

LITIGATION ALERT

SUPREME COURT CLARIFIES CAUSAL “DIRECTNESS” REQUIREMENT IN PRIVATE CIVIL ACTIONS UNDER RICO



On June 5, 2006, the Supreme Court issued its decision in No. 04-433, *Anza v. Ideal Steel Supply Corp.*, clarifying the causal “directness” requirement in private civil actions under the Racketeer Influenced and Corrupt Organizations Act (RICO). By a vote of 7-2, the Court held that a company failed to state a civil RICO claim against a competitor where the company alleged only that the competitor’s fraudulent evasion of state sales taxes had placed the company at a competitive disadvantage. Such allegations, the Court held, are insufficient to establish that a plaintiff’s injuries “were the direct result of a RICO violation.”

The case arose under 18 U.S.C. § 1962(c) and was brought pursuant to 18 U.S.C. § 1964(c), which creates a private right of action for “[a]ny person injured in his business or property by reason of a violation” of RICO’s substantive provisions. Ideal Steel Supply Corporation invoked Section 1964(c) in a civil suit against its competitor, National Steel Supply, Inc., in the Southern District of New York. Ideal alleged that National had engaged in an unlawful “pattern of racketeering activity” by failing to charge its customers New York state sales taxes and then by fraudulently concealing this practice from the state. Ideal alleged that National’s sales tax scheme “allowed National to reduce its prices without affecting its profit margin,” thereby placing Ideal at a competitive disadvantage. Ideal’s argument proved unavailing in the district court, which dismissed the complaint, but the 2nd Circuit adopted Ideal’s theory of the case, holding that where a complaint alleges a pattern of racketeering activity “that was intended to and did give the defendant a competitive advantage over the plaintiff, the complaint adequately pleads proximate cause, and the plaintiff has standing to pursue a civil RICO claim.”

The Supreme Court reversed, finding that Ideal’s complaint failed the test set forth in *Holmes v. Securities Investor Protection Corporation*, where the Court held that Section 1964(c) requires proof of “some direct relation between the injury asserted and the injurious conduct alleged.” Such a direct relation cannot exist, the Court concluded, where the immediate victim of the alleged unlawful conduct is a party other than the plaintiff, and where the cause of the plaintiff’s injuries is a set of actions “entirely distinct from the alleged RICO violation.” In the majority’s view, Ideal failed to state a civil RICO claim because the direct victim of National’s alleged tax evasion was the state of New York, rather than Ideal itself, and because Ideal’s injuries were caused by “a set of actions (offering lower prices) entirely distinct from the alleged RICO violation (defrauding the state).” In reaching this conclusion, the Court emphasized that the

“directness” requirement serves the important functions of preventing “intricate, uncertain [causal] inquiries from overrunning RICO litigation” and preserving a bright “line between RICO and the antitrust laws.” The Court remanded a separate claim under Section 1962(a) for reconsideration in light of its decision with respect to Ideal’s claim under Section 1962(c).

Justice Thomas concurred in part and dissented in part. In his view, “[t]he Court’s stringent proximate-causation requirement . . . eliminates recovery for plaintiffs whose injuries are precisely those that Congress aimed to remedy through the authorization of civil RICO suits,” namely, persons injured by organized crime. Although Justice Thomas acknowledged that Ideal’s suit had “no apparent connection to organized crime,” he had no trouble identifying the causal connection between Ideal’s injury and National’s conduct: “Here, the relationship between the alleged RICO violation and the alleged injury is clear: Petitioners underpaid sales tax, permitting them to undercharge sales tax, inflicting competitive injury on respondent.”

Justice Breyer concurred in part and dissented in part, concluding that RICO “does not cover claims of injury by one competitor where the legitimate pro-competitive activity of another competitor immediately causes that injury.” In Justice Breyer’s view, Ideal had failed to allege “a harm caused directly by something other than ordinary competitive activity, i.e., lower prices, a better product, a better distribution system, or a better production method.” Although Justice Breyer recognized that Ideal had alleged an illegal scheme to defraud the state, he contended that National had “in effect cut the price of the item by the amount of the sales tax and then kept the money instead of passing it on to the state.” In Breyer’s view, “the source of the savings is . . . beside the point as long as the price cut itself is legitimate.”

Also on Monday, the Court issued a brief order in the case of *Mohawk Industries v. Williams* (05-465). The Court determined that certiorari in Mohawk had been improvidently granted as to the question of whether a corporation and its agents could constitute a RICO “association-in-fact” enterprise, and remanded the case to the 11th Circuit for reconsideration of proximate causation in light of the decision in *Ideal*.

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