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Supreme Court Holds That a RICO Claim Predicated on Mail Fraud Does Not Require a Showing of First-Party Reliance

On June 9, 2008, the Supreme Court issued a unanimous decision in *Bridge* v. *Phoenix Bond & Indemnity Co*.[1] Resolving a split among the lower courts, the Court held that a plaintiff bringing a RICO claim predicated on mail fraud need not plead or prove that it relied on the defendant's alleged misrepresentations.

I. Background

Congress enacted RICO as an "aggressive initiative to supplement old remedies and develop new methods for fighting crime."[2] The principal substantive subsection of the statute provides that "[i]t shall be unlawful for any person employed by or associated with any enterprise engaged in, or the activities of which affect, interstate or foreign commerce, to conduct or participate, directly or indirectly, in the conduct of such enterprise's affairs through a pattern of racketeering activity . . . ."[3] The statutory term "racketeering activity" is defined[4] to include dozens of state and federal crimes, among them mail fraud prohibited by 18 U.S.C. § 1341 and wire fraud prohibited by 18 U.S.C. § 1343. In addition to criminal penalties, RICO created a private cause of action that allows a plaintiff whose business or property has been injured "by reason of" the defendant's RICO violation to recover treble damages.[5]

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1 No. 07-210, Slip Op. (U.S. June 9, 2008) ("*Bridge* Slip Op.").

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

3 18 U.S.C. § 1962(c). Causation under the other two substantive subsections of RICO, 18 U.S.C. § 1962(a), (b), raises separate issues not addressed in *Bridge* and not treated here. With respect to the RICO conspiracy offense, 18 U.S.C. § 1962(d), the Supreme Court held in *Beck* v. *Prupis*, 529 U.S. 494 (2000), that there could be no civil RICO conspiracy liability in the absence of an underlying "racketeering activity," and that the harm complained of must flow from the racketeering activity and not from non-criminal acts associated with the conspiracy.

4 18 U.S.C. § 1961(1).

5 18 U.S.C. § 1964(c) ("Any person injured in his business or property by reason of a violation of section 1962 of this chapter may sue therefor in any appropriate United States district court and shall recover three-

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In *Holmes* v. *Securities Investor Protection Corp.*,[6] the Supreme Court held that a RICO plaintiff's injury occurred "by reason of" the defendant's violation only if the violation was the injury's proximate cause.[7] The Court emphasized that there must be "some direct relations between the injury asserted and the injurious conduct alleged."[8]

Anza v. *Ideal Steel Supply Corp.*[9] provided the Court with an opportunity to apply the proximate causation requirement in a fraud case. The Second Circuit had held that reliance by the plaintiff on the defendant's misrepresentations was not necessary to establish proximate causation in a case where one competitor was allegedly able to undercut another's prices by failing to include sales tax in its price and by filing fraudulent sales tax returns.[10] The Supreme Court declined to reach what it termed the "substantial question" of the existence of such a reliance requirement but, instead, held on other grounds that proximate causation had not been established.[11] It articulated several factors relevant to the proximate causation inquiry, including: whether damages will be difficult to ascertain; whether the plaintiff's injury could have resulted from factors other than the defendants' alleged violations; whether there is a risk of duplicative recoveries by other plaintiffs; and whether another more immediate victim of the alleged violation can be expected to enforce the law by pursuing its own claims.[12] Justice Kennedy's majority opinion in *Anza* also appealed to policy and prudential factors in holding that proximate causation had not been established.[13] This represented a sharp departure from two decades of Supreme Court RICO jurisprudence, in which the Court's touchstone was to read the words used by Congress with their ordinary English meanings and leave policy or prudential concerns for Congress to address if it chose to do so. Justice Thomas's dissent took the majority to task for this departure and urged the Court to return to the mode of analysis it had followed for so long.[14] Justice Thomas also addressed the reliance issue and

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fold the damages he sustains and the cost of the suit, including a reasonable attorney's fee, except 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.").

6 503 U.S. 258 (1992).

7 *Id.* at 268.

8 *Id.*

9 547 U.S. 451 (2006).

10 *Ideal Steel Supply Corp.* v. *Anza*, 373 F.3d 251, 263 (2d Cir. 2004).

11 *Anza*, 547 U.S. at 461.

12 *Id.* at 458-60.

13 Justice Kennedy stated:

> The element of proximate causation recognized in *Holmes* is meant to prevent these types of intricate, uncertain inquiries from overrunning RICO litigation. It has particular resonance when applied to claims brought by economic competitors, which, if left unchecked, could blur the line between RICO and the antitrust laws. *Id.* at 460.

14 *Id.* at 463, 478-79 (Thomas, J., concurring in part and dissenting in part).

stated that he would hold reliance by the plaintiff *not* required for a civil RICO claim under 18 U.S.C. § 1962(c) with a mail or wire fraud predicate.[15]

After *Anza*, the courts of appeals remained split on the question the Supreme Court there left open, with the Sixth, Eighth, and Eleventh Circuits requiring reliance by the plaintiff and the First, Fourth, and Seventh Circuits imposing no such requirement.[16] Within the Second Circuit, courts continued to apply the Second Circuit's holding in *Anza* that reliance by the plaintiff on the defendant's misrepresentation is not a necessary element in RICO fraud cases,[17] but language in *McLaughlin* v. *American Tobacco Co.*[18] cast doubt on the continuing validity of that holding.

II. Facts and Procedural History of *Bridge*

The plaintiffs and defendants in *Bridge* were regular participants in public auctions held by the Treasurer's Office of Cook County, Illinois to sell tax liens on the property of delinquent taxpayers. Under the rules of the auction, bids for the liens were stated as percentage penalties the property owner had to pay the winning bidder in order to clear the lien. If a taxpayer did not clear a lien, the lienholder could obtain a tax deed for the property, effectively purchasing it for the value of the delinquent taxes. Because property acquired in this manner often could be sold at a significant profit, most properties attracted multiple 0% bidders willing to accept no penalty at all on a lien. The county addressed ties among 0% bidders with a "rotational" allocation system that awarded properties to bidders in proportion to the number of their 0% bids. To prevent manipulation by bidders attempting to multiply their 0% bids, the county implemented a "Single, Simultaneous Bidder Rule" requiring each bidder to affirm that it had submitted bids only in its own name and had not used "apparent agents, employees, or related entities" to submit simultaneous bids. The plaintiffs in *Bridge* alleged that the defendants had obtained a disproportionate share of liens through violations of the Single, Simultaneous Bidder Rule involving numerous acts of mail fraud.

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15 *Id.* at 475-78.

16 *Compare VanDenBroeck* v. *CommonPoint Mortgage Co.*, 210 F.3d 696, 701 (6th Cir. 2001), *Appletree Square I, L.P.* v. *W.R. Grace & Co.*, 29 F.3d 1283, 1287 (8th Cir. 1994), *and Sikes* v. *Teleline, Inc.*, 281 F.3d 1350, 1360-61 (11th Cir. 2002) (all applying rule that plaintiff must have relied on defendant's misrepresentations), *with Systems Mgmt., Inc.* v. *Loiselle*, 303 F.3d 100, 104 (1st Cir. 2002), *Mid Atlantic Telecom, Inc.* v. *Long Distance Servs., Inc.*, 18 F.3d 260, 263 (4th Cir. 1994), *and Phoenix Bond & Indem. Co.* v. *Bridge*, 477 F.3d 928, 932 (7th Cir. 2007) (all rejecting this rule); *see also Sandwich Chef of Tex., Inc.* v. *Reliance Nat'l Indem. Ins. Co.*, 319 F.3d 205, 223 (5th Cir. 2003) (recognizing a "narrow exception to the requirement that the plaintiff prove direct reliance on the defendant's fraudulent predicate act . . . when the plaintiff can demonstrate injury as a direct and contemporaneous result of fraud committed against a third party.").

17 *See, e.g.*, *Rothberg* v. *Chloe Foods Corp.*, No. CV-06-5712(CPS), 2007 WL 1218376, at *12 n.59 (E.D.N.Y. July 25, 2007).

18 522 F.3d 215, 222 (2d Cir. 2008) ("In cases such as this one when mail or wire fraud is the predicate act for a civil RICO claim, the transaction or 'but for' causation element requires the plaintiff to demonstrate that he relied on the defendant's misrepresentations.").

The district court dismissed the plaintiffs' complaint for lack of standing.[19] Because the plaintiffs were not recipients of the defendants' alleged misrepresentations, the district court reasoned that they "at best were indirect victims of the alleged fraud" who fell outside the "zone of interests" protected by the RICO statute.[20] The Seventh Circuit reversed, holding that a direct victim of a fraudulent scheme can recover through RICO even if it was not the direct recipient of the defendant's misrepresentations.[21]

III. The Supreme Court's Decision

The Supreme Court affirmed the Seventh Circuit. Writing for a unanimous Court, and picking up on his dissent in *Anza*, Justice Thomas focused on the texts of the mail fraud and RICO statutes. He noted that "[u]sing the mail to execute or attempt to execute a scheme to defraud is indictable as mail fraud, and hence a predicate of racketeering under RICO, even if no one relied on any misrepresentation. And one can conduct the affairs of a qualifying enterprise through a pattern of such acts without anyone relying on a fraudulent misrepresentation."[22] RICO's private right of action, Justice Thomas explained, does not impose any additional reliance requirement on private plaintiffs. The broad language of 18 U.S.C. § 1964(c) allows recovery by "[a]ny person" injured by a violation, and "a person can be injured 'by reason of' a pattern of mail fraud even if he has not relied on any misrepresentations."[23] This was, Justice Thomas said, "a case in point."[24]

Moreover, the proximate cause principles articulated in *Holmes* and *Anza* did not bar the plaintiffs' claims. Their loss of valuable liens was "a foreseeable and natural consequence of petitioners' scheme to obtain more liens for themselves . . . . And here, unlike in *Holmes* and *Anza*, there are no independent factors that account for respondents' injury, there is no risk of duplicative recoveries by plaintiffs removed at different levels of injury from the violation, and no more immediate victim is better situated to sue."[25]

While clarifying that the texts of the mail fraud and RICO statutes impose no independent reliance requirement, Justice Thomas acknowledged that the presence or absence of reliance bears on the causation analysis. "In most cases," he observed, "the plaintiff will not be able to establish even but-for causation if no one relied on the misrepresentation."[26] The absence of reliance could also prevent the plaintiff from establishing proximate causation. "Accordingly, it may well be that a RICO plaintiff alleging injury by reason of a pattern of mail fraud must establish at least third-party reliance in order to prove causation."[27] Still, Justice Thomas emphasized, " 'the fact that proof of reliance is often used to prove an

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19 *Phoenix Bond & Indem., Co.* v. *Bridge*, No. 05 C 4095, 2005 WL 3527232, at *7 (N.D. Ill. Dec. 21, 2005).

20 *Id.* at *5.

21 *Phoenix Bond & Indem. Co.* v. *Bridge*, 477 F.3d 928, 932-33 (7th Cir. 2007).

22 *Bridge* Slip Op. at 8-9 (citation omitted).

23 *Id.* at 9.

24 *Id.*

25 *Id.* at 18.

26 *Id.*

27 *Id.* at 19.

element of the plaintiff's cause of action, such as the element of causation, does not transform reliance itself into an element of the cause of action.' "[28]

Justice Thomas concluded by rejecting the defendant petitioners' contention that a requirement of first-party reliance was necessary to prevent the "over-federalization" of traditional state-law claims.[29] "Whatever the merits of petitioners' arguments as a policy matter, we are not at liberty to rewrite RICO to reflect their — or our — views of good policy."[30]

IV. Significance of the Decision

The Supreme Court did not in terms retract its earlier decision in *Anza*, but the *Bridge* opinion does represent a change in tone. The *Bridge* opinion was written by the dissenter in *Anza* and relies heavily on the *Anza* dissent. Although acknowledging that the *Anza* majority had said that the existence of a RICO reliance requirement was a "substantial question,"[31] the unanimous *Bridge* Court said that "petitioners' proposed requirement of first-party reliance seems to come out of nowhere."[32] While *Anza* signaled some willingness to develop judicial doctrine restricting RICO's scope, *Bridge* falls in line with the long series of decisions that read the words of the statute in accordance with their ordinary English meanings and decline to narrow RICO according to a conception of its intended purpose or policy considerations.

The *Bridge* Court's refusal to adopt a bright-line rule on reliance means that lower courts will have to engage in a fact-specific inquiry to determine whether a plaintiff's pleadings or proof comport with the proximate causation requirement. A plaintiff advancing a claim predicated on mail or wire fraud[33] will generally have to show that *someone* relied on the defendant's alleged misrepresentation, and that this reliance caused the plaintiff's injury. Evaluation of whether the causal connection is sufficiently direct to allow recovery under RICO will require litigants and courts to analogize particular factual scenarios to those presented in *Holmes*, *Anza*, and *Bridge*.

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If you have any questions about the issues addressed in this memorandum or if you would like a copy of any of the materials mentioned, please do not hesitate to call or email Charles A. Gilman at (212) 701-3403 or cgilman@cahill.com; Ed Krugman at (212) 701-3506 or ekrugman@cahill.com; Jon Mark at (212) 701-3100 or jmark@cahill.com; John Schuster at (212) 701-3323 or jschuster@cahill.com; Nathan Holcomb at (212) 701-3748 or nholcomb@cahill.com.

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28 *Id.* (quoting *Anza*, 547 U.S. at 478 (Thomas, J., concurring in part and dissenting in part)).

29 *Id.* at 19-20.

30 *Id.* at 20.

31 *Id.* at 6 (quoting *Anza*, 547 U.S. at 461).

32 *Id.* at 8.

33 The reasoning in *Bridge* applies equally to the wire fraud statute.