be inappropriately filed. Congress did not impose standing limitations in trying to address the serious problem of criminal activity and organized crime in this country.

What follows are descriptions of three critical areas of potential limitation left open after *Sedima*. The three potential elements of *conduct*, *pattern*, and *damages* will require vast amounts of judicial analysis in the next few years; they are the new battlegrounds defined in *Sedima*. The *conduct element* involves the degree of responsibility that the RICO defendant must possess. The *pattern element* addresses what factual conditions must exist to make the RICO claim different than an ordinary claim. Finally, the *damage element* will further determine whether RICO is merely a redundancy or a new cause of action the remedy for which is limited to and defined by the pattern of proscribed conduct. Together, these elements will shape the RICO suit and determine whether the spectre raised by the ‘legitimate’ RICO defendants is imagined or real. If the elements can be given meaning, RICO can still be limited to appropriate cases penalizing particular forms of egregious conduct. If these elements prove so ephemeral that courts cannot ascribe any substance to them except hollow applications of minimum proof requirements, then RICO will truly ravage the landscape. What is important to note is that *Sedima* does not answer the questions, and indeed has little to say about them.

III. THE FUTURE OF RICO SUITS AGAINST THE PROFESSIONALS: TOWARDS MEANINGFUL LIMITATIONS

Understood in context, *Sedima* cannot be the last word on RICO’s general application to ‘legitimate’ defendants. While the creativity of the defense bar may well spur new arguments, *Sedima* more than suggests that the debate must focus on the express statutory requirements that are present in RICO. While legislative changes are possible and are being actively pursued, courts will certainly be called upon to define and give

42. To date, the most serious proposals for legislative reform are those forwarded by the RICO Task Force. See ABA RICO REPORT, supra note 1, at 427-34.
meaning to those elements. Three areas are critical in the continued judicial analysis of RICO.

A. The 'Pattern' Element

Sedima was not totally uncompromising in giving a broad reading to RICO. Indeed, it expressly raised a possible defense that had been largely rejected in those few courts that had previously considered it. In footnote fourteen, which the RICO defense bar hopes will become a legend in its own time, Justice White discussed at some length the importance of the 'pattern' requirement set forth in section 1962(c)\(^4\), and defined in section 1961(5).\(^4\) The Court noted that "in common parlance two of anything do not generally form a 'pattern.'"\(^4\) This logical approach found support in the legislative history showing that the pattern requirement was meant to instill a 'continuity plus relationship' notion into the pattern concept.\(^4\) Referencing another part of the same bill that included RICO, the Court observed that the term pattern "'embraces criminal acts that have the same or similar purposes, results, participants, victims, or methods of commission, or otherwise are interrelated by distinguishing characteristics and are not isolated events.'"\(^4\)

While the Supreme Court's purpose in engaging in an extended discussion of the pattern requirement is unclear, it is more than a safe bet to predict that RICO defendants will eagerly embrace the concept for all that it is worth, and perhaps more. Accordingly, it is useful to make a few observations about it. First, prior to Sedima, little substantive meaning was given to the pattern requirement. Most courts found that, so long as two predicate acts were alleged, the pattern element was met.\(^4\) A few courts found greater meaning, opining that the required pattern necessarily meant that the alleged racketeering acts be connected to each other by some common scheme, as opposed to a series of isolated acts.\(^4\) If

\(^4\) 105 S. Ct. at 3285 n.14 (construing 18 U.S.C. § 1962(c) (1982)).
\(^4\) 105 S. Ct. at 3285 n.14. Section 1962(c) is the principal substantive RICO section used in civil cases. See ABA RICO Report, supra note 1, at 57. (97% of RICO cases are based on section 1962(c)).
\(^4\) 105 S. Ct. at 3285 n.14 (quoting 18 U.S.C. § 3575(e)).
Sedima is to be taken at its word, however, there may be something about the pattern requirement that is even more substantive than any limitations previously suggested. As used by Justice White, the pattern requirement is critical; the Court did not deny that RICO has been used inappropriately. The problem, however, could not be addressed by artificial standing limitations or definitional chicanery. Rather, the problem of RICO’s overuse was a direct result of courts not having given any meaning to the pattern element.80

In the few brief months since Sedima was decided, the pattern requirement has already received attention. Emboldened by footnote fourteen, some district courts have expressly held that they are not bound by earlier, more restrictive decisions and have given the pattern requirement new weight in analyzing RICO claims.81 Others have been less enthusiastic, although this may be the result of cases in which the number and quality of the predicate acts chilled whatever interest the court may have had in taking an aggressive stance.82

Assuming for the sake of argument that courts do raise the gauntlet on pattern, there are several issues to address. Indeed, footnote fourteen is unclear about how courts should analyze the pattern element. Perhaps the best way to explore the question is by using an example. Suppose that a RICO defendant, an attorney, was involved in preparing a prospectus in connection with an investment packaged by the usual coterie of promoters and operators. All of the players are now being sued by the investor.

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of Eris, 537 F. Supp. 6 (W.D. Pa. 1981) (no pattern requirement when all predicate acts were alleged bribes made by different people to same public officials at same event).

50. 105 S. Ct. at 3287 (noting that the problems with RICO resulted primarily from the “failure of Congress and the courts to develop a meaningful concept of ‘pattern.’” Id.)


In Northern Trust, plaintiff alleged that it was injured as a result of a kickback scheme. Defendant Inryco was a general contractor on a construction project. One of its employees was responsible for subcontracting the project. That employee entered into a kickback arrangement with one of the subcontractors. Plaintiff alleged that the solicitation of the kickback together with the payment of the kickback, two separate predicate acts, constituted a pattern. Spurred by Sedima, the district court concluded that it was not bound by United States v. Weatherspoon, 581 F.2d 586 (7th Cir. 1978), since Sedima created a “whole new ballgame.” The court concluded that pattern “connotes a multiplicity of events: Surely the continuity inherent in the term presupposes repeated criminal activity, not merely repeated acts to carry out the same criminal activity.” 615 F. Supp. at 831 (emphasis in original). Cf. United States v. Moeller, 402 F. Supp. 49 (D. Conn. 1975) (suggesting that the RICO pattern requirement should relate to different criminal episodes).

52. See Alexander Grant & Co. v. Tiffany Indus., Inc., 770 F.2d 717 (8th Cir. 1985) (observing that the pattern element was present in an amended complaint alleging 48 acts of mail fraud and 10 acts of wire fraud over a lengthy period of time and containing other attributes identified by Sedima).
The predicate acts alleged against the attorney are three different acts of mail fraud consisting of letters or phone calls from the attorney to the investor, and a general allegation of securities fraud in connection with the preparation of the prospectus.

The initial question is whether a pattern can exist based upon this single investment involving this single investor. The 'continuity' notion suggests that perhaps something beyond the single transaction may be needed. Many plaintiffs have instinctively anticipated this argument and have sought to discover facts about other investments put together by the same defendants. This effort to broaden the scope of the RICO case is proper if focusing solely on the pattern requirement, but it raises difficult issues in terms of the manageability of the case. Why should a court permit one investor to spend weeks or even months discovering facts relating to an entirely different investment program if the investors in the other endeavor are not themselves plaintiffs? Absent RICO's requirements, standing limitations and the proper scope of discovery may well limit the plaintiff-investor's efforts to investigate any separate investments. The fact that the same defendants may have defrauded someone else may well be of no moment in a normal suit, but arguably is critical in the RICO suit if the pattern element is disputed.53

Because the pattern element is contested, a court may permit the RICO plaintiff in our hypothetical case to discover facts concerning other investments. Assume that there are three other 'similar' investments put together by the same group of defendants, and assume further that the defendant attorney was not involved in drafting or reviewing the prospectus in the other three programs. Finally, assume the attorney was an investor in one of them. The problem is whether the attorney was involved in a pattern based upon more than two predicate acts in the single scheme and the different role in another investment. Present law and the Supreme Court's approach in Sedima do not resolve the question.

A number of factors are potentially relevant in determining the existence of a pattern: (1) the number of predicate acts alleged; (2) the relative chronology of the predicate acts to the alleged injury suffered by the plaintiff; (3) the relationship of the number and timing of the predicate acts; (4) the role or relative culpability of the particular defendant in connection with the predicate acts; and (5) the connection or relationship between the predicate acts and the affairs of the RICO enterprise. By analyzing these factors, as well as other factors that may be developed over time, the courts can, perhaps, follow the Supreme Court's suggestion

53. If the pattern element is not contested, the court may determine that discovery into the other investments is not required, or its value outweighed by the cost or lack of relevance under revised rule 26. See Fed. R. Civ. P. 26(b).
and infuse some meaning into the pattern element.

In connection with our hypothetical, the analysis could proceed as follows. Assuming that the attorney’s alleged commission of the three acts of mail fraud and one act of securities fraud occurred in a relatively brief period of time, the court could conclude that they were sufficiently related to a single scheme and, thus, did not constitute a pattern in and of themselves. The court then would have to decide whether to analyze the attorney’s connection with the other investment programs. In that review, the role of the attorney is critical. In one other program, the attorney was an investor, not the drafter of the prospectus. The distinction should be important for ‘pattern’ purposes. Unless the change in role was merely to dupe others into investing, the fact suggests that, rather than being a perpetrator of criminal acts, the attorney was a victim. Thus, even if the plaintiff alleges that the attorney committed another predicate act in connection with the second investment, the ‘relationship’ aspect of the test is lacking. The second program does not contribute to the making of a pattern.

Given the many factual issues that relate to determining the existence of a pattern, courts may not feel comfortable addressing the issue at a preliminary stage of the case, such as on a motion to dismiss. The proper time to analyze the pattern question will depend upon the nature of the alleged predicate acts and the additional sources of information that the RICO plaintiff has a valid interest in discovering. If the plaintiff had a reasonable opportunity to know the facts prior to the filing of the suit, and the court believes that the universe of predicate acts that may exist is already set forth, it may be appropriate to consider the pattern element at a preliminary stage in the litigation. If there appears to be a substantial question about whether a pattern exists, a court also could order limited discovery addressed solely to the pattern issue in order to clarify the record. This will be useful for many reasons, including: (1) Determining whether the predicate acts in fact occurred; (2) understanding the relationship between the RICO enterprise and allegedly criminal conduct prior to resolving the pattern question; and (3) making a preliminary determination of the need to conduct full-scale discovery into other acts involving the RICO enterprise that do not directly involve the plaintiff. Resolving the pattern issue is critical both for determining whether a case can proceed under RICO in the first instance, which is often the only basis for federal court jurisdiction, as well as for effectively structuring discovery. Accordingly, courts should consider addressing the pattern issue at an early stage, even if some discovery is required on the point.

B. The ‘Conduct’ Element

In Sedima, the Court did not directly consider the nature of the ‘con-
duct' element set forth in section 1962(c). Under that section, a RICO defendant must conduct or participate in the affairs of the enterprise through a pattern of racketeering activity. Nonetheless, in generally describing the parameters of the RICO offense, the Court in *Sedima* noted that the conduct element was significant. Questions about the conduct element were raised in a companion case, but the Court elected not to consider them on the merits since they had not been presented in the petition for certiorari.

Common sense suggests that a RICO defendant have some meaningful involvement in the alleged criminal acts in order to 'conduct' the affairs of the RICO enterprise. To date, a few cases have attempted to articulate the conduct element. In *Bennett v. Berg*, a case against numerous defendants including an accounting firm, the Eighth Circuit suggested that allegations against the accountants may have been insufficient on the conduct point. According to the court, "A defendant's participation must be in the conduct of the affairs of a RICO enterprise, which ordinarily will require some participation in the operation or management of the enterprise itself." The court speculated that accountants will not usually come within that definition. Several courts have suggested that the conduct requirement should be construed to require meaningful participation. Some courts, however, have rejected efforts to require a significant degree of participation, often noting the liberal reading given the conduct element in criminal cases.

Establishing a meaningful conduct limitation would be of special benefit to professionals. The accounting profession would benefit in particular,

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55. 105 S. Ct. at 3285.
57. 710 F.2d 1361 (8th Cir.) (en banc), *cert. denied*, 464 U.S. 1008 (1983).
58. 710 F.2d at 1364.
since most RICO cases against accounting firms concern audits and/or audit opinions. By definition, assuming the accountant structured the relationship properly, the interaction between an accounting firm and its client in an audit engagement involves a significant degree of separation. Accountants do not perceive themselves as being employed by their clients in the traditional sense in the audit context; rather, they are engaged to provide certain services to their clients as objective reviewers. An auditor, for example, does not make company policy or suggest business alternatives. Rather, the auditor examines the financial statements initially generated by the audit client. In the normal situation, therefore, auditors can present strong arguments that they do not conduct or participate in the affairs of their clients, assuming the conduct requirement is given any degree of meaning.\(^{61}\) No court has yet explored the ramifications of fully recognizing such a requirement as suggested by Bennett.

Imposing a meaningful participation requirement also would assist attorneys sued under RICO. To date, most RICO cases against attorneys have occurred in the context of securities offerings. By focusing on the professional relationship involved, courts could begin to separate the egregious cases in which RICO liability is warranted from those cases in which the professional defendant was simply ‘doing his job’ in providing professional advice.

C. Damage Theory under Sedima

Since so few civil RICO cases have reached trial, there is little case law or academic comment on the theory of damages under RICO.\(^{62}\) Prior to Sedima, defendants had articulated the ‘racketeer enterprise’ concept as including a damage component. The plaintiff’s RICO damages had to include injuries from something beyond the injuries resulting directly from the commission of the predicate acts.\(^{63}\) As noted above, this de-

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61. In one accountant’s liability case, a district court adopted the holding in Bennett requiring some meaningful conduct, but then determined that the test was met based upon allegations that an accounting firm was simply involved in the activity in question. See Federal Bank & Trust Co. Sec. Litig., Fed. Sec. L. Rep. (CCH) ¶ 91,565 (D. Or. 1984). A related claim against the American ‘parent’ accounting firm was dismissed, however, since that firm’s only responsibility would have been based upon some notion of respondeat superior.


fense—part damage model, part conceptual—proved difficult to articulate despite its similarity to accepted limitations existing under antitrust law.

There is no established theory of damages under RICO, but there are several possibilities. 64 First, there is no express requirement that the predicate acts have any relationship to the damage model selected. Section 1964, 65 which authorizes damages in a private civil suit, does not directly concern the predicate acts or the pattern of racketeering. It simply requires a causal relationship between the damages and a violation of one of the four subparts of section 1962. Thus, it could be argued that once a violation of section 1962 is shown, section 1964 controls the determination of damages without reference to predicate acts. If this approach is correct, antitrust law damage theory is relevant given the similarity in language between the Clayton Act 66 and section 1964. A second approach seeks to make a somewhat subjective evaluation of the nature of the predicate acts and pattern of racketeering alleged in the case. It then requires the selection of the most analogous damage theory from among existing state law candidates. 67 Under this case-by-case approach, the damage model is defined by the same acts that constitute the substantive offense.

The Supreme Court in *Sedima* apparently adopted a third damage model. Justice White expressly rejected the 'racketeering enterprise' damage approach and, perhaps spurred by the dissent’s discussion of damages, 68 addressed RICO's damage theory at some length. 69 In doing so, the Court addressed issues not previously discussed elsewhere. As opposed to ‘predicate act plus,’ Justice White adopted a direct damage model that ultimately may prove to be a more significant limitation than the rejected indirect or 'racketeer injury' damage model. 70

Although *Sedima* is noteworthy primarily for its rejection of standing

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64. 105 S. Ct. 3275, 3292, 3298-99 (Marshall, J., dissenting). It is appropriate that Justice Marshall authored the lead dissent on this point, since the ‘RICO injury’ concept was developed as an analogy to the ‘antitrust injury’ concept articulated by Justice Marshall in *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477 (1977). See supra notes 40-41 and accompanying text.


68. 105 S. Ct. 3288 (Powell, J., dissenting). See also ABA RICO Report, *supra* note 1, at 285-87 ("the very dispersion of views is testimony to the fact that no answer to this question flows inevitably from any of these standard forms of statutory analysis"). The ABA report identified the damage option somewhat differently than does this Article, although the basic question whether RICO requires a connection between either the predicate acts or the pattern and the claimed damages is present in both.

69. 105 S. Ct. at 3285-86.

70. *Id.*
requirements, the damage model was expressed in standing terms. In a civil RICO action, a "plaintiff only has standing if, and can only recover to the extent that, he has been injured in his business or property by the conduct constituting the violation." 71 Assuming the other elements are met, the compensable injury necessarily is the harm caused by predicate acts since the commission of those acts is what RICO was intended to deter; therefore, any recoverable damages will flow from the commission of the predicate acts. 72

The decision in *Sedima* did not turn on the application of the damage theory to the case at hand so the discussion of damages in RICO cases is neither complete nor particularly instructive. The thrust appears to be that RICO damages are limited to those directly caused by the predicate acts themselves. According to *Sedima*, courts need not weigh the predicate acts and select a damage model from existing law. Section 1964 does not simply adopt antitrust damage concepts. Rather, RICO has its own damage model: damages must result from and are potentially limited to those arising directly from the predicate acts. Accordingly, as is the case with the pattern element, a clear articulation of the predicate acts is crucial in determining the existence and significance of the RICO damage allegations.

*Sedima* potentially supports a RICO damage model that may well serve to differentiate between an appropriate RICO case and an inappropriate case. A repeated complaint against RICO, especially by professional defendants, is that RICO is redundant because it merely duplicates existing causes of action for securities law violations, common law fraud, or even negligence. The Court's damage discussion suggests that it recognizes that, while the same facts may give rise to a RICO claim, the damages available under RICO differ substantially from other causes of action that may apply.

A hypothetical example suggests a possible limitation. Assume that an accounting firm performed an audit on a company that had borrowed funds from a lending institution, and that the lending institution suffered a loss when the audited company went bankrupt. The bankruptcy occurred despite the fact that financial statements examined by the accounting firm reflected that the company was in reasonably good financial condition. Ordinarily, one could expect the lending institution, if sufficiently aggrieved, to file a state law negligence or fraud suit against the accountants. Emboldened by *Sedima*'s broad reading of the civil RICO statute, the lender considers a RICO suit. A search is made to determine whether any predicate acts exist to support the claim. As is often the

72. *Id.* at 350-54.
case, the number of direct contacts with the accountants is relatively few and insignificant—an occasional phone call, meeting, or mailing of a report. Nonetheless, given the latitude of the mail and wire fraud statutes, a RICO claim is made. Putting aside the pattern issue, the question is how Sedima’s damage model applies.

The Court’s approach requires at least a meaningful nexus between the predicate acts and the claimed injury. While most complaints will probably survive a motion to dismiss simply by alleging the necessary ‘reliance’ or causation theories, actual proof of the nexus between damages and the predicate acts may be difficult. Many of the allegations critical to the proof of the mail fraud predicate act may prove to be trivial and meaningless contacts in the actual case. For example, in the above hypothetical, the actual claim for injury may well relate to the auditor’s negligence in conducting the audit, not to an occasional phone call. The damage was caused by the auditor’s negligence, or, in particularly egregious cases, recklessness. In the rare case, which perhaps is the only appropriate case for RICO sanctions, the accountant became an active participant with the company in misleading its investors or creditors by taking direct part in the fraud, such as by taking a bribe to overlook fabricated financial information.

What of the incidental predicate acts? If it was the negligent audit that actually injured the lender, Sedima suggests that RICO does not provide for damages simply because two phone calls were made to verify the value of the lender’s collateral. Improper expression of an unqualified opinion on a financial statement is not a predicate act. The lender was injured by other conduct not constituting a predicate act under RICO.

Substantial analysis remains to be performed on RICO’s damage theory as courts begin to apply Sedima to specific cases. While it will never serve to restrict the filing of RICO cases, as was the effect of the prior conviction requirement, the recognition of a direct damage theory will address Judge Oakes’ primary concern in Sedima: insuring its use in cases in which the magnitude and severity of the alleged criminal conduct justifies RICO’s sanctions. 73 Under the direct damage model, predicate acts are important because they define the damages to be recovered. They are not merely jurisdictional hooks without lasting significance in the case—they define and, therefore, potentially limit damages.

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73. This analysis suggests that courts may need to ‘carve out’ RICO damages from damages obtainable under another liability theory. While it raises certain practical problems, such allocations must be made in some types of cases. See Farnon, supra note 62, at 353 n.42.
IV. CONCLUSION

Following *Sedima*, it is fair to say that we have completed the first wave of judicial thinking about this most complicated and significant statute. What is left of the defendant's attack on RICO is yet to be seen. Certainly, substantial defenses relating to RICO's conduct, pattern, and damage elements still need to be explored. The professionals stand in the middle of the fray, being both likely targets for RICO's wrath as well as primary beneficiaries of any substantive limitations that can be developed. The hoped-for result need not, and in light of *Sedima* cannot, be an absolute immunity from RICO for professionals, even though the prospects of potential RICO liability threaten important professional values. To date, courts have not considered the professional's role in rendering services to others in applying RICO. In part, this is a function of the nature of the debate to this point. Inundated by procedural and definitional attacks, the pre-*Sedima* decisions necessarily focused on RICO's terms and not on its application in specific contexts such as suits against professionals. More lies ahead than behind in this area.