A NECESSARY SUPPLEMENT: REINVIGORATING CIVIL RICO'S SECURITIES FRAUD PREDICATE

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In December 1995, Congress passed the Private Securities Litigation Reform Act ("PSLRA") over President Bill Clinton's veto.[1] Despite President Clinton's opposition, the new law commanded widespread, bipartisan support. PSLRA constituted a bold, wide-ranging attempt to restrict securities fraud litigation, which had become an unmitigated mess, according to some legislators.[2] PSLRA amounted to a wholesale revamp of the procedural and substantive rules that formed the core of the private securities enforcement regime in the United States. Among other changes to this regime—most of which attracted far more notice from academics, legal practitioners, and judges—PSLRA amended the United States Code to remove securities fraud predicates from the reach of what has become known, colloquially, as "Civil RICO."[3]

Congress passed the Racketeer and Influenced Corrupt Organizations Act ("RICO") in 1970, as part of a comprehensive effort to attack organized crime.[4] "RICO was an aggressive initiative to supplement old remedies and develop new methods for fighting crime."[5] Although RICO is most familiar as a tool for high-profile federal prosecutions of organized crime figures,[6] it also contains a lesser-known series of provisions, which permits private citizens to initiate civil actions against criminal enterprises.[7] Civil RICO's private remedy offers those affected by ongoing criminal behavior a means of personal redress beyond the state-directed mechanisms of the criminal justice system. Victims of corporate and securities fraud seized this opportunity by suing criminal enterprises, which perpetrated not only traditional organized crime, but white-collar crime as well.

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1 Private Securities Litigation Reform Act of 1995, Pub. L. No. 104-67, 109 Stat. 737 (codified as amended in scattered sections of 15 U.S.C.).

2 *See, e.g.*, 141 CONG. REC. 38319 (1995) (statement of Sen. Alfonse D'Amato) ("This system as it stands is encouraging the kind of operation that hurts small investors and makes no sense . . . .").

3 *See* 18 U.S.C. § 1964(c) (2012).

4 RICO is codified at 18 U.S.C. § 1961 (2012).

5 Sedima, S.P.R.L. v. Imrex Co., 473 U.S. 479, 498 (1985).

6 *See* Ed Magnuson et al., *Cover Stories Hitting the Mafia: A Wave of Trials is putting the Nation's Crime Bosses Behind Bars*, TIME, Sept. 29, 1986, at 16 (crediting RICO with helping to destroy La Cosa Nostra, perhaps the best-known organized crime syndicates at the time). RICO's prominence as an anti-Mafia tool has pervaded pop culture; a memorable exchange in the pilot episode of *The Sopranos* involves Tony Soprano confessing to his psychiatrist that he is anxious because of the "RICO statutes."

7 The civil component of RICO is codified at 18 U.S.C. § 1964(c).

Over the course of a quarter-century, Civil RICO emerged as an important litigation tool for shareholders seeking to recoup their losses from perpetrators of securities fraud.[8] Among the reasons for Civil RICO's popularity as a remedy was the fact that the statute allowed successful plaintiffs to recover treble damages, in addition to attorneys' fees and court costs.[9] A Civil RICO action thus carried pragmatic advantages over other tort actions that could yield fewer tangible benefits for plaintiffs and their attorneys. The added severity of Civil RICO may also have encouraged early, plaintiff-friendly resolution of claims.

PSLRA added a sentence to Civil RICO's statutory provisions, which severely undercut its usefulness as a civil remedy for victims of securities fraud. Post-PSLRA, the Civil RICO statute states that "no person may rely upon any conduct that would have been actionable as fraud in the purchase or sale of securities to establish a violation of section 1962."[10] Additionally, PSLRA removed mail and wire fraud[11] relating to securities fraud from the list of actionable predicates for Civil RICO.[12] These seemingly small changes to the statute significantly affected the Civil RICO regime.

Eliminating the securities fraud predicate for Civil RICO was only one way in which PSLRA limited injured parties' ability to successfully sue perpetrators of securities fraud.[13] PSLRA's restrictions on litigation have not been loosened by later legislation; in fact, Congress subsequently passed additional laws that further restricted plaintiffs' attempts to seek compensation for losses resulting from securities fraud.[14] These limitations on fraud victims' options for economic redress, coupled with several Supreme Court decisions that further constrained the ambit of securities fraud litigation,[15] heighten the need for Congress to rebalance a system which currently weighs heavily against victims of securities fraud. One way of doing so would be to partially reverse PSLRA's changes to Civil RICO. Civil RICO should be amended to permit

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[8] *See Sedima*, 473 U.S. at 499. In particular, see note 16 therein, which pointed to two studies noting that a plurality of Civil RICO factions—at the time—cited securities fraud as a predicate. *Id.* at 499 n.16.

[9] 18 U.S.C. § 1964(c) ("Any person . . . shall recover threefold the damages he sustains and the cost of the suit, including a reasonable attorney's fee . . . .").

[10] 18 U.S.C. § 1964(c).

[11] *See* 18 U.S.C. §§ 1341, 1343 (2012) (criminalizing the use of the mails or wires in service of a "scheme or artifice to defraud").

[12] *See* Douglas E. Abrams, *Crime Legislation and the Public Interest: Lessons from Civil RICO*, 50 SMU L. REV. 33, 35 n.15 (1996) ("The 1995 Securities Litigation Reform Act amended only 18 U.S.C. § 1964(c), the provision creating civil RICO, the private treble-damages remedy. The 1995 Act left untouched the government's criminal and civil remedies created by 18 U.S.C. §§ 1963 and 1964(a) and (b), respectively."); see also 2 Sec. Counseling for Small & Emerging Companies § 201:11 (2009), which notes that mail and wire fraud were also eliminated as predicate RICO acts if such conduct also constituted securities fraud. For more information relating to mail and wire fraud, see H.R. Rep. No. 104-369, at 47 (1995).

[13] Mary Kreiner Ramirez, *Just in Crime: Guiding Economic Crime Reform after the Sarbanes-Oxley Act of 2002*, 34 LOY. U. CHI. L.J. 359, 403, 403 n.235, 404 nn.236-38 (2003).

[14] *See infra* Part I.B.

[15] See *infra* Part I.C (discussing such judicial restraints placed on private enforcement efforts).

more lawsuits based on securities fraud predicates, though other limitations should be put into place in order to prevent meritless litigation.

In this Article, I argue that the judicial and legislative restraints on securities fraud litigation have fostered a situation whereby remedies available to victims of securities fraud are too limited. Congress should restore securities fraud as a predicate for Civil RICO actions; in doing so, it will enhance the options available to victims, with few of the negative ramifications feared by Civil RICO's detractors.

Part One of this Article outlines the restrictive scheme that PSLRA and its judicial and legislative progeny have imposed on attempts to litigate securities fraud. Part Two recounts the rise and fall of Civil RICO as a remedy for victims of securities fraud.[16] Part Three explains how reinstating Civil RICO, while incorporating several legal mechanisms designed to avoid the problems that led to Civil RICO's redefinition under PSLRA, is a sensible approach which will enhance the reliability, fairness, and integrity of American securities markets.

I. PRIVATE SECURITIES LITIGATION: A MODERN HISTORY

A. Private Enforcement: A "Necessary Supplement"

Securities regulation serves an important national interest.[17] The Supreme Court has noted that "[t]he magnitude of the federal interest in protecting the integrity and efficient operation of the market for nationally traded securities cannot be overstated."[18] A formal regulatory regime for securities emerged in the United States at the height of the Great Depression, with the passage of the Securities Act of 1933 and the Securities Exchange Act of 1934.[19] These laws established the Securities and Exchange Commission (SEC), the primary federal agency tasked with monitoring and enforcing securities laws, and created a framework for the effective regulation of securities trading.[20] Yet

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[16] Civil RICO necessarily requires the existence of a criminal enterprise and predicate activity. This requirement is unusual given the exclusively civil nature of the remedy. The grey space between criminal and civil has received increasing attention in recent years. Professors Thomas Koenig and Michael Rustad have used the term "Crimtorts" in relation to the middle ground between crime and tort. In 2008, the *Widener Law Journal* hosted a symposium, which addressed some of the issues arising out of this new grey area of the law. *See* Symposium, *Crimtorts Videos*, WIDENER L.J. (Feb. 25, 2008), http://law.widener.edu/NewsandEvents/Articles/2008/hb022908crimtorts/CrimtortsVideos.aspx.

[17] *See, e.g.*, 15 U.S.C. § 78b (2012) (stating that securities trading is "affected with a national public interest" and that unfair markets can lead to "national emergencies"). For a helpful discussion of behavioral theories underlying securities regulation and litigation, see Robert Prentice, *Whither Securities Regulation? Some Behavioral Observations Regarding Proposals For Its Future*, 51 DUKE L.J. 1397 (2002).

[18] Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Dabit, 547 U.S. 71, 78 (2006).

[19] Securities Act of 1933, Pub. L. No. 73-22, 48 Stat. 74 (codified as amended at 15 U.S.C. §§ 77a-77mm (2012)); Securities Exchange Act of 1934, Pub. L. No. 73-291, 48 Stat. 881 (codified as amended at 15 U.S.C. §§ 78a-78kk (2012)).

[20] A primary goal of the legislation was to protect consumers from the manipulation of

government action was never intended to be the sole weapon for enforcing the securities laws and ensuring that securities markets operated in a fair and efficient manner. For decades, private litigation has been an "essential tool for enforcement of the 1934 Act's requirements."[21]

Indeed, Congress' push to limit private securities litigation in the 1990s was a departure from the healthy American tradition of private securities enforcement.[22] Alongside the SEC, a system of "private attorneys general" emerged over the course of the twentieth century to protect investors from, and seek compensation for, criminal and tortious securities fraud.[23] This model mirrors private enforcement principles which have developed in other contexts;[24] the rise of the *qui tam* action is but one prominent example of the overall consensus that government action alone is often insufficient when it comes to enforcing complex areas of economic activity.[25]

Private securities enforcement is rooted in Section 10(b) of the 1934 Act, and Rule 10b-5, promulgated by the SEC pursuant to that section.[26] The Supreme Court's 1964 determination that "[p]rivate enforcement of the proxy rules [found in the Securities Exchange Act of 1934] provides a necessary supplement to [SEC] action" created the legal foundation for non-governmental entities to use civil actions to regulate the securities industry and recoup related losses.[27] Over the years, the courts and Congress have refined this basic premise so that the "private damages action . . . resembles, but is not identical to, common-law tort actions for deceit and misrepresentation."[28]

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stock prices. *See* S. REP. NO. 73-792, at 1 (1934).

[21] Basic Inc. v. Levinson, 485 U.S. 224, 230-31 (1988). Of course, some argue that the opposite is true. The existence of a private right of action implied under Rule 10b-5, which is the most common source of private securities litigation, has been referred to as a "judicial oak which has grown from little more than a legislative acorn[,]" and is considered illegitimate by a minority of scholars and judges. *See* Amanda M. Rose, *Reforming Securities Litigation Reform: Restructuring the Relationship Between Public and Private Enforcement of Rule 10B-5*, 108 COLUM. L. REV. 1301, 1302-03 (2008).

[22] I refer to this as an "ongoing push" because PSLRA was not the final Congressional attempt to restrict private securities enforcement. The Securities Litigation and Uniform Standards Act, *infra* Part I.B, is an example of Congress' attempt to further restrict private enforcement. Securities Litigation and Uniform Standards Act of 1998, Pub. L. No. 105-353, 112 Stat. 3227 (codified at 15 U.S.C. § 78a (2012)).

[23] Elizabeth Chamblee Burch, *Securities Class Actions as Pragmatic Ex Post Regulation*, 43 GA. L. REV. 63, 74-75 (2008). Some argue that private litigation is effective *ex post* but not in deterring improper activity *ex ante*. *See, e.g.*, *id.* at 92-97.

[24] For a critical, albeit older, view of the private enforcement model, see John C. Coffee, Jr., *Rescuing the Private Attorney General: Why the Model of the Lawyer as Bounty Hunter is Not working*, 42 MD. L. REV. 215, 243-45 (1983) (discussing "perversely misguided" incentives for private attorneys general).

[25] For an excellent history of *qui tam* actions in the United States, see Vermont Agency of Natural Resources v. United States *ex rel.* Stevens, 529 U.S. 765, 774-77 (2000).

[26] 17 C.F.R. § 240.10b-5 (2013).

[27] J.I. Case Co. v. Borak, 377 U.S. 426, 432 (1964) (recognizing that shareholders enjoy an implied private right of action to enforce violations of the proxy rules of the Securities Exchange Act of 1934).

[28] Dura Pharm., Inc. v. Broudo, 544 U.S. 336, 341 (2005) (citing legislative amendments and judicial interpretations which have affected this implied cause of action).

Private enforcement works because "the possibility of civil damages or injunctive relief serves as a most effective weapon" for enforcement of securities laws, even if it requires an occasional blurring of the lines between the spheres of civil and criminal law.[29]

This blurring reflects the fact that private enforcement serves a purpose greater than that of everyday tort actions on behalf of injured parties. Unlike most civil litigation, the private enforcement regime seeks to punish wrongdoers and deter future criminal behavior,[30] and thereby assumes a distinctive regulatory role.[31] Securities fraud lawsuits are about more than mere compensation.

Private enforcement is especially vital in light of the difficulties faced by regulatory agencies in confronting and preventing securities fraud.[32] James Cox and Randall Thomas, in a series of studies of the SEC's enforcement practices, have discussed the regulatory agency's issues and challenges in enforcing the securities laws.[33] Cox and Thomas point to uneven SEC enforcement, spurred by severe limitations placed on the agency as a result of resource shortages.[34] Furthermore, they have argued that the SEC often focuses on cases that are less likely to be targeted by private plaintiffs, pointing out that overlap between private and public plaintiffs in the securities enforcement arena is relatively uncommon.[35] In particular, they note that the SEC does not select its enforcement targets based on the magnitude of investor losses;[36] rather, other factors—such as the nature and complexity of the fraudulent scheme, or the depth of the public outcry regarding a specific instance of fraud[37]—play an important role in determining how the SEC

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[29] *Borak*, 377 U.S. at 432.

[30] Deterrence and punishment are cited among the primary purposes of securities enforcement. *See generally* John C. Coffee, Jr., *Reforming the Securities Class Action: An Essay on Deterrence and Its Implementation*, 106 COLUM. L. REV. 1534 (2006) (offering excellent background reading about the underlying motivations of securities litigation).

[31] *Dura*, 544 U.S. at 345 (citing Randall v. Loftsgaarden, 478 U.S. 647, 664 (1986)).

[32] The purpose of this paper is not to discuss the SEC's ability to enforce securities regulation; in fact, the Commission does a laudable job. However, there have been noted cases of SEC failure in recent years. *See, e.g.*, Gretchen Morgenson, *Following Clues the SEC Didn't*, N.Y. TIMES, Feb. 1, 2009, at BU.1 (discussing the SEC's failure to investigate both Bernard Madoff's $50 billion fraud and a second fraud at Allied Capital, despite numerous leads concerning both frauds). Ultimately, the SEC's ability to confront securities fraud is cabined by a host of legal and practical limitations. *See* Laura A. McDonald, *Restoring the Balance After the Private Securities Litigation Reform Act of 1995,* 38 FLA. ST. U. L. REV. 911, 912-13 (2011).

[33] *See* James D. Cox & Randall S. Thomas, *SEC Enforcement Heuristics: An Empirical Inquiry*, 53 DUKE L.J. 737, 737 (2003).

[34] *Id.* at 757-58.

[35] James D. Cox & Randall S. Thomas, *Mapping the American Shareholder Litigation Experience: A Survey of Empirical Studies of the Enforcement of the U.S. Securities Law*, DUKE LAW SCHOLARSHIP REPOSITORY 1, 9 (2010) [hereinafter *Mapping*], *available at* http://lsr.nellco.org/ duke_fs/171.

[36] *Id.*

[37] It is not necessarily clear if the SEC is an independent or executive agency. *See* Note, *The SEC is Not an Independent Agency*, 126 HARV. L. REV. 781, 781 (2013).

expends its limited resources.[38] This lack of overlap evidences the fact that private enforcement is important for both regulating the securities industry and ensuring that victims are properly compensated.

Indeed, while the aims of deterrence and punishment are important to understanding the unique place of private securities enforcement as compared to the rest of the tort system, compensation, the overarching purpose of most tort actions, still acts as a primary motivator for civil actions. In the absence of private enforcement, it is not clear that victims of securities fraud would be able to easily recover their losses.[39] Adversarial private litigation is often the primary, and most efficient, means of accomplishing this goal and obtaining compensation for victims.[40]

For these reasons, government enforcement is simply inadequate; it cannot address the full range of securities law violations, and it focuses on different ends than private enforcement. Robust private litigation is, therefore, critical to ensuring the viability and integrity of the American securities markets.

However, private securities enforcement is far from perfect. As one author argues, neither of the two primary objectives of private securities enforcement—deterrence and compensation—is satisfied by the existing regime; in fact, securities fraud may even be overdeterred.[41] In 2008, the Supreme Court warned that private securities enforcement "may raise the cost of being a publicly traded company under our law and shift securities offerings away from domestic capital markets."[42]

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[38] For a discussion of the uptick in SEC enforcement actions in the early 21st century, in the wake of the Enron scandal, see James Cox et al., *Public and Private Enforcement of the Securities Laws: Have Things Changed Since Enron?*, 80 NOTRE DAME L. REV. 893, 899 (2005).

[39] Howell Jackson has calculated the annual financial sanctions imposed for securities law violations between 2000 and 2002, and determined that public monetary sanctions totaled $1,864,409,277, while private monetary sanctions totaled $2,027,959,333, of which greater than 95% came from private class actions. *See* Howell E. Jackson, *Variation in the Intensity of Financial Regulation: Preliminary Evidence and Potential Implications*, HARVARD LAW. SCH. JOHN M. OLIN CTR. FOR LAW, ECON. & BUS., Discussion Paper 521, at 27 (Aug. 18, 2005), *available at* www.law.harvard.edu/programs/olin_center/papers/pdf/Jackson_521.pdf. However, a later study by Jackson, which calculated 2002-04 actions, found public enforcement to be more monetarily successful. This difference is likely attributed to enhanced SEC powers and a wave of securities enforcement actions—both public and private—in the wake of the corporate scandals of the early 21st century and the subsequent passage of Sarbanes-Oxley. *See* Howell E. Jackson, *Variation in the Intensity of Financial Regulation: Preliminary Evidence and Potential Implications*, 24 YALE J. ON REG. 253, 280 (2007).

[40] Criminal asset forfeiture statutes, such as 18 U.S.C. §§ 982 and 1963 (2012), and civil forfeiture actions brought by agencies such as the SEC, may be inadequate to compensate victims given both the government's limited resources to bring such actions and the heightened standards of proof required in the criminal context.

[41] *See* Rose, *supra* note 21, at 1303.

[42] Stoneridge Inv. Partners v. Scientific-Atlanta, Inc., 552 U.S. 148, 164 (2008). *Stoneridge* may prove to be the high point of the Supreme Court's skepticism about securities fraud litigation. In a 5-3 decision, the *Stoneridge* Court adopted several definitions which constrained securities fraud actions brought pursuant to § 10(b). *Id.* Notably, the decision in *Stoneridge* was announced on January 15, 2008 and was the last major securities fraud case decided by the Court prior to the wave of major bank failures which precipitated the global financial crisis. *Id.* More recent decisions, such as *Amgen Inc. v. Connecticut Retirement Plans and Trust Funds*, 133 S. Ct.

Beyond the problems peculiar to private securities enforcement, the full range of criticisms leveled at other expansive, expensive litigation is often directed at securities litigation. Some complain that securities litigation, which frequently employs the class action vehicle, yields little in actual benefits for the victims of securities fraud, and that the spoils of such lawsuits merely line the pockets of plaintiffs' attorneys.[43]

The argument that plaintiffs' lawyers are the only true beneficiaries of private securities enforcement was key to PSLRA's passage.[44] PSRLA's opponents hurled invective at so-called "strike suits." Defined as "meritless suits brought by class action plaintiffs' lawyers to extort settlement and attorneys' fees,"[45] strike suits were among the motivations cited by Congress in the run-up to PSLRA's passage.[46] PSLRA-supporting Members of Congress, argued that they were in fact protecting private securities system, and claimed that the system was being "undermined by those who seek to line their own pockets by bringing abusive and meritless suits."[47] Anti-plaintiff rhetoric is a common feature of debates about securities litigation,[48] and it constituted much of the basis for PSLRA's support in Congress.[49]

However, while "there is at least a strong public perception of a securities litigation crisis," empirical evidence in this regard has traditionally proven inconclusive.[50] Furthermore, the legitimate concern over strike suits is neither new nor notable. Nearly four decades ago, the Supreme Court addressed this concern by limiting § 10(b) standing to those who suffered directly as a result of securities fraud—the so-called "purchaser-seller requirement."[51] In *Blue Chip Stamps*, the Court noted that during the Congressional debates over the 1934 Act, the problem of strike suits was discussed as a possibility, indicating that Congress anticipated the potential for widespread abuse of the regulatory

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1184 (2013), demonstrate that the Court's skepticism may have receded somewhat. At the time of this writing, the Court had recently granted *certiorari* in a case that asks it to reconsider the "fraud on the market" theory first advanced in *Basic*. *See* Halliburton Co. v. Erica P. John Fund, Inc., 134 S. Ct. 636, 636 (2013).

[43] Cox & Thomas, *supra* note 35, at 13.

[44] "The private securities litigation system is too important to the integrity of American capital markets to allow this system to be undermined by those who seek to line their own pockets by bringing abusive and meritless suits." H.R. REP. NO. 104-369 at 31 (1995) (Conf. Rep.), *reprinted in* 1995 U.S.C.C.A.N. 730, 730.

[45] Amanda M. Rose, *Life after SLUSA: What Is the Fate of Holding Claims?* 69 DEF. COUNS. J. 455, 455 (2002).

[46] *Id.*

[47] *See* "Statement of Managers," H.R. CONF. REP. NO. 104-369, at 31 (1995) (Conf. Rep.), *reprinted in* 1995 U.S.C.C.A.N. 730, 1995 WL 709276 at *30.

[48] *See infra* Part I.B.

[49] For a discussion of the PSLRA Congress' misplaced reliance on academic studies which alleged a "strike suit" crisis, see Leonard B. Simon & William S. Dato, *Legislating on a False Foundation: The Erroneous Academic Underpinnings of the Private Securities Litigation Reform Act,* 33 SAN DIEGO L. REV. 959, 962 (1996).

[50] John W. Avery, *Securities Litigation Reform: The Long and Winding Road to the Private Securities Litigation Reform Act of 1995*, 51 BUS. LAW. 335, 340 (1996).

[51] Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 723, 731-32 (1975).

scheme it was creating.[52] However, while meritless litigation is a problem, wholesale restriction of private securities enforcement is not the solution. Rather, courts and Congress should take measured steps to prevent strike suits from reaching problematic levels. Paring down problematic statutes and regulations is a far more sensible approach than destroying useful remedies in their entirety.

B. PSLRA: From Veto to Law

PSLRA was Congress' attempt to address many of the concerns surrounding private securities enforcement.[53] With the election of a powerful Republican Congress in 1994, advocates for limiting private securities litigation began to assemble the pieces of what would later become PSLRA.[54] While supporters of PSLRA railed generally against "abusive practices committed in private securities litigation,"[55] the path to passing PSLRA was complicated by confusion over its suggested remedies, and a lack of clarity regarding which problems the bill sought to address.[56]

As much as it engendered strong support, the bill also encountered substantial opposition. Leading legal academics lobbied heavily against the bill. Arthur Miller predicted that PSLRA would "destroy the private enforcement capacities that have been given to investors to police our nation's marketplace."[57] John Sexton warned that "real victims [would] be prevented from seeking redress" were the bill to become law.[58] Some legislators opposed the bill as well. During the initial debates, Rep. John Dingell (D-MI) took a

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[52] *Blue Chip Stamps*, 421 U.S. at 740-41.

[53] The Washington Post published an influential editorial calling for the veto override. Editorial, *Override the Securities Bill Veto*, WASH. POST, Dec. 22, 1995, at A18. The editorial said that the existing state of the law created "real and substantial injustices," which had fostered "egregious misuse of securities laws." *Id.* This editorial was entered into the Congressional Record by more than one senator on December 22. *See* 141 CONG. REC. 38,319 (1995) (statement of Sen. D'Amato); 141 CONG. REC. 38,322-23 (1995) (statement of Sen. Domenici); 141 CONG. REC. 38,326 (1995) (statement of Sen. Dodd). The consensus that private securities enforcement was badly broken reached even many liberal Democrats; Sen. Bill Bradley (D-NJ), in supporting the veto, stated that "frivolous lawsuits act as a damper on economic growth . . . [and] impose a burden on the economy and should be stopped." 141 CONG. REC. 38,322 (1995) (statement of Sen. Bradley).

[54] Tort reform was a key component of the Republican Party's pre-election platform. The "Contract with America," the House Republicans' list of pre-election proposals, included a "common sense legal reform act" intended to "stem the endless tide of litigation." *See* CONTRACT WITH AMERICA, accessed at http://www.nationalcenter.org/ContractwithAmerica.html (last visited Apr. 25, 2014).

[55] *See* "Statements of Managers," *supra* note 47, at 41.

[56] For more details on the legislative history behind PSLRA, see Avery, *supra* note 50, at 337.

[57] 141 CONG. REC. 38,199 (1995) (letter from Professor Arthur R. Miller of Harvard Law School).

[58] *See* 141 CONG. REC. 38,201 (1995) (letter from Dean John Sexton of New York University School of Law). Sen. Harry Reid (D-NV), a supporter of PSLRA, launched a serious broadside against Sexton during floor debate, implying that Sexton's opposition to the bill was motivated by a conflict of interest spurred by his role as Dean of NYU Law School. *See* 141 CONG. REC. 38,244-45 (1995) (statement of Sen. Reid).

harsher tone, calling PSLRA "outrageous legislation" that "should be rejected."[59]

President Clinton vetoed the bill, citing a fear of "closing the courthouse door on investors who have legitimate claims."[60] Clinton's veto was to no avail—PSLRA was one of only two vetoes overridden by Congress during the course of his presidency.[61] The House approved the override 319-100; the Senate barely did, by a 68-30 vote.[62]

PSLRA employed a multifaceted approach to rein in private securities litigation. Congress' primary focus was on tightening pleading standards, which it hoped would restrict frivolous Rule 10b-5 lawsuits from being brought, and stall meritless litigation prior to discovery.[63] These heightened pleading standards are among the most significant components of PSLRA.[64]

PSLRA requires a plaintiff, suing for securities fraud, to specifically outline the material misrepresentations alleged to constitute fraud on the market.[65] The plaintiff must pinpoint, in detail, "each statement alleged to have been misleading," as well as "the reason or reasons why the statement is misleading."[66] The statute further requires that "if an allegation regarding the statement or omission is made on information and belief, the complaint shall state with particularity all facts on which that belief is formed."[67] Under the statutory scheme established by PSLRA, failure to specifically explain the nature of misleading securities statements inevitably leads to dismissal.[68]

PSLRA also imposes a clear scienter requirement.[69] A plaintiff must allege that the defendant in a securities fraud action possessed a particular

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[59] 141 CONG. REC. 7127 (1995) (statement of Rep. John Dingell).

[60] 141 CONG. REC. 37,797 (1995) (veto message of President Clinton). For a full articulation of Administration issues with PSLRA, see also Statement of Administration Policy on S. 240 (June 23, 1995) (on file with *The Business Lawyer*, University of Maryland School of Law).

[61] MITCHEL A. SOLLENBERGER, CONG. RESEARCH SERV., 98-147, PRESIDENT CLINTON'S VETOES CRS 3 (2004), *available at* http://archives.democrats.rules.house.gov/archives/98-147.pdf. The other veto that Congress overrode was a line-item veto of certain projects, H.R. 2631, on November 13, 1997. *Id.*

[62] 141 CONG. REC. 37,807 (1995); 141 CONG. REC. 38,354 (1995).

[63] Kevin S. Shmelzer, *The Door Slammed Shut Needs to be Reopened: Examining the Pleading Requirements Under the Private Securities Litigation Reform Act*, 78 TEMP. L. REV. 405, 421 (2005).

[64] For a discussion of how PSLRA's heightened pleading requirements developed, see *id.* at 408-21.

[65] It should be noted that allegations of fraud are required to be pleaded with "particularity." FED. R. CIV. P. 9(b).

[66] 15 U.S.C. § 78u-4(b)(1) (2012).

[67] *Id.*

[68] 15 U.S.C. § 78u-4(b)(3)(A).

[69] *See* 15 U.S.C. § 78u-4(b)(2). A pre-PSLRA circuit split on the pleading standard for scienter was a prime motivator for PSLRA. Christopher J. Miller, *"Don't Blame Me, Blame the Financial Crisis": A Survey of Dismissal Ruling on 10b-5 Suits for Subprime Securities Losses*, 80 FORDHAM L. REV. 273, 283 (2011). *Compare* GlenFed, Inc. Sec. Litig., 42 F.3d 1541, 1546-47 (9th Cir. 1994) (requiring that plaintiff merely state that scienter existed), *with* Shields v. Citytrust Bancorp, Inc., 25 F.3d 1124, 1127-28 (2d Cir. 1994) (requiring that plaintiff state particular facts that give rise to a "strong inference" of scienter) *and* Greenstone v. Cambex Corp., 975 F.2d 22, 25-26 (1st Cir. 1992) (requiring a plaintiff to allege specific facts in support of a general averment).

inculpatory state of mind.[70] The plaintiff must further demonstrate that the defendant either knew of the statement's false and misleading nature or was reckless in that failure to know.[71] A plaintiff must plead the allegations which establish scienter with particularity to each alleged misleading statement—outlining "facts giving rise to a strong inference that the defendant acted with the required state of mind."[72] The Supreme Court recently interpreted this section of the statute to require that plaintiffs show a "cogent inference" of scienter, which is "at least as compelling as any opposing inference of nonfraudulent intent."[73] Since the defendant's state of mind is often difficult to ascertain in the absence of discovery, this imposes a serious handicap on private securities enforcement.

Additionally, PSLRA stipulates that a plaintiff suing under Rule 10b-5 has "the burden of proving that the act or omission of the defendant . . . caused the loss for which the plaintiff seeks to recover damages."[74] The Supreme Court has ruled that this allegation of loss causation must be made in the initial complaint.[75] Functionally, this requires plaintiffs in Rule 10b-5 motions to outline the crux of their tort allegation—causation—at the earliest stage of the litigation.

The primary rationale for heightened pleading is to avoid discovery, which can be expensive, cumbersome, and time-consuming.[76] Indeed, PSLRA also imposes a stay on discovery while a motion to dismiss is pending.[77] The collective effect of these restrictions, which seek to discourage strike suits brought by overzealous attorneys, is to enhance the efficiency of private securities enforcement. However, some allege that in limiting discovery and making civil litigation more efficient, these restrictions also hobble legitimate attempts to seek redress.[78]

PSLRA implemented several additional changes to existing law, which further restricted securities-related lawsuits. Among the various provisions, the Act:

- Mandated the assessment of sanctions for violations in line with Federal Rule of Civil Procedure 11(b), which controls pleadings that contain factual errors.[79]
- Implemented a system of proportionate liability in securities fraud situations involving multiple defendants.[80]

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[70] 15 U.S.C. § 78u-4(b)(2)(A).

[71] 15 U.S.C. § 78u-4(b)(2)(B).

[72] 15 U.S.C. § 78u-4(b)(2)(A).

[73] Tellabs, Inc. v. Makor Issues & Rights, Ltd., 551 U.S. 308, 314, 323-24 (2007).

[74] 15 U.S.C. § 78u-4(b)(4).

[75] Dura Pharm., Inc. v. Broudo, 544 U.S. 336, 346-48 (2005).

[76] Burch, *supra* note 23, at 79.

[77] 15 U.S.C. § 78u-4(b)(3)(B).

[78] Laura A. McDonald, *Restoring the Balance After the Private Securities Litigation Reform Act of 1995*, 38 FLA. ST. U. L. REV. 911, 931 (2011). For an excellent summary of the changes wrought by the PSLRA see *id.* at 928-31.

[79] 15 U.S.C. § 78u-4(c)(2).

[80] 15 U.S.C. § 78u-4(f)(2)(B)(i).

- Created a "safe harbor" for forward-looking statements issued by companies and affiliated persons, thus restricting litigation arising out of such statements.[81]
- Provided that class actions would be consolidated under the guidance of a lead plaintiff, in the hopes of streamlining complex and lengthy litigation.[82]

The aforementioned provisions have been the most meaningful and thus have attracted the most scholarly, judicial, and political attention.[83] Although not discussed nearly as much in these precincts as modifications in the pleading requirements, the provision that restricts the private cause of action under Civil RICO is a significant part of PSLRA. Later in this Article, I outline the history of Civil RICO and discuss the legislative treatment of Civil RICO within PSLRA.[84]

C. Further Restrictions on Private Securities Enforcement

PSLRA was passed against the backdrop of an increasingly conservative and business-friendly Supreme Court, which sought to restrict private securities enforcement and civil litigation generally. The aforementioned cases, *Tellabs* and *Dura Pharmaceuticals*, are examples of restrictive construction of PSLRA.[85] The Court's interpretations of PSLRA fit with other limitations it has imposed in recent years on private securities litigation.[86]

Furthermore, in recent times, the Court's overall attitude towards procedural matters has evinced skepticism of private plaintiffs and their claims. The Court has interpreted pleading rules to require stricter, heightened pleading for an array of civil actions.[87] These restrictions have further complicated attempts to recover damages for securities fraud.

Since PSLRA, Congress has passed additional legislation which adds to the restrictions on private enforcement found in PSLRA. The Securities Litigation Uniform Standards Act of 1998 (SLUSA) expressly preempted class actions

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[81] 15 U.S.C. § 78u-5(c).

[82] 15 U.S.C. § 78u-4(a)(3)(B)(i). It should be noted, of course, that Congress has taken many further steps to restrict and reform class actions, of all varieties, in recent years.

[83] There is a paucity of scholarly literature addressing PSLRA's modifications of Civil RICO. *See, e.g.*, McDonald, *supra* note 78, at 928-31.

[84] *See infra* Part II.

[85] *See* Tellabs, Inc. v. Makor Issues & Rights, Ltd., 551 U.S. 308, 323-24 (2007).

[86] *See, e.g.*, Stoneridge Inv. Partners v. Scientific-Atlanta, Inc., 522 U.S. 148 (2008). As mentioned earlier, this may have been the high point of restrictive securities fraud interpretations.

[87] *See*, *e.g.*, Ashcroft v. Iqbal, 556 U.S. 662, 678 (2009) (requiring heightened pleading standards where plaintiff alleged violations of his civil rights by governmental officials); Bell Atlantic v. Twombly, 550 U.S. 544, 556 (2007) (requiring heightened pleading standard where plaintiff alleged that the "Baby Bells" engaged in parallel conduct discouraging competition); *see also* Arthur R. Miller, *From* Conley *to* Twombly *to* Iqbal: *A Double Play on the Federal Rules of Civil Procedure*, 60 DUKE L.J. 1, 10 (2010) (describing "a long-term trend that has favored increasingly early case disposition in the name of efficiency, economy, and avoidance of abusive and meritless lawsuits").

for securities fraud, preventing them from being brought in state courts, which are often perceived as more plaintiff-friendly than their federal counterparts.[88] "Sarbanes-Oxley," as the landmark 2002 securities reform law is commonly known,[89] addresses securities fraud through enhanced criminal penalties and regulatory provisions, although it hardly affects private securities enforcement. The same is true of "Dodd-Frank," a major 2010 law that focuses on structural issues in the securities markets but not on private enforcement remedies.[90] While Dodd-Frank adds to the SEC's enforcement arsenal, with provisions that permit the agency to bring more expansive civil litigation, the law does not meaningfully change the playing field of private civil enforcement.[91]

To some degree, PSLRA reforms, which sought to stymie private enforcement, have contributed to freer, but riskier, securities markets.[92] One scholar accuses PSLRA of fostering a "decade of decadence," visible in the seemingly never-ending scandals of the period.[93] As just one example, the fraud epidemic of the early 2000s—in which corporate titans such as Enron, WorldCom, Adelphia, and others were exposed as paper tigers. There is little reason to believe that the current regime, in place since 1995, is adequate, in and of itself, to deter securities fraud, punish the predators, and compensate the victims.

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[88] Securities Litigation Uniform Standards Act of 1998, Pub. L. No. 105-353, sec. 101, § 16(b), 112 Stat. 3227, 3228 (codified as amended at 15 U.S.C. § 78bb(f) (2012)); *see also* David M. Levine & Adam C. Pritchard, *The Securities Litigation Uniform Standards Act of 1998: The Sun Sets on California's Blue Sky Laws*, 54 BUS. LAW. 1, 3 (1998) (discussing how state laws were far more permissive). A unanimous Supreme Court subsequently held that SLUSA preempted state securities class actions. *See* Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Dabit, 547 U.S. 71 (2006) (adopting Seventh Circuit broad interpretation of SLUSA).

[89] Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745 (codified as amended in §§ 11, 15, 18, 28, and 29 U.S.C.). Commonly referred to as Sarbanes-Oxley after the lead Senate (Sen. Paul Sarbanes, D-MD) and House (Rep. Michael Oxley, R-OH) members, this law is considered one of the most significant legislative attempts to address securities regulation in the last fifty years. *See* Andre Douglas Pond Cummings, *"Ain't No Glory in Pain": How the 1994 Republican Revolution and the Private Securities Litigation Reform Act Contributed to the Collapse of the United States Capital Markets*, 83 NEB. L. REV. 979, 1059-64 (2005) (critiquing the Act's attempt to "recapture any lost protections or federal regulations given away in the PSLRA").

[90] Dodd–Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111–203, 124 Stat. 1376 (2010) (Title IX, Subtitle B, explains increasing regulatory enforcement and remedies).

[91] *See, e.g.*, DAVID WOODCOCK & MICHAEL HOLMES, SECURITIES LITIGATION AND ENFORCEMENT: GET PREPARED FOR DODD-FRANK, 4 (2010), *available at* http://www.velaw.com/uploadedFiles/VEsite/Resources/Dodd-FrankAct080410.pdf (arguing that Dodd-Frank "paves the way for future changes that could bring more private litigation"). This assumption is rooted in speculation that Congress will eventually grant private litigants the same powers that it has chosen to give the SEC; however this proposition lacks historical support.

[92] *See* Cummings, *supra* note 89, at 1029 & n.231.

[93] Brian S. Sommer, *The PSLRA Decade of Decadence: Improving Balance in the Private Securities Litigation Arena with a Screening Panel Approach*, 44 WASHBURN L.J. 413, 416 (2005).

II. CIVIL RICO: ANTIFRAUD REMEDY OR MISUNDERSTOOD STATUTE?

A. From Mobsters to Fraudsters: A Brief History

In 1970, Congress passed the Organized Crime Control Act (OCCA).[94] The centerpiece of this anti-crime legislation, which was signed into law two weeks prior to midterm elections, was Title IX: RICO.[95] Congress stated that the purpose of RICO was "the elimination of the infiltration of organized crime and racketeering into legitimate organizations operating in interstate commerce."[96]

RICO incorporated a number of criminal and civil remedies to address racketeering, loosely defined as organized criminal activity affecting interstate commerce.[97] In addition to arming federal law enforcement with additional weapons in the fight against organized crime, RICO's civil causes of action have enhanced the ability of the federal government, as well as private victims, to seek redress in court.[98]

The Civil RICO statute provides that "[a]ny person injured in his business or property by reason of a violation of section 1962" is entitled to sue in federal court and could recover treble damages.[99] The supposed original intention of RICO—to allow victims to demand satisfaction from humbled mobsters—might have been naïve.[100] But Congress clearly intended, at the time of RICO's passage in 1970, to allow the victims of other criminal organizations—those sheathed in skyscrapers and boardrooms—to recover what they could from those who had wronged them, and Congress' inclusion of securities fraud as a predicate implies as much. While traditional organized

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[94] Organized Crime Control Act of 1970, Pub. L. No. 91-452, 84 Stat. 922 (codified as amended in scattered sections of the U.S.C.).

[95] The election of 1970 was largely a referendum on "law and order" issues. For a detailed analysis of the legislative history and intentions behind OCCA, see Abrams, *supra* note 12, at 41-50.

[96] S. REP. NO. 91-617, at 76 (1969).

[97] For a formal—and very detailed—definition of "racketeering activity" as used in RICO, see 18 U.S.C. § 1961(1) (2012).

[98] RICO's asset forfeiture provision vests forfeiture authority and post-recovery possession in the government. 18 U.S.C. § 1963(b)-(m) (2012). This asset forfeiture provision does include sections authorizing the restoration of property to individual victims of the RICO conspiracy. 18 U.S.C. § 1963(g)(1) & (h)(3). Notably, however, the government is not *required* to compensate victims, necessitating private litigation to recover the proceeds of securities fraud.

[99] *See* 18 U.S.C. § 1964(c) (2012).

[100] Given organized crime's tendency to prey on the vulnerable, it is unlikely that many victims had the time, money or gall to initiate lawsuits against traditional organized crime groups in federal court. Congressional supporters of PSLRA cited this intended purpose as a primary reason for supporting changes to Civil RICO, arguing that the securities fraud predicate constituted a "loophole" in a law otherwise intended to target organized crime. *See* 141 CONG. REC. 7135 (statement of Rep. Cox). Opponents of PSLRA argued that this difference was semantic, rooted in changing definitions of organized crime, further noting that OCCA's original inclusion of securities fraud as a predicate suggests that securities fraud was always an intended target for Civil RICO coverage and not an inadvertent one. *See* 141 CONG. REC. 7135-36, 7138 (statements of Rep. Bryant and Rep. Dingell).

crime is arguably more notorious, it is unclear why victims of securities fraud are less deserving of redress than victims of loan-sharking and other "traditional" RICO predicates. RICO's criminal provisions have been used to prosecute perpetrators of securities fraud such as Michael Milken.[101] If conduct amounting to securities fraud is covered under RICO's criminal liability sections, it should also qualify for the opprobrium attached to its civil liability section.

Civil RICO litigation encompasses four primary requirements. First, the plaintiff must demonstrate that the activity in question affected interstate commerce.[102] Second, the plaintiff must demonstrate real injury by reason of a violation of a § 1962 predicate.[103] The Supreme Court has interpreted this to mean that the RICO predicate crime must be the proximate cause of the plaintiff's injury.[104] The Court has ruled unanimously that to have standing for Civil RICO purposes, a plaintiff must be a direct—not indirect—victim of the predicate crime.[105] The Court has also, significantly, limited the scope of Civil RICO to prevent those not intimately involved in the criminal activity at issue from being liable, thus protecting incidental and minor participants involved in racketeering enterprises.[106]

The third element of a Civil RICO claim is that the alleged torts must have been committed by a criminal enterprise.[107] RICO enterprises have a

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[101] L. Gordon Crovitz, *How the RICO Monster Mauled Wall Street*, 65 NOTRE DAME L. REV. 1050, 1064 (1990); *see also* Avital Louria Hahn, *Corporate Crooks Could Face RICO*, INVESTMENT DEALERS' DIGEST, Sept. 30, 2002, Vol. 68 Issue 37, at 8, *available at* http://connection.ebscohost.com/c/articles/7523518/corporate-crooks-could-face-rico (noting that some of the parties involved in the securities fraud epidemic of 2002 might face RICO charges). Milken was indicted on RICO charges, but ultimately pleaded guilty to securities fraud and conspiracy charges. *See* Kurt Eichenwald, *Milken Defends 'Junk Bonds' As He Enters His Guilty Plea,* N.Y. TIMES (Apr. 25, 1990), http://www.nytimes.com/1990/04/25/business/milken-defends-junk-bonds-as-he-enters-his-guilty-plea.html.

[102] Courts have not discussed RICO's interstate commerce requirement in detail, but the plaintiff's burden, as with most federal statutory "interstate commerce" requirements, is not difficult to meet. United States v. Beasley, 72 F.3d 1518, 1526 (11th Cir. 1996), *cert. denied*, 518 U.S. 1027 (1996) ("To satisfy [RICO's] interstate commerce requirement, only a slight effect on interstate commerce is required."). *See also* United States v. Riddle, 249 F.3d 529, 538 (6th Cir.), *cert. denied*, 534 U.S. 930 (2001) ("[A] de minimis connection suffices for a RICO enterprise that 'affects' interstate commerce."); Musick v. Burke, 913 F.2d 1390, 1398 (9th Cir. 1990) (holding that the conduct required to satisfy interstate commerce requirement is minimal). One would imagine that given the necessarily interstate nature of securities trading and regulation, this was rarely an issue during the time securities fraud was a RICO predicate.

[103] *See, e.g.*, ELEVENTH CIRCUIT CIVIL PATTERN JURY INSTRUCTIONS 7.1 at 511 (2013), *available at* http://www.ca11.uscourts.gov/documents/pdfs/civjury.pdf (offering a slightly different articulation of the elements of a civil RICO claim, replacing proof of "injury" with proof that the illegal income in question was derived from a pattern of racketeering).

[104] Holmes v. Sec. Investor Prot. Corp., 503 U.S. 258, 268 (1992).

[105] Anza v. Ideal Steel Supply Corp., 547 U.S. 451, 461 (2006).

[106] Reves v. Ernst & Young, 507 U.S. 170, 185 (1993).

[107] The RICO statute defines "enterprise" to "include[] any individual, partnership, corporation, association, or other legal entity, and any union or group of individuals associated in fact although not a legal entity." 18 U.S.C. § 1961(4) (2012).

structure[108]—a lone businessman engaged in insider trading cannot face civil liability under the statute.[109] This concept is a meaningful constraint on RICO's application. However, the criminal enterprise requirement has fostered the misconception that RICO is a remedy whose value should be limited to fighting traditional organized crime, violent gangs, and other organizations whose behavior fits with commonly held notions of criminality.

Finally, Civil RICO plaintiffs must establish that the predicate acts in question were part of a "pattern of racketeering activity."[110] The RICO statute offers an exhaustive list of criminal violations that constitute "racketeering activity"; these predicate acts range from murder to visa fraud.[111] RICO further provides for an expansive understanding of the word "pattern," defining "pattern" to include any two predicate acts which are temporally separated by ten years' time or less.[112]

B. Civil RICO and Its Critics: The End of the Securities Fraud Predicate

Criticisms of the use of Civil RICO to recoup losses arising out of securities fraud generally fall into one of two categories. The first category encompasses the wide range of general criticisms of litigation: that the litigation in question is too expensive, that it leads to meritless "strike suits," and that it unjustly enriches plaintiffs' attorneys. The second category of criticism centers around the belief that RICO was not intended to address securities fraud, and that attempts to use Civil RICO against anyone but the archetypal, intimidating mobster constitute a departure from the original intentions of Congress.[113]

This "intentionalist" argument is a common attack on Civil RICO's appropriateness as a remedy in white-collar contexts. At heart, it claims that RICO has come loose from its bearings, especially insofar as Civil RICO lawsuits are not exclusively directed at organized crime.[114] Yet the fact that

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[108] *See* Limestone v. Lemont, 520 F.3d 797, 805 (7th Cir. 2008) ("[E]nterprise is proved by evidence of an ongoing organization, formal or informal, *and by evidence that the various associates function as a continuing unit.*") (quoting United States v. Turkette, 452 U.S. 576, 583 (1981)) (internal quotations omitted).

[109] This distinction arises from a common law rule that an individual is unable to conspire with himself. *See* River City Mkts, Inc. v. Fleming Foods W., Inc., 960 F.2d 1458, 1461 (9th Cir. 1992).

[110] *See* 18 U.S.C. § 1961(5) (defining "pattern of racketeering activity").

[111] 18 U.S.C. § 1961(1) (specifying what degree of criminal liability is needed for an act to rise to predicate status; some must be merely "chargeable," others "indictable," and still others—such as the securities fraud predicate—actual "offenses," i.e., the result of a conviction).

[112] This definition of "pattern" seems unusually broad. *See* H.J. Inc. v. Nw. Bell Tel. Co., 492 U.S. 229, 237 (1989) (noting that the RICO statute "does not so much define a pattern of racketeering activity as state a minimum necessary condition for the existence of such a pattern").

[113] *H.J. Inc.*, 492 U.S. at 237.

[114] *See* Abrams, *supra* note 12, at 47. This intentionalist argument ignores decades of the remedy's development and evolution. *See, e.g.*, Elizabeth C. Peterson & Catherine E. Moreno, *The Expanding Territorial Reach of RICO: It's Not Just for U.S.-Based Organized Crime Anymore*, *available at* http://www.wsgr.com/publications/PDFSearch/bloomberg0510.pdf

Civil RICO claims are not directed at the originally intended targets—traditional organized crime—does not affect the statute's value as a litigation tool. The securities fraud predicate is found in the original text of RICO, and Congress' inclusion of the predicate signifies its clear intent.[115] That the targets of Civil RICO are not only shadowy gangsters but well-heeled businessmen is not a problem; society attaches disapproval to criminal schemes regardless of the perpetrators' identities and associations.[116] Indeed, Civil RICO has long been understood to apply to a diverse range of enterprises whose criminal activities might be beyond the scope of RICO's purported original intent.[117]

The framers of RICO imagined the law, including its civil components, as a powerful tool to fight criminal organizations' increased activity in American economic life. The Senate Report, which accompanied OCCA's passage, confirms as much, citing organized crime's "major threat to the proper functioning of the American economic system."[118] Lest such language be thought to refer only to traditional organized crime, the Senate Report also stated, "ultimately at stake is . . . the viability of our free enterprise system itself."[119] RICO's Congressional authors adopted broad language and remedies in order to ensure that the law could flexibly react to different types of predatory activity.[120]

The Supreme Court recognized as much in *Sedima*. According to the Court, "Congress wanted to reach both 'legitimate' and 'illegitimate' enterprises" in legislating Civil RICO, because "[t]he former enjoy neither an inherent incapacity for criminal activity nor immunity from its consequences."[121] Indeed, *Sedima* expressly rejected the proposition that Civil RICO was ambiguous, or that Congress was unclear in its intent. The Court stated, "The fact that RICO has been applied in situations not expressly anticipated by Congress does not demonstrate ambiguity. It demonstrates breadth."[122]

("Although RICO was intended to reach organized crime perpetrated by the Mafia, in the four decades since its inception, RICO has been used to reach conduct as varied as municipal tax evasion, civil fraud, and even terrorism.").

[115] 18 U.S.C. § 1962 (2012).

[116] *See* Seth Benjamin Cobin, *Upperworld Gangsters, Underworld Businessmen: Made Men, Corporate Raiders, and the Discrepancies Between the Enforcement of Organized and Organizational Crime*, 30 HAMLINE J. PUB. L. & POL'Y 627, 635 (2008) (noting white-collar criminal enterprises can be just as bad, if not worse, and just as organizational, as Mafia-related criminal activity).

[117] *See* Nat'l Org. for Women, Inc. v. Scheidler, 510 U.S. 249, 262 (1994); Scheidler v. Nat'l Org. for Women, Inc., 537 U.S. 393, 397 (2003); Scheidler v. Nat'l Org. for Women, Inc., 547 U.S. 9, 20 (2006). This litigation concerned a Civil RICO claim alleging that individuals and organizations involved in the anti-abortion movement had blocked women's access to certain health services. The legal issues underpinning this two-decade-long litigation saga are less germane to this Article than the fact that the action was within Civil RICO's ambit.

[118] *See* S. REP. NO. 91-617, at 76 (1969).

[119] *Id.* at 80-81.

[120] *Id.* at 83 ("[T]hese remedies are flexible, allowing of several alternate courses of action for dealing with a particular type of predatory activity . . . .").

[121] Sedima, S.P.R.L. v. Imrex Co., 473 U.S. 479, 499 (1985).

[122] *Id.*

Another font of criticism is that RICO, over the years, has developed into a "general federal antifraud remedy."[123] That Civil RICO would be widely used was consistent with the way in which it was written; "RICO was drafted in expansive terms to ensure that its objectives would not be thwarted by a difficult or impossible burden of proof."[124] Despite this clear intent, by the mid-1990s, however, a consensus had emerged that Civil RICO had, in practice, overreached its expansive and broad mandate.[125]

Although academic and legislative frustration with Civil RICO reached a head in the mid-1990s with the passage of PSLRA, belief in Civil RICO's overuse had been germinating for years. In the securities fraud predicate's heyday, even some proponents of robust private enforcement argued that Civil RICO's overuse was problematic. Justice Thurgood Marshall, dissenting in *Sedima*, argued that Civil RICO "virtually eliminates decades of legislative and judicial development of private civil remedies under the Federal securities laws."[126] While Marshall's dissent argued that Civil RICO should not be the primary recourse for private securities enforcement, it was not a broadside against the concept of securities fraud litigation generally.[127] Indeed, much of Marshall's dissent is focused not on the securities fraud predicates, but on the use of predicates for mail and wire fraud in civil RICO lawsuits. However, all the opinions in *Sedima*, including the majority opinion that endorses a wider reading of Civil RICO, underlie a degree of frustration with the broad application of Civil RICO. [128]

Complaints about Civil RICO, therefore, were not limited to the securities fraud predicate; they reflected frustration with Civil RICO's general overuse.

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[123] Abrams, *supra* note 12, at 37.

[124] Donald J. Moran, *Pleading a Civil RICO Action Under Section 1962(c): Conflicting Precedent and the Practitioner's Dilemma*, 57 TEMP. L.Q. 731, 731 (1984).

[125] *See* A. Darby Dickerson, *Curtailing Civil RICO's Long Reach: Establishing New Boundaries for Venue and Personal Jurisdiction Under 18 U.S.C. § 1965*, 75 NEB. L. REV. 476, 487-88 (1996); R. Stephen Stigall, *Preventing Absurd Application of RICO: A Proposed Amendment to Congress's Definition of "Racketeering Activity" in the Wake of* National Organization for Women, Inc. v. Scheidler, 68 TEMP. L. REV. 223, 228 (1995); Dana L. Wolff, *RICO's Role in Securities Fraud Litigation: Should it Be Facilitated or Restricted?* 21 J. LEGIS. 359, 363 (1995).

[126] *Sedima*, 473 U.S. at 505 (Marshall, J., dissenting).

[127] Ironically, Marshall's statement was quoted by bill sponsor Christopher Cox in support of the RICO amendment. *See* 141 CONG. REC. 7134 (1995) (statement of Rep. Cox). Justice Marshall may have favored less use of civil RICO for securities fraud enforcement, but it is doubtful that he would have endorsed the wide-ranging pleading and court access restrictions which formed PSLRA's core.

[128] Notably, Supreme Court opinions also attempted, at times, to restrict the scope of Civil RICO's application. *See, e.g.*, Shearson/Am. Exp., Inc. v. McMahon, 482 U.S. 220, 242 (1987) (ruling that Civil RICO claims, specifically those arising out of securities fraud predicates, could be addressed in arbitration settings as opposed to federal district court); Agency Holding Corp. v. Malley-Duff & Assocs., 483 U.S. 143, 156 (1987) (imposing four-year statute of limitations from discovery of injury on RICO claims). The Court has further ruled on the question of tolling. *See* Klehr v. A.O. Smith Corp., 521 U.S. 179, 194 (1997). *But see* Am. Nat'l Bank & Trust Co. v. Haroco, Inc., 473 U.S. 606, 609 (1985) (ruling that to sustain a civil RICO claim, it was not necessary that respondents suffer damages from the fact that predicate offenses were conducted as part of the RICO enterprise itself).

PSLRA, however, was an attack on the securities fraud predicate and its derivatives; it was not part and parcel of an overall program of Civil RICO reform, which might have addressed other shortfalls in the statutory text that enabled purported misuses of the statutory scheme. That reforms were necessary is not in dispute, but the means in which a singular reform was carried out failed to match the complexity of the problem.

Indeed, the decision to strip the securities fraud predicate from Civil RICO was hastily made. One Member of Congress, in the initial debates on PSLRA, pointed out that the amendment to alter the RICO statute had been offered without hearings, debate, or discussion.[129] Another argued that the amendment, offered by Rep. Christopher Cox of California[130]—who later served as Chairman of the SEC—was "broader than any RICO amendment that Congress has ever considered before."[131]

The changes, it was said, would "prevent lawsuits against some of the biggest white-collar criminals in the Nation's history."[132] SEC Chairman Arthur Levitt argued that securities fraud RICO actions "tend to coerce settlements and force defendants to litigate issues that would not otherwise arise in securities cases," stating further that "it is both unnecessary and unfair to expose defendants in securities cases to the threat of treble damages and other extraordinary remedies provided by RICO."[133]

While PSLRA removed securities fraud as a predicate, specifically limiting it in 18 U.S.C. § 1964(c), the revised law did preserve the predicate when there has been a criminal conviction for securities fraud.[134] This concession was relatively minor. "[O]nly a small fraction of all securities fraud cases are

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[129] 141 CONG. REC. 7114 (1995) (statement of Rep. Frost) (criticizing Rep. Cox for rushing Civil RICO amendment to the floor of the House). This amendment, H.AMDT. 266, passed on March 7, 1995 by a 292-124 roll call.

[130] 141 CONG. REC. 7134-35 (1995) (statement of Rep. Cox) (explaining the justification for his amendment). Cox claimed that the failure to include the Civil RICO amendment in the original legislation was an oversight that occurred when the bill was reported out of the House Commerce and Judiciary Committees.

[131] 141 CONG. REC. 7119, (1995) (statement of Rep. Conyers). Conyers echoed Frost's concern (*supra* note 129) about the amendment being rushed to the floor, quite acerbically stating that "[t]he problem that we have is that the gentleman's amendment is asking the Congress in broad daylight to believe that the biggest amendment for fighting civil fraud that has ever been put on the books was accidentally left out. I guess we accidentally did not have any hearings. I guess there accidentally were not any witnesses." 141 CONG. REC. 7128 (1995) (statement of Rep. Conyers).

[132] 141 CONG. REC. 7128.

[133] Arthur Levitt, Chairman, U.S. Sec. & Exch. Comm'n, Testimony before the Subcommittee on Telecommunications and Finance Committee on Commerce in the House of Representatives 15, 16 (Feb. 10, 1995), *available at* http://www.sec.gov/news/testimony/testarchive /1995/spch025.txt.

[134] *See* GREGORY P. JOSEPH, CIVIL RICO: A DEFINITIVE GUIDE 123 (3d ed., 2010). This was a departure from the traditional legislative understanding of RICO. Traditionally, there has been no private conviction requirement for civil RICO. *See* Sedima, S.P.R.L. v. Imrex Co., 473 U.S. 479, 488-89 (1985).

handled as criminal cases."[135] Given the complexity of securities fraud prosecutions, and owing largely to the expense, time, and effort required to secure a conviction,[136] few criminal cases for 'chargeable' or 'indictable' securities fraud are actually pursued by prosecutors. Criminal charges require the government to bear a high burden in proving the charges, and bedrock constitutional principles such as the right against self-incrimination can inhibit investigations and prosecutions.[137] However indirectly, this exception inappropriately imposes an extremely high standard on a civil claim, while also furnishing civil defendants with a host of criminal procedure rights to which they are not, in this context, entitled.[138]

Ultimately, the criminal conviction exception is a mere gloss on the removal of securities fraud as a predicate. Situations in which criminal convictions are actually obtained do not make ideal Civil RICO cases. Usually, the convicted felons have been ordered to pay restitution by a court, and investigators and asset forfeiture experts have conducted an extensive search for funds. When the criminal justice system adequately addresses securities fraud, Civil RICO is usually not necessary; it is a remedy for those occasions where the government cannot, through the powerful mechanisms of criminal liability, stop securities fraud-related racketeering activity.[139]

The absence of a useful securities fraud predicate in the Civil RICO context is far less justified than it might have seemed two decades ago. The revolution in pleading has minimized the risk of frivolous litigation overall, while weaknesses in government securities regulation have become more apparent. Given intervening legal developments, reinstating Civil RICO for securities fraud predicates will not lead to an explosion of litigation. Rather, existing statutory and judicial limitations on litigation will ensure that such claims are measured and effective.

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135 *See Why So Few Securities Fraud Cases Are Criminally Prosecuted*, KNOWLEDGE@WHARTON (Aug. 30, 2000), http://knowledge.wharton.upenn.edu/article.cfm?articleid=230. This is a quotation from William S. Laufer, a Professor at Wharton School of Business at the University of Pennsylvania.

136 *Id.*

137 Lefkowitz v. Turley, 414 U.S. 70, 77 (1973) (stating that the right to self-incrimination enables a defendant to refuse testifying at criminal trial and "privileges him not to answer official questions put to him in any other proceeding, civil or criminal, formal or informal, where the answers might incriminate him in future criminal proceedings").

138 The PSLRA restriction on securities fraud RICO applies to all RICO claims, including government-backed civil actions seeking equitable relief under 18 U.S.C. § 1964(a). The federal government is not permitted to bring lawsuits for treble damages under § 1964(c). For more on Government Civil RICO lawsuits, see U.S. DEPARTMENT OF JUSTICE, CIVIL RICO: A MANUAL FOR FEDERAL ATTORNEYS 2 (2007), *available at* http://www.justice.gov/usao/eousa/foia_reading_room/usam/title9/civrico.pdf.

139 Government-initiated civil actions are similarly not an answer, as they are often governed by procedures analogous to those which constrain government action in criminal proceedings. For example, the Department of Justice's Criminal Division must pre-approve any complaints or investigations made by government authorities pursuant to RICO, including civil ones. *See* U.S. ATTORNEY'S MANUAL 9-110.101 (1997).

III. REINSTATING CIVIL RICO: A MEASURED, SENSIBLE STEP

PSLRA, subsequent legislation, and the courts' concomitant construction of laws that restrict private enforcement have fostered an atmosphere where successfully suing for securities fraud is exceedingly difficult.[140] In an attempt to restrict litigious "fishing expeditions," Congress and the courts have shut one door after another in the face of those who raise legitimate complaints. As Sen. Richard Bryan (D-NV) pointed out during floor debates, PSLRA makes it nearly impossible to bring a securities fraud case to trial.[141]

Congress should authorize the use of securities fraud as a predicate for Civil RICO. However, Congress need not completely revert to the state of the law *ex ante* PSLRA. I propose four further changes to the law, which would restrict Civil RICO claims. Congress should implement these reforms if and when it reinstates the securities fraud predicate.

First, Congress should explicitly state that such claims will be bound by legislative and judicial restrictions placed on any civil litigation that arises directly out of the New Deal securities laws. This will ensure that strike suits and meritless litigation are severely limited. The range of restrictions detailed above, through PSLRA, changes to the Federal Rules regarding heightened pleading for fraud,[142] and judicial interpretations can be an effective means of controlling Civil RICO litigation.

Civil RICO actions based on securities fraud predicates would not, at present, be restricted by all in-place heightened pleading requirements since they are not, in and of themselves, fraud claims. I propose that Civil RICO actions which rely solely or predominantly on securities fraud predicates should be required to abide by heightened pleading requirements for fraud which are delineated in Federal Rule of Civil Procedure 9.[143] This would

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[140] For example, witness the recent decline in securities fraud filings despite the present economic climate. *See, e.g.*, Sheri Qualters, *Securities Fraud Suits Resurface*, NAT'L. L.J., Nov. 30, 2009, at 7 ("Federal securities class action filings slid by 22 percent in the first half of 2009, with 87 new cases compared with 112 in the first half of 2008."). *Cf.* Jackson, *supra* note 39 (noting that in the past period of economic decline, securities fraud enforcement ticked upward).

[141] 141 CONG. REC. 17,434 (1995) (statement of Sen. Bryan) ("I have prepared a little chart here which I think indicates the number of hurdles that have to be surmounted in order to get to the finish line. It will be more difficult to get these cases brought because of the limitations imposed. The shorter statute of limitations. The surrender of control of the wealthiest plaintiff which in effect becomes the lead plaintiff presumptively under this. The automatic discovery stage prevents the plaintiff from ascertaining what the state of mind is of the defendants who have perpetrated the fraud. The safe harbor provisions, that the distinguished Senator from Maryland has talked about; aiders and abettors--they are home free. They do not have any liability at all. The RICO liability has been wiped out.").

[142] *See* Bell Atlantic v. Twombly, 550 U.S. 544, 556 (2007) (expressing concern that defendants would be forced to conduct extensive pretrial discovery). In Limestone v. Village of Lemont, 520 F.3d 797, 803 (7th Cir. 2008), Judge Posner noted the similarity of RICO to antitrust cases (dealt with in *Twombly*), saying that "RICO cases, like antitrust cases, are 'big' cases and the defendant should not be put to the expense of the big-case discovery on the basis of a threadbare claim."

[143] *See* FED. R. CIV. P. 9(b) ("In alleging fraud or mistake, a party must state with particularity the circumstances constituting fraud or mistake.").

prevent plaintiffs from using Civil RICO as an end-run around the securities fraud laws' pleading requirements. It would allow meritorious civil RICO claims to go forward without opening the door to a landslide of meritless litigation.

Second, Congress should ensure that all Civil RICO claims arising out of securities fraud are removed to federal court. Two decades ago, the Supreme Court ruled unanimously that state courts enjoy concurrent jurisdiction with federal courts over Civil RICO claims.[144] I take no position, at this moment, as to whether the relentless federalization of tort claims in recent years has been a positive, negative, or neutral development. Congress has already federalized securities litigation class actions through the passage of SLUSA, and should ensure that Civil RICO claims—those arising out of securities fraud predicates only—are brought in federal court.

This change is justified on practical grounds. Securities fraud litigation tends to be complex in nature, and many claims never make it past the initial procedural stages, especially after the addition of heightened pleading requirements. (Many other claims are settled during the early stages of litigation.) As a result, there is a paucity of judicial interpretation when it comes to an array of vital issues, both procedural and substantive, that arise out of private enforcement.[145] This problem could be compounded if securities fraud is reinstated as a predicate. Since Civil RICO has not been part of the universe of securities litigation for fifteen years, courts will need to quickly reinterpret precedent and legislative provisions in light of intervening changes in the law. Federalizing Civil RICO claims that arise from securities fraud predicates will foster the development of a substantial, and hopefully uniform, body of related precedent and interpretation.

Furthermore, securities fraud involves uniquely national concerns which warrant federal jurisdiction and oversight. Given that the cause of action arises under federal law, touches on a key area of federal interest, and affects interstate commerce, universal removal of Civil RICO claims which cite a securities fraud predicate to federal court is a no-brainer.

One argument against reinstating the securities fraud predicate for Civil RICO is that it will result in duplicative litigation. This claim, which was among the bases cited by SEC Chairman Arthur Levitt for supporting PSLRA in 1995, has not weathered well. An unintended consequence of PSLRA has been the initiation of racketeering actions, which mimic Civil RICO, under state anti-racketeering statutes.[146] PSLRA has simply shifted the venue for securities fraud racketeering lawsuits, and in doing so, risks the development of widely disparate legal approaches and the emergence of a real forum-shopping problem for racketeering litigation.

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144 Tafflin v. Levitt, 493 U.S. 455, 467 (1990).

145 Stephen Bainbridge & G. Mitu Gulati, *How do Judges Maximize? (The Same Way Everybody Else Does –Boundedly): Rules of Thumb in Securities Fraud Opinions*, 51 EMORY L.J. 83, 116 (2002).

146 *See* David M. Zensky & Joseph L. Sorkin, *State RICO and the PSLRA*, NAT'L L.J., Mar. 31, 2008, at 12.

The third reform Congress should institute relates to the statute of limitations for Civil RICO claims. In *Agency Holding v. Malley-Duff*, the Supreme Court imposed a four-year statute of limitations on Civil RICO claims, noting that the RICO statute itself was silent on the issue.[147] The Court rooted its holding in an analogy between Civil RICO and Section 4B of the Clayton Antitrust Act, reasoning that the former was close enough in character to the latter to justify the same, four-year statute of limitations.[148] In line with bringing securities fraud Civil RICO into the greater securities litigation family, the Court should apply a tighter statute of limitations, requiring that claims be filed within one year of discovery and three years of the actual, fraudulent transaction.[149] This would essentially incorporate the statute of limitations applied by the Court to 10b-5 litigation in past rulings.[150]

Finally, Congress should explicitly restate the purpose of Civil RICO, with an eye towards a broader understanding of the statute's purpose. Given the evident discomfort among observers with RICO being used for more than typical notions of criminality, Congress should establish that all criminal enterprises, even if they fail to fit a specific stereotype, pose a threat that requires deterrence and affects victims.[151] Such a declaration would comport with a contemporary understanding that securities fraud constitutes behavior worthy of approbation.

Although such a Congressional finding would be primarily symbolic, it would provide important guidance to courts charged with interpreting Civil RICO. Courts' interpretations of RICO routinely evidence discomfort with the disconnect between the statute's origins and its application. Courts have resolved these disputes by generally pointing to expansive understandings of RICO. Congress should clarify that RICO is not merely a decades-old law aimed at traditional organized crime; instead, RICO is a dynamic statutory scheme aimed at combating a wide range of criminal activity through civil and criminal remedies. This will limit the practice of judges, legislators, and litigators digging through a yellowed Congressional Record in an attempt to prove that RICO's original authors were focused on a different threat than the one RICO frequently addresses today.

These reforms would serve another important purpose: to bring securities fraud Civil RICO into the larger rubric of other securities litigation. Instead of being a statutory outlier, securities fraud Civil RICO will be fully bound by the rules and regulations affecting other forms of securities litigation. None of

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147 Agency Holding Corp. v. Malley-Duff & Assocs., 483 U.S. 143, 146, 156 (1987).

148 *See* Limestone v. Village of Lemont, 520 F.3d 797, 805 (7th Cir. 2008) (expanding on the similarities between antitrust litigation and Civil RICO); U.S. DEPARTMENT OF JUSTICE, CIVIL RICO: A MANUAL FOR FEDERAL ATTORNEYS 26 (2007) (discussing, in detail, how Civil RICO was modeled after the antitrust laws).

149 This is not the place to discuss the complex, controversial question of tolling, but I note that basic tolling principles permit a plaintiff to sue if discovery of the underlying cause of action was prevented by a defendant's actions.

150 Lampf v. Gilbertson, 501 U.S. 350, 364 (1991) (imposing fairly strict statute of limitations on Rule 10b-5 claims).

151 Cobin, *supra* note 116.

these proposed reforms would affect Civil RICO claims based on predicates aside from securities fraud.

Civil RICO is more than a run-of-the-mill civil remedy. Judgments under Civil RICO carry both steep tangible costs—the treble damages and costs imposed on a liable defendant—and the condemnation that comes with being placed in a category labeled 'criminal enterprise.' Civil RICO lawsuits should not be lightly brought, and other remedies to foreclose frivolous litigation should be strictly enforced to prevent meritless Civil RICO actions. However, given the seriousness of the conduct that underlies criminal securities fraud, Civil RICO should be an option for those who have suffered at the hands of criminal enterprises, regardless of the nature of the crimes committed.

CONCLUSION

There are few issues as critical to society as the health of its financial system. Periodic attacks on the integrity of this system, through securities fraud that at times seems endemic, pose a serious threat to both economic stability and common conceptions of justice. Private enforcement is integral to a functioning, robust, and successful system of securities regulation—for purposes of both deterrence and compensation.

The removal of Civil RICO from the arsenal of those fighting securities fraud should be reversed. With an eye to the legitimate concerns about Civil RICO's breadth that partially motivated Congress' decision to amend it, Congress should reassess its decision and reinstate securities fraud as a Civil RICO predicate. Doing so, while implementing the limitations prescribed in this Article, will allow Congress to satisfy both the concerns of Civil RICO's critics and the pressing national need for private securities enforcement.