

## MEMO

To: Public  
From: Jeffrey Harrington

### **Limitations Period in Civil RICO Litigation**

Congress enacted the Racketeer Influenced Corrupt Organizations Act (RICO)<sup>1</sup> in the late 1960s in order to combat organized crime. In addition to criminal sanctions, RICO permits private actions to be brought in federal district courts. Because the Supreme Court has interpreted the Act to encompass a range of activities well beyond typical mobster operations<sup>2</sup> (i.e. white-collar crime), defendants seek cost-effective defenses that lead to dismissal of plaintiffs' claims or favorable summary judgment. The statute of limitations is one defense that has figured prominently in civil RICO litigation as much for its unsettled aspects as for its ability to get professionals out of court relatively quickly and inexpensively.

### **The Applicable Statute of Limitations**

The RICO statute does not expressly establish a period of limitations. The applicable statute of limitations for federal actions under RICO was judicially established in *Agency Holding Corp., v. Malley-Duff & Associates, Inc.*<sup>3</sup>, where the Supreme Court adopted the four-year period applicable to Clayton Act civil enforcement actions. The Court reasoned the Clayton Act provides a closer analogy than state statutes in terms of its purpose and structure<sup>4</sup>. Prior to *Malley-Duff*, courts had to decide whether to apply some other federal statute of limitations or resort to state law. Turning to state law for guidance required 1) determination of which state's law to apply for purposes of timeliness and 2) which state statute to borrow from given the

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<sup>1</sup> 18 U.S.C.A. §§1961-1968

<sup>2</sup> see *Sedima, S.P.R.L. v. Imrex Co., Inc.*, 473 U.S. 479 (1985) and *American National Bank and Trust Co. of Chicago v. Haroco, Inc.*, 473 U.S. 606 (1985).

<sup>3</sup> 483 U.S. 143 (1987)

<sup>4</sup> *Id.* at 143. In the Court's view, the need for a uniform limitations period arose from the diverse nature of predicate acts and the fact that certain important RICO concepts were unknown at common law.

essential nature of the federal cause of action.<sup>5</sup> This practice led to what the Court in *Malley-Duff* termed “intolerable uncertainty for parties and time-consuming litigation.”<sup>6</sup> In spite of this criticism, however, the Court merely established the four-year limitation period without deciding when the period accrues or how it is tolled.

### **Accrual of the Limitations Period**

In the wake of *Malley-Duff*, three distinct approaches arose for determining when a civil RICO limitations period begins to run, two of which have been recently rejected by the Supreme Court: the “Injury and Pattern Discovery” rule, the “Last Predicate Act” rule, and the “Injury Discovery” rule<sup>7</sup>. When statutes say nothing about when a cause of action accrues, federal courts generally apply a discovery rule<sup>8</sup>. Since RICO claims require a pattern of racketeering, which may be complex and hard to detect, some courts placed accrual at the time the claimant discovered, or should have discovered, both an injury and a pattern of RICO activity<sup>9</sup>. The plaintiff in *Rotella v. Wood*<sup>10</sup> argued for the “Injury and Pattern Discovery” rule on these grounds, but the Supreme Court responded that such an approach would allow finding a pattern of racketeering in predicate acts as much as 10 years apart<sup>11</sup>, which could potentially allow a cause of action to last decades. Such would defeat the fundamental aim of limitations periods: repose, elimination of stale claims, and certainty regarding potential liability<sup>12</sup>.

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<sup>5</sup> 21 Willamete L. Rev. 683, 689

<sup>6</sup> *Agency Holding Corp. v. Malley-Duff & Associates, Inc.* at 143

<sup>7</sup> *Rotella v. Wood*, 528 U.S. 549, 553 (2000). Plaintiff was a patient at a psychiatric facility and brought suit against physicians and their related business entities, alleging they improperly conspired to admit, treat, and retain him for reasons related to their own financial interests, rather than his psychiatric condition. Defendants argued the action was time barred.

<sup>8</sup> see *Klehr v. A.O. Smith Corp.*, 521 U.S. 179, 191 (1997); *United States v. Kubrick*, 444 U.S. 111 (1979)

<sup>9</sup> see *Caproni v. Prudential Securities, Inc.*, 15 F.3d 614, 619-620 (C.A. 6 1994); *Granite Falls Bank v. Henrikson*, 924 F.2d 150, 154 (C.A. 8 1991); *Bath v. Bushkin, Gaims, Gaines & Jones*, 913 F.2d 817, 820-821 (C.A. 10 1990)

<sup>10</sup> 528 U.S. 549

<sup>11</sup> §1961(5) “pattern of racketeering” requires at least two acts of racketeering activity occurring within a 10-year period.

<sup>12</sup> *Rotella*, 528 U.S. at 554

Previous to *Rotella*, the Supreme Court had rejected the Third Circuit’s “Last Predicate Act” rule in *Klehr v. A.O. Smith Corp.*<sup>13</sup>. The “Last Predicate Act” rule is identical to the “Injury and Pattern Discovery” rule except accrual begins anew each time the defendant commits a predicate act related to the same pattern of activity. Again, the Court reasoned predicate acts can continue indefinitely and be separated by as many as 10 years, thus allowing a right of action to exist well beyond any limit contemplated by Congress<sup>14</sup>.

The fact that two of the three predominate approaches to accrual have been rejected does not mean the third, the “Injury Discovery” rule, has been adopted. While the “Injury Discovery” rule is favored by the majority of Circuits to have addressed the matter<sup>15</sup>, the Supreme Court has expressly declined to make it the final rule<sup>16</sup>. One option the Court leaves open is the “Injury Occurrence” rule espoused by Justice Scalia, under which discovery of the injury would be irrelevant. Such an approach would favor defendants and, thus, raise concern on the other side of the balance. Perhaps aware of this danger, the Court in *Rotella* noted, without stating more, that RICO’s statute of limitations is subject to equitable principles of tolling<sup>17</sup>, an option that has served to bolster plaintiffs’ position against the trend towards more stringent limitations.

### **Tolling the Limitations Period**

Courts that have permitted equitable tolling of the four-year limitations period in civil RICO cases have tended to base their decision on one of three grounds: fraudulent concealment, continuing tort or conspiracy, or pendency of another court action. There are cases in every Circuit that demonstrate courts’ willingness to toll the statute of limitations where the defendant

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<sup>13</sup> 521 U.S. 179 (1997). Dairy farmers who purchased allegedly defective feed storage silo brought a RICO action against manufacturer and seller of silo.

<sup>14</sup> *Id.* at 189

<sup>15</sup> *Rotella*, 528 U.S. at 554

<sup>16</sup> *Rotella*, 528 U.S. at 554.

<sup>17</sup> 528 U.S. at 560-561.

has fraudulently concealed either the injury or the fraud<sup>18</sup>. However, there are at least three ways a plaintiff's conduct can vitiate the right to equitable tolling even where a defendant's fraudulent concealment is found. For example, Third Circuit courts have held that where the plaintiff is on notice of a potential claim, the doctrine of fraudulent concealment is not grounds for tolling no matter how egregious the defendant's fraudulent concealment is<sup>19</sup>. Improper pleading has also prevented tolling even where the defendant might be guilty of fraudulent concealment. At least one Seventh Circuit Court of Appeals has refused to toll the limitations period because the plaintiff failed to allege either that she exercised due diligence or that defendants actively concealed their misrepresentations<sup>20</sup>.

The most significant reason courts have refrained from tolling the limitations period even in the presence of fraudulent concealment is a plaintiff's lack of due diligence. The contours of due diligence differ slightly among the Circuits. A Second Circuit court forwards an objective test of due diligence that requires the plaintiff to investigate the situation when inquiry would reasonably be believed to develop the truth<sup>21</sup>. Similarly, the Supreme Court in *Klehr* held plaintiffs could only assert the fraudulent concealment doctrine if they had been reasonably diligent in trying to discover their civil RICO claims<sup>22</sup>. A Ninth Circuit court seems to add to the requirement by stating a plaintiff must plead with particularity the circumstances surrounding the

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<sup>18</sup> 156 A.L.R. 361.

<sup>19</sup> *Davis v. Grusemeyer*, 996 F.2d 617 (3<sup>rd</sup> Cir. 1993). A civil RICO action brought by an automobile body shop owner against law enforcement officials based on their activity during a sting operation and during prosecution of the owner once he was caught in the sting operation.  
*Anderson v. Consol-Pennsylvania Coal Co.*, 945 F.2d 394 (3<sup>rd</sup> Cir. 1991), judgment aff'd, 945 F.2d 394 (3<sup>rd</sup> Cir. 1991). Property owners filed a civil RICO action alleging that rail companies, coal companies, and others conspired to acquire their real-estate at lower than its true value by misrepresenting condemnation powers and by concealing coal companies' involvement in a right-of-way acquisition and construction of a rail line. The court held the theory of fraudulent concealment may work to extend the limitations period; however, admissions of actual notice undercut equitable theories of the tolling advanced.

<sup>20</sup> *Davenport v. A.C. Davenport & Son Co.*, 903 F.2d 1139 (7<sup>th</sup> Cir. 1990)

<sup>21</sup> *In re Ahead by a Length, Inc.*, 100 B.R. 157 (Bankr. S.D.N.Y. 1989). Trustee for an involuntary Chapter 7 corporate debtor brought an adversary proceeding against defendants, who had allegedly agreed to submit phony invoices to the corporate debtor from corporations they owned.

<sup>22</sup> 521 U.S. at 194

concealment and state facts showing due diligence in trying to uncover the facts. That is, the plaintiff must allege facts showing affirmative conduct on the part of the defendant that would, under the circumstances, lead a reasonable person to believe he did not have a claim for relief<sup>23</sup>. Some courts shift the burden of proof to the defendant once the defendant's fraudulent concealment has been established. For example, in the D.C. Circuit, a defendant found guilty of fraudulent concealment can only prevent the tolling of the limitations period by showing the plaintiff could have discovered the cause of action by exercise of due diligence<sup>24</sup>.

Courts in several Circuits have held a continuing tort or conspiracy may serve as grounds for equitable tolling in civil RICO cases. A First Circuit decision holds that a continuing tort sufficient to toll the statute of limitations is characterized by continual unlawful acts, not continuing ill effects from the original act<sup>25</sup>. A Second Circuit court specifies plaintiffs must allege at least two acts of racketeering activity occurring within 10 years of each other, and that such acts must be related and pose a threat of continued criminal activity. Advancing what sounds like a modified version of the "Last Predicate Act" rule, the same court recognized a "separate accrual" rule whereby a new claim accrues and the limitations period begins anew each time plaintiff discovers, or should have discovered, a new injury<sup>26</sup>. Similarly, in considering the "continuing conspiracy" exception, a Fifth Circuit court held that each time a plaintiff is injured

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<sup>23</sup> *Continental Ins. Co. v. Pierce County, Wash.*, 690 F. Supp. 930 (W.D. Wash. 1987), judgment aff'd, 877 F. 2d 64 (9<sup>th</sup> Cir. 1989). Somewhat confusingly, however, the court ultimately concluded that as long as the plaintiffs had no reason to suspect a predicate act, a defendant's fraudulent concealment would toll the statute of limitations.

<sup>24</sup> *Riddle v. Riddel Washington Corp.*, 866 F.2d 1480 (D.C. Cir. 1989); see also *Solano v. Delmed, Inc.*, 759 F. Supp. 847 (D.D.C. 1991)

<sup>25</sup> *UST Capital Corp. v. Charter Nat. Life Ins. Co.*, 684 F. Supp. 757 (D. Mass. 1986). The court held that because the plaintiff failed to cite a case which held that it is an "unlawful act" to bring a lawsuit to collect on a fraudulently acquired debt, the statute of limitations was not tolled.

<sup>26</sup> *Congregacion de la Mision Provincia de Venezuela v. Curi*, 978 F. Supp. 435 (E.D.N.Y. 1997).

by an act of the defendant, a cause of action accrues to recover damages and, as to those damages, the statute of limitations runs from the commission of the act<sup>27</sup>.<sup>28</sup>

Courts may also toll the statute of limitations when there is another court action pending, typically a class action. A Second Circuit court has held that upon commencement of a class suit, the statute of limitations is tolled for all members of the putative class. For tolling in this situation, the court required adequate notice to the defendant and at least a generic identification of the potential plaintiffs who might participate in the judgment<sup>29</sup>. Nothing conclusive is yet known regarding whether a pending state claim may be grounds for equitable tolling in this context; however, an unpublished opinion from a district court in Illinois finds the filing of a prior state court action provides no basis for tolling the statute of limitations on a federal RICO action.<sup>30</sup>

## Conclusion

Perhaps criticism courts have received from the expansive reading given the RICO Act has resulted in the modern trend towards imposing a more stringent limitations period. Courts, mindful of the liability business individuals and other professionals outside of the world of organized crime are exposed to under RICO, are clearly reluctant to increase defendants' exposure by allowing liberal methods of determining accrual and equitable tolling. The validity of policies behind limitations notwithstanding, courts should not lose sight of the main objective

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<sup>27</sup> *Al George, Inc. v. Envirotech Corp.*, 939 F.2d 1271 (5<sup>th</sup> Cir. 1991) Where defendants in a patent infringement suit filed an action against the patent holder, alleging antitrust and RICO violations, malicious prosecution, and unfair competition, the court held that the last predicate act in pursuance of the alleged conspiracy was the filing of the patent infringement suit, so the "continuing conspiracy" theory could not be invoked to save the antitrust and RICO causes of action from being time barred.

<sup>28</sup> Arguably, these decisions came out before the ruling in *Klehr* went into effect, though the opinion in *Curi* was actually issued nearly three months after *Klehr*. In any event, the decisions illustrate how equitable tolling can save claims the Supreme Court, ostensibly, meant to bar.

<sup>29</sup> *Camotex, S.R.L. v. Hunt*, 741 F.Supp. 1086 (S.D.N.Y. 1990). See also *Anderson v. Consol-Pennsylvania Coal Co.*, 740 F. Supp. 1126 (W.D. Pa 1990), judgment aff'd, 945 F.2d 394 (3d Cir. 1991).

<sup>30</sup> *Board of Managers of Dunbar lakes Condominiums Nos. I, II, III, IV, V, VI, VII, VIII, IX and X v. Dunbar Home, Inc.*, 1991 WL 18194 (N.D. Ill. 1991) [unpublished]

behind RICO, which is to eliminate racketeering activity by turning victims into “private attorneys general.”<sup>31</sup> Courts should be careful that efforts at encouraging prompt litigation do not deprive civil RICO of its teeth.

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<sup>31</sup> *Klehr*, 521 U.S. at 187