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WHITE-COLLAR CRIME

Expert Analysis

Federal RICO Statute: Extraterritorial Reach and Other Recent Issues

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The federal racketeering statute, originally drafted to "eradicat[e]…organized crime in the United States,"[1] continues to expand in scope and applicability. Indeed, despite the numerous white collar initiatives and new financial criminal statutes, such as Sarbanes-Oxley, enacted to deal with a spate of perceived holes in the nation's regulatory scheme, RICO prosecutions remain as popular as ever.[2] *United States v. Philip Morris*,[3] a recent decision from the U.S. Court of Appeals for the District of Columbia Circuit, highlights the ways in which the government continues to push the envelope in such cases.

The issues raised in that case, as outlined in various certiorari petitions to the U.S. Supreme Court by defendants and the government, are topics of interest to white collar practitioners who already are handling RICO cases outside the originally intended "organized crime" context. Specifically, the case raises questions regarding the extraterritorial application of the RICO statute, whether a group of corporations can constitute a racketeering "enterprise," and whether the government can seek disgorgement of profits as a result of RICO violations.

Extraterritoriality of Statute

The issue of extraterritorial reach of federal criminal statutes has grown in importance as increased globalization results in more international business, travel and accessibility.[4] In certain cases, such as the Foreign Corrupt Practices Act, a statute will focus exclusively on extraterritorial conduct and no question exists of its application to acts occurring outside the United States.[5] In other instances, like the federal perjury and money laundering statutes, the criminal statute includes a provision directly addressing its extraterritorial application.[6]

More often than not, however, federal statutes are silent as to whether they apply extraterritorially. The federal racketeering, or RICO, statute is one such example. RICO's reach to extraterritorial conduct has been a source of disagreement among the federal circuit courts. The Supreme Court may have an opportunity to consider and resolve the issue if it grants the certiorari petition of British American Tobacco (Investments) Ltd. (BATCo), a foreign corporation sued in the United States under the civil RICO provisions.[7]

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An unsigned, per curiam opinion from a panel of the D.C. Circuit details the lawsuit brought by the United States in 1999 against nine cigarette manufacturers and two tobacco-related trade organizations alleging violations of sections 1962(c) and (d) of the RICO Act.[8] After a nine-month bench trial, all the defendants were found liable under the statute for what the government alleged to be a "decades-long conspiracy to deceive the American public about the health effects and addictiveness of smoking cigarettes."[9]

BATCo was the only foreign company defendant in that case. Because no evidence was introduced demonstrating that BATCo manufactured or marketed cigarettes in the United States, the company argued on appeal that the district court erred in imposing liability on the basis of its conduct outside the United States. Specifically, BATCo asserted that a presumption against extraterritoriality generally is recognized by courts and that the RICO statute has no extraterritorial reach. Rather than address directly the extraterritorial application, the D.C. Circuit found that the presumption against extraterritoriality did not apply because the district court concluded that BATCo's foreign conduct had an impact in the United States.

The court reasoned that "[b]ecause conduct with substantial domestic effects implicates a state's legitimate interest in protecting its citizens within its borders, Congress's regulation of foreign conduct meeting this 'effects' test is '*not* an *extraterritorial* assertion of jurisdiction.'"[10] The court therefore determined that it only needed to decide whether the district court erred in determining that BATCo's conduct had a substantial, direct, and foreseeable effect in the United States, as required under the "effects" test.

The district court had found that BATCo conducted abroad sensitive nicotine research for an American subsidiary/affiliate and secretly shared the results with that company and conspired with the other defendants to form, fund, and participate in international organizations used to perpetuate the allegedly fraudulent and deceptive scheme. The D.C. Circuit held that "these unchallenged findings, together with the findings of the tremendous domestic effects of the fraud scheme generally, make clear that the district court committed no error in finding that BATCo's participation had substantial, direct, and foreseeable effects in the United States."[11]

BATCo filed a petition for certiorari, asserting that the lower courts' decisions contravened "a longstanding principle of American law that

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legislation of Congress, unless a contrary intent appears, is meant to apply *only* within the territorial jurisdiction of the United States."[12] BATCo's petition raised two separate issues. First, whether the circuit court erred in finding that the "traditional presumption against extraterritoriality is completely irrelevant in determining whether Congress intended the RICO statute to reach the wholly foreign conduct of a foreign corporation, if such foreign conduct is alleged to have had a direct and substantial effect within the United States." Second, the petition asked whether the D.C. Circuit's reliance on the "effects" test as a measure of RICO's extraterritorial reach was appropriately and correctly applied.

BATCo argued that both issues are appropriate for adjudication by the Supreme Court because the lower courts are divided over whether RICO applies extraterritorially and whether the "effects" test, developed by the courts in the context of federal antitrust and securities laws areas, should be applied in the RICO context. As an initial point, BATCo argued that the D.C. Circuit Court's analysis was backwards, noting that other circuits applied the "effects" analysis against the backdrop of the presumption against extraterritoriality.[13]

Further, BATCo observed that courts had expressed uncertainty regarding the application of the "effects" test in the RICO context. In particular, BATCo cited the U.S. Court of Appeals for the Second Circuit's decision in *North South Finance Corp. v. Al-Turki*.[14] In *Al-Turki*, the Second Circuit wrote that "specifying the test for extraterritorial application of RICO is delicate work," suggesting that applying the "effects" and/or "conducts" tests developed in analyzing securities and antitrust laws would be improper. "We…do not assume that congressional intent in enacting RICO justifies a similar approach to the statute's foreign application."[15]

Ultimately, the Second Circuit did not resolve the question because the parties had "assumed that the 'effects' test applied to RICO and conceded that it could not be satisfied."[16] A district court in the D.C. Circuit has suggested that RICO might apply to foreign conduct in the nature of "classic organized crime," at which the statute initially was aimed, but not to other types of activities now covered by the broad application of the RICO statute.[17] Given these contrasting opinions, BATCo argued that a substantial disagreement exists among federal courts over the extent, if any, of RICO's extraterritorial reach.

Even if it were determined that the "effects" test properly should be applied to the question of whether foreign conduct is punishable under the RICO statute, BATCo argued that its conduct did not satisfy the traditional "effects" test as used in antitrust and securities cases. Traditionally, relevant domestic effects must be substantial, direct and the foreseeable result of the foreign conduct.

BATCo asserted that the district court failed to "include a single factual finding of substantial and foreseeable effects within the United States resulting directly from BATCo's foreign activities." Further, BATCo asserted that the district court improperly invoked the fraud scheme generally as proof that BATCo's conduct had a domestic effect in the United States, arguing, "[i]t is precisely this type of generalized and indirect effect, not directly attributable to BATCo itself, that is insufficient under a properly circumscribed 'effects' test."[18]

BATCo's petition demonstrates the confused state of the law with respect to the extraterritoriality of the RICO statute and the appropriate test to be applied by courts in determining whether federal courts properly can assert jurisdiction in a particular case. If the D.C. Circuit's ruling stands, its expansion of the extraterritorial jurisdiction of U.S. courts will have a significant impact on white collar defendants.

'Boyle' is evidence of the U.S. Supreme Court's tendency toward broad interpretation of the statutory language set forth in the RICO statute, including the definition of 'enterprise.' It is no longer necessary to show that the enterprise possessed a 'hierarchical structure' or 'chain of command.'

Some commentators argue that continuing aggressively to expand the United States' extraterritorial reach may result in reciprocal efforts by other countries. For this reason, they advocate limiting extraterritorial prosecutions of business crimes "to instances when the federal government is the victim of the crime and the conduct requires prosecution as protection of a governmental interest. Conduct merely having a substantial effect on individuals within the country, they argue, should not be a sufficient basis for a United States prosecution of a business crime."[19]

Other Issues

Can a Group of Corporations Constitute an "Enterprise"? Another issue raised by the various certiorari petitions stemming from *United States v. Philip Morris* is whether the D.C. Circuit's conclusion that a group of corporations can form a RICO enterprise was erroneous. Two of the American-based tobacco company defendants have argued that the circuit court's conclusion contravenes the plain language of the RICO statute.[20]

The RICO statute makes it unlawful for "any person…associated with any enterprise…to conduct or participate, directly or indirectly, in the conduct of such enterprise's affairs through a pattern of racketeering activity."[21] The statute defines a "person" as including "any individual or entity capable of holding a legal or beneficial interest in property."[22] Accordingly, a corporation, as well as an individual, can be liable under the statute. Further, an enterprise is defined as "any individual, partnership, corporation, association, or other legal entity, and any union or group of individuals associated in fact although not a legal entity."[23]

The tobacco company defendants disputed the district court's ruling that a RICO enterprise can be made up a group of individuals and corporations, arguing that the statute provides an exclusive list of possible enterprises that covers groups of individuals associated in fact, not mixed groups of individuals and corporations associated in fact. Relying on D.C. Circuit precedent, which was in harmony with that of several other circuits, the circuit court stated that although "'[RICO] defines 'enterprise' as including the various entities specified; the list of entities is not meant to be exhaustive.' As such, a group of individuals, corporations, and partnerships associated in fact can qualify as a RICO 'enterprise,' even though section 1961(4) nowhere expressly mentions this type of association."[24]

In its certiorari petition, Philip Morris USA argues that the D.C. Circuit's reading is contrary to the basic canons of statutory interpretation. It argues that "[w]hile the first category of 'enterprises'—legal entities—expressly includes both corporations and individuals, the second category—unions and groups of individuals associated in fact—plainly does not."[25]

In the context of its case, Philip Morris argues that no legislative history supports the notion that the RICO statute was enacted to reach the actions—some of which may be speech protected by the First Amendment—made by an informal group of corporations attempting to influence government policy relating to a particular industry. "A corporation by itself may be within the ordinary and defined meaning of a RICO 'enterprise,' but one would not think of a group of unaffiliated corporations informally cooperating in an effort to influence government policy (much less a group of competing corporations) as a single 'enterprise.'"[26]

"Disgorgement" as a Remedy for RICO Violations. In addition to the five separate petitions filed by the defendants in the tobacco litigation, the Obama administration has filed a petition, asking the Supreme Court to restore the government's power to demand disgorgement of the tobacco companies' profits as a result of their

RICO violations. The government contends that the tobacco industry should forfeit the "ill-gotten gains" of its deceptive actions.

That issue was decided against the government in 2005 after a 2-1 panel of the D.C. Circuit Court ruled that language in the RICO statute giving courts jurisdiction to "prevent and restrain" RICO violations only allows for "forward-looking" remedies, where "disgorgement" of profits would be a "backward-looking" remedy in *United States v. Philip Morris USA Inc.*[27] The Supreme Court denied certiorari on that issue in October 2005, but commentators opine that the issue "remained alive" during the remainder of the case.[28]

A concurring opinion to the D.C. Circuit's 2005 decision wrote, "[t]he plain fact is that wealth deprivation is an extremely crude device for 'prevent[ing]' criminal behavior."[29] That being said, the court noted that the availability of disgorgement as a remedy in RICO actions is in question. For instance, the Second Circuit is among those that has held that disgorgement could, under limited circumstances, be considered a means of preventing and restraining future RICO violations and therefore permissible under the RICO statute.[30] Although an issue unique to civil cases, one commentator notes that the debate has broader implications with respect to statutory interpretation and preference of a mechanical, strict method versus one which "calls upon courts to make intelligent choices and, on appropriate occasions, to deviate from the most straightforward reading of statutory text."[31]

Recent Supreme Court Expansion of RICO Statute. The Supreme Court continues to indicate a willingness to read the RICO statute broadly. In *United States v. Boyle*,[32] a case arising out of the Second Circuit, the Supreme Court contemplated the definition of enterprise. In *Boyle*, the Court endeavored to resolve a dispute as to whether it was required that the association-in-fact enterprise have an "ascertainable structure" beyond a pattern of racketeering activity. The Court answered the question in three parts.

With respect to the association-in-fact enterprise's "structure," the Court held that the term required at least three structural features: a purpose, relationships among those associated with the enterprise, and longevity sufficient to permit the associates to pursue the enterprise's purpose. Second, the Court considered whether the structure must be "ascertainable." In the context of a criminal case, the Court found that term redundant, noting that "[w]henever a jury is told that it must find the existence of an element beyond a reasonable doubt, that element must be 'ascertainable' or else the jury could not find that it was proved."[33]

Finally, the Court considered whether the structure must go "beyond that inherent in the pattern of racketeering activity." Noting that an enterprise's "structure" and "a pattern of racketeering activity" were separate elements to be proven beyond a reasonable doubt, in some cases the evidence used to prove a pattern of racketeering activity and the evidence used to establish a structured enterprise may "coalesce."[34] The Supreme Court affirmed the RICO conviction of the defendant in *Boyle*, rejecting the argument that although an illegal RICO enterprise must have a "structure," the jury must be instructed as to its "ascertainable" nature. The Court went so far as to state that the jury instructions need not include the term "structure" at all.

Boyle is evidence of the Court's tendency toward broad interpretation of the statutory language set forth in the RICO statute, including the definition of "enterprise." The Court's expansive reading has been noted by courts within the Second Circuit, writing that "*Boyle* establishes a low threshold for [demonstrating]…an [association-in-fact] enterprise, requiring only 'a group of [entities] associated together for a common purpose of engaging in a course of conduct.'" Accordingly, it is no longer necessary to show that the enterprise possessed a "hierarchical structure" or "chain of command."[35]

If the Court decides to hear the tobacco companies' appeals, *Boyle* may portend another government victory and continued trend toward an ever-widening application of the RICO statute, especially when coupled with the extraterritoriality issue presented in BATCo's petition.

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1. Congressional Statement of Findings and Purpose, 18 USCA §1961.

2. Compare Federal Justice Statistics Resource Center, FY 2008 Number of Defendants in RICO Cases filed (totaling 166) with Federal Justice Statistics Resource Center, FY 1998 Number of Defendants in RICO Cases filed (totaling 214).

3. 566 F.3d 1095 (D.C. Cir. 2009).

4. Ellen S. Podgor, "A New Dimension to the Prosecution of White Collar Crime: Enforcing Extraterritorial Social Harms," McGeorge Law Review (2006).

5. See, e.g., 15 USC §§78dd-1 to -3.

6. See, e.g., 18 USC §1623(b) (perjury) (stating that statute is applicable whether the conduct occurred within or without the United States); 18 USC §1956(f) (money laundering) (providing for extraterritorial jurisdiction over prohibited conduct if: 1) the conduct is by a United States citizen or, in the case of a non-United States citizen, the conduct occurs in part in the United States; and 2) the transaction or series of related transactions involves funds or monetary instruments of a value exceeding $10,000).

7. *British American Tobacco (Investments) Limited v. United States*, Petition for a Writ of Certiorari, 08-980 (February 2010) (hereinafter referred to as "BATCo Petition").

8. 566 F.3d 1095 (D.C. Cir. 2009).

9. Id. at 1105-06.

10. Id. at 1130 (citing *Laker Airways Ltd. v. Sabena, Belgian World Airlines*, 731 F.2d 909, 923 (D.C. Cir. 1984)) (emphasis in original).

11. Id. at 1131.

12. BATCo Petition at p.i (citing *EEOC v. Arabian Am. Oil Co.*, 499 U.S. 244, 248 (1991)) (emphasis in original).

13. Id. at p. 23.

14. 100 F.3d 1046 (2d Cir. 1996).

15. Id. at 1052.

16. BATCo Petition at p. 18 (citing *Al-Turki*, 100 F.3d at 1052).

17. *Doe I v. State of Israel*, 400 F.Supp.2d 86, 115 (D.D.C. 2005).

18. BATCo Petition at pp. 24-27.

19. Ellen S. Podgor, "'Defensive Territoriality': A New Paradigm for the Prosecution of Extraterritorial Business Crimes," Georgia Journal of International and Comparative Law (Fall 2002).

20. Philip Morris USA Inc. Petition for a Writ of Certiorari , 09-976 (Feb. 19, 2010); Lorillard Tobacco Co. Petition for a Writ of Certiorari, 09-1012 (Feb. 19, 2010).

21. 18 USC §1962(c).

22. 18 USC §1961(3).

23. 18 USC §1961(4).

24. 566 F.3d at 1111 (citing *United States v. Perholtz*, 842 F.2d 343, 353 (D.C.Cir.1988)). See also, *United States v. Huber*, 603 F.2d 387, 394 (2d Cir.1979) (holding that corporations can be part of an association-in-fact enterprise because section 1961(4)'s list is not exhaustive).

25. Philip Morris Petition at pp. 24-25 (citations omitted).

26. Id. at pp. 25-26.

27. 396 F.3d 1190 (D.C. Cir. 2005), cert. denied, 126 S. Ct. 478 (2005).

28. Lyle Denniston, "U.S. Seeks $280 Billion Tobacco Remedy," SCOTUSBlog (Feb. 19, 2010).

29. 363 F.3d at 1204.

30. *United States v. Carson*, 52 F.3d 1173 (2d Cir. 1995).

31. Christopher L. McCall, "Equity Up in Smoke: Civil RICO, Disgorgement, and *United States v. Philip Morris*, Fordham Law Review (March 2006) (internal citations omitted).

32. 129 S.Ct. 2237 (2009).

33. Id. at 2244.

34. Id. at 2245 (citing *United States v. Turkette*, 452 U.S. 576, 583 (1981)).

35. See, e.g., *Elsevier Inc. v. W.H.P.R. Inc.*, __F.Supp.2d__, 2010 WL 710786, *7 (SDNY Feb. 19, 2010); *McGee v. State Farm Mut. Auto. Ins. Co.*, 2009 WL 2132439, *4 n. 7 (EDNY July 10, 2009).