CASE COMMENTS

SOLE PROPRIETOR AS DEFENDANT AND "ENTERPRISE" UNDER RICO

United States v. Benny, 786 F.2d 1410 (9th Cir. 1986)

In *United States v. Benny*[1] the United States Court of Appeals for the Ninth Circuit further defined the "associated with" requirement of RICO, 18 U.S.C. section 1962(c),[2] by indicating that a sole proprietor can associate with his own proprietorship so long as the "enterprise"[3] can be separated from the individual, either by formal incorporation[4] or where other people work for the proprietor.[5]

George Benny, sole proprietor of "George I. Benny," was convicted under RICO provision 18 U.S.C. section 1962(c).[6] The indictment alleged schemes to defraud institutional lenders.[7] Benny argued that the RICO conviction should be reversed because the defendant or "person"[8] and the "enterprise"[9] cannot be the same individual.[10]

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1. 786 F.2d 1410 (9th Cir. 1986).

2. 18 U.S.C. § 1962(c) (1984 & Supp. 1988) provides as follows:

> It 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 enterprises' affairs through a pattern of racketeering activity or collection of unlawful debt.

3. *See infra* note 9.

4. *See infra* note 62.

5. 786 F.2d 1410, 1414-16.

6. 786 F.2d 1410, 1413. In addition to the RICO count, the jury convicted Benny of twenty-one counts of mail fraud under 18 U.S.C. § 1341-42 (1984).

7. *Id.* Benny's sole proprietorship engaged, *inter alia*, in the acquisition and management of real estate. His schemes involved defrauding institutional lenders in the financing of a northern California apartment building and a planned community to be built on a Nevada Ranch. Benny either employed or associated with four other defendants, each of whom pleaded guilty to lesser charges in exchange for their testimony against Benny.

8. RICO defines "person" as including "any individual or entity capable of holding a legal or beneficial interest in property." 18 U.S.C. § 1961(3) (1984 & Supp. 1988).

9. RICO defines "enterprise" to include "any individual, partnership, corporation, association, or other legal entity, and any unions or group of individuals associated in fact although not a legal entity." 18 U.S.C. § 1961(4) (1984 & Supp. 1988). *See* United States v. Parnes, 305 F.2d 430 (2d Cir. 1974), *cert. denied*, 419 U.S. 1105 (1975) (the Second Circuit Court of Appeals first dealt with the scope of the term "enterprise"). *See generally* Note, *The Enterprise Element in RICO: A Proposed Interpretation*, 49 GEO. WASH. L. REV. 123 (1980) (distinction must be made between de facto associational enterprise and legal entity enterprise). *See also* Woodbridge, *RICO: The Corporation as "Enterprise" and Defendant*, 52 U. CIN. L. REV. 503, 505 (1983) ("the enterprise element is the cornerstone of RICO").

Benny appealed his conviction in the United States District Court for the Northern District of California to the Ninth Circuit Court of Appeals.[11] The Ninth Circuit affirmed the conviction and *held*: a sole proprietor may be convicted under RICO section 1962(c) where the sole proprietorship is the "enterprise" with which the defendant proprietor "associates," if the proprietorship is incorporated or the proprietor has other employees.[12]

To be convicted under RICO section 1962(c) a "person" must be employed by or "associated with" an "enterprise" that uses interstate commerce for racketeering activity or collection of unlawful debt.[13] The RICO statute includes both formal and informal organizations in its definition of enterprise.[14] Most RICO litigation involves defining "enterprise" because the concept of "enterprise" is the hub of a RICO conviction.[15] The *Benny* case, however, focuses on the parameters of the phrase "associates with" in the context of section 1962. The central issue of the *Benny* decision, and a theoretical question rarely discussed by courts and commentators, is how a sole proprietor can associate with his own business within the meaning of section 1962.

Congress enacted RICO in 1970[16] to give new strength to the government's crusade against organized crime and its economic roots.[17] Notwithstanding this legislative intent, the government prosecuted few RICO cases following RICO's enactment.[18] This trend ended in 1975 when the head of a Justice Department strike force lectured to United States Attorneys on the potential use of the statute.[19] Much of the RICO litigation since 1975 has focused on section 1962.[20]

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10. 786 F.2d 1410, 1414-16. *See infra* notes 55-57 and accompanying text.

11. United States v. Benny, 559 F. Supp. 264, 265-66 (N.D. Cal. 1983).

12. 786 F.2d at 1414-16.

13. *See infra* note 17.

14. *See* 1 K. BRICKEY, CORPORATE CRIMINAL LIABILITY § 7:03 (1984).

15. *Id.*

16. The Racketeer Influenced and Corrupt Organization Act (RICO) was enacted as Title IX of the Organized Crime Control Act of 1970, Pub. L. No. 91-452, §§ 901-904, 84 Stat. 922, 941-44 (1970).

17. Russello v. United States, 471 U.S. 858 (1983).

18. 1 K. BRICKEY, *supra* note 14, § 7:01.

19. *Id.*

20. "Section 1962 defines four distinct RICO offenses:
§ 1962(a) prohibits investment of income that is derived directly or indirectly from a pattern of racketeering activity or through collection of an unlawful debt.
§ 1962(b) prohibits acquisition or maintenance of an interest in or control of an enterprise engaged in or affecting interstate commerce.
§ 1962(c) prohibits those who are employed by or associated with enterprises that are en-

The Supreme Court first addressed RICO[21] in *United States v. Turkette*.[22] In *Turkette* the Court established the standard by which courts should interpret the statute, and delved into its own interpretation of section 1962(c).[23] In holding that a RICO enterprise includes legal as well as illegal entities,[24] the Court stated that the RICO statute should be liberally construed to accomplish its remedial purposes in fighting organized crime.[25] The court also indicated that an "enterprise" is not a "pattern of racketeering activity" under section 1962(c), but is an entity separate and apart from the pattern of activity in which it engages.[26] This "separate entity" requirement has led to unresolved confusion among the circuits.[27]

Turkette gave rise to the much litigated issue of whether a corporation may be simultaneously both a defendant and the enterprise under section 1962(c).[28] The circuits differ in their resolution of this issue.[29] The Eleventh Circuit, in *United States v. Hartley*,[30] held that a corporation may be

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gaged in or that affect commerce from conducting or participating, directly or indirectly, in the conduct of the affairs of the enterprise through a pattern of racketeering activity or unlawful debt collection.

§ 1962(d) makes conspiracy to commit any substantial RICO violation an independent punishable offense."

1 K. BRICKEY, *supra* note 14, § 7:02. *See also* Woodbridge, *supra* note 9, at 504 ("RICO punishes as defendants those persons who commit predicate offenses in connection with the enterprise").

21. United States v. Turkette, 452 U.S. 576, 579 (1980). The original indictment charged the defendant and 12 others as an "enterprise" (a group of individuals associated in fact) with, *inter alia*, conspiring to distribute narcotics.

22. The other important Supreme Court case dealing with RICO is Sedima, S.P.R.L. v. Imrex Co., Inc., 473 U.S. 479 (1985) (failed attempt to narrow RICO elements by imposing a "racketeering enterprise injury" requirement on top of the statutory requirement of showing of injury resulting from an enterprise being conducted through a pattern of racketeering activity). For a discussion of *Sedima* and *Turkette*, see Papai v. Gremosnik, 635 F. Supp. 1402 (N.D. Ill. 1986).

23. *See supra* notes 2, 14 and 15.

24. White, J., delivered the opinion of the Court in which Burger, C.J., and Brennan, Marshall, Blackmun, Powell, Rehnquist, and Stevens, JJ., joined. Stewart, J., filed a dissenting statement.

25. 452 U.S. at 587. The Court quoted from § 904(a) of RICO, 84 Stat. 947. *See supra* note 17 (Congress envisioned a broad reading of RICO).

26. 452 U.S. at 583.

27. *See generally* Woodbridge, *supra* note 9.

28. K. BRICKEY, *supra* note 14, § 7:03.1.

29. *See infra* notes 31 and 36.

30. 678 F.2d 961 (11th Cir. 1982). Defendants were convicted before the United States District Court for the Middle District of Florida of conspiracy, mail fraud, violations of the National Stolen Property Act and RICO. The RICO conviction was for defrauding the United States Department of Defense by intentionally supplying it with frozen shrimp that did not conform to military contract specifications.

both a defendant and the enterprise under section 1962(c).[31] *Turkette* requires proof of the corporation as a separate entity from the enterprise. The *Hartley* court, however, decided that the existence of the corporation, in and of itself, proved the separate enterprise element.[32] Commentators favor the Eleventh Circuit's holding; however, only this circuit takes such an approach.[33]

In a decision reached at virtually the same time as *Hartley*, the Fourth Circuit decided in *United States v. Computer Sciences Corporation*,[34] that the "enterprise" must be something different from the RICO defendant.[35] In explaining why an unincorporated division of a company could not conspire with its parent company, the court reasoned that a person cannot conspire with himself.[36] Thus, because the court found that the unincorporated division was a part of the parent corporation, the court discharged the corporation's section 1962(c) liability.[37] Although *Computer Sciences* has attracted a great deal of criticism,[38] a majority of the

31. *Id.* at 988-90. *See supra* notes 8-9. *See generally* Blakey, *The RICO Civil Fraud Action in Context: Reflections on Bennet v. Berg*, 58 NOTRE DAME L. REV. 237, 286-325 (1982) (discussing distinction between "enterprise" and "person").

32. 678 F.2d 961, 988-90. The court gave three rationales for its holding: 1) evidence of the defendant's corporate existence would satisfy the enterprise element separate and apart from the other statutory requirements; 2) the problem would not have come about if the government had "charged the defendants collectively as an 'association in fact' and charged the defendant corporation singly as the enterprise." *Id.*; and 3) under "basic corporations law" the court could "pierce the Corporate Veil" and "view Treasure Isle . . . in a different light for each of the roles it assumes in this case." *Id. See* Haas, *Criminal Law II*, 59 N.Y.U.L. REV. 1243, 1262 (1984). *See also* K. BRICKEY, *supra* note 14, § 7:03.

33. *See* Blakey, *supra* note 31, at n.181. ("*Hartley* is a thoughtful, well-reasoned opinion . . ."). *See also* Woodbridge, *supra* note 9, at 523. ("the strong anticrime stance adopted by Congress militates in favor of allowing prosecutors to indict corporations as defendants under RICO.") *But see* Tarlow, *RICO Revisited*, 17 GA. L. REV. 291, 345 n.232 ("United States v. Hartley is characterized by superficial and unpersuasive reasoning.")

34. 689 F.2d 1181 (4th Cir. 1982). *Hartley* was decided on June 17, 1982, while *Computer Science* was decided on June 16, 1982. (*Computer Science* involved criminal action brought against a corporation and six defendants for alleged RICO offenses, wire fraud, mail fraud, and making false claims to United States Government.)

35. *Id.* at 1190. ("A corporation, in common parlance, is not regarded as distinct from its unincorporated divisions either.")

36. *Id.* For the definition of "person," see *supra* note 8.

37. *Id.*

38. *See* Woodbridge, *supra* note 9, at 521-22. (The author claims that the court's holding in *Computer Science* that the RICO enterprise must be something different from the persons whose behavior the act was designed to prohibit is unsupported. The author supports *Hartley* as having "delved more deeply into the logic of the situation and reached a solution compatible with RICO policy as well as corporate law principles.") *See also* K. BRICKEY, *supra* note 14, § 7:03 at n.83. (The court in *Computer Science* erroneously relied on the district court's analysis of the enterprise

courts adhere to this view.[39]

The Seventh Circuit reached a compromise between the divergent holdings of *Hartley* and *Computer Sciences*.[40] In *Haroco, Inc. v. American National Bank and Trust Co. of Chicago*,[41] the court agreed with the Fourth Circuit that a corporation could not be named as both the "person" and the "enterprise" under section 1962(c).[42] To better effectuate the overall purpose of RICO,[43] however, the *Haroco* court held that the language of section 1962(a)[44] does permit the corporation to be both a "person" and the "enterprise" when the corporation is the beneficiary and not the victim of the crime.[45] Because the Supreme Court affirmed *Haroco* on other grounds, the disagreement between the circuits remains unresolved.[46]

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issue. That court used the antitrust doctrine that there is no legal existence for an unincorporated division separate from the corporation.) Brickey also notes at *id.* §§ 6:11-6:21, that such notions of intra-enterprise and intra-corporate liability are unique to antitrust conspiracy liability. *See also* Brickey, *Conspiracy, Group Danger and the Corporate Defendant*, 52 U. CIN. L. REV. 431 (1983). *See supra* note 30.

39. *See* Schofield v. First Commodity Corp. of Boston, 793 F.2d 28 (1st Cir. 1986), Bennett v. United States Trust Co. of New York, 770 F.2d 308, 315 (2d Cir. 1985), *cert. denied*, 106 S. Ct. 800 (1986); B.F. Hirsch v. Enright Refining Co., 751 F.2d 628, 633-34 (3d Cir. 1984); Haroco v. American National Bank and Trust Co. of Chicago, 747 F.2d 384, 401-402 (7th Cir. 1984), *aff'd on other grounds*, 473 U.S. 606 (1985); Rae v. Union Bank, 725 F.2d 478, 480-81 (9th Cir. 1984); Bennett v. Berg, 685 F.2d 1053, 1061-62 (8th Cir. 1982), *modified*, 710 F.2d 1361 (en banc), *cert. denied*, 464 U.S. 1008 (1983); United States v. Computer Sciences Corp., 689 F.2d 1181, 1190 (4th Cir. 1982), *cert. denied*, 459 U.S. 1105 (1983); Yancoski v. E.F. Hutton Co., 581 F. Supp. 88, 97 (E.D. Penn. 1983); Van Schaick v. Church of Scientology of Cal. Inc., 535 F. Supp. 1125, 1135-1136 (D. Mass. 1982); Parnes v. Heinold Commodities, Inc., 548 F. Supp. 20, 23-24 (N.D. Ill. 1982).

40. *See* Haas, *supra* note 32, at 1267-68.

41. 747 F.2d 384 (7th Cir. 1984), *aff'd*, 473 U.S. 606 (1985) (per curiam).

42. *Id.* at 402.

43. *See supra* note 17 and accompanying text.

44. Section 1962(a) provides in pertinent part:

> It shall be unlawful for any person who has received any income derived, directly or indirectly, from a pattern of racketeering activity or through collection of an unlawful debt in which such person has participated as a principal within the meaning of section 2, title 18, United States Code, to use or invest, directly or indirectly, any part of such income, or the proceeds of such income, in acquisition of any interest in, or the establishment or operation of, any enterprise which is engaged in, or the activities of which affect, interstate or foreign commerce.

18 U.S.C. § 1962(a) (1984).

45. *Id. See* Haas, *supra* note 32, at 1263-64. The author discusses the difference between *Haroco* as a criminal RICO case and *Hartley* and *Computer Sciences* as civil RICO cases. He notes that although the Eighth Circuit is bound by its holding in *Bennett* favoring *Computer Sciences*, that circuit is still free to choose between *Hartley* and *Computer Sciences* in criminal RICO cases.

But see Haroco, 747 F.2d at 400. (The court expressly held that the civil-criminal distinction was irrelevant.)

46. *See* Haas, *supra* note 32, at 1260-68.

In *McCullough v. Suter*[47] the Seventh Circuit distinguished its holding in *Haroco*[48] to uphold the conviction of a sole proprietor under section 1962(c).[49] The defendant and several employees ran a coin investment scam under a *nom de guerre*.[50] The Court held that a sole proprietorship may be the "enterprise" with which the proprietor "associates" if the proprietorship is formally incorporated[51] or has other employees.[52]

The *McCullough* court recognized that the result would be different if the sole proprietorship were merely a "one-man show."[53] A person cannot associate with himself, any more than he can conspire with himself, simply by using a different name.[54] Because the defendant had several employees, however, the court considered his business an enterprise,[55] not just a "one-man band."[56] The court regarded this enterprise as distinct and separate from the defendant sole proprietor, and thereby concluded that a conspiracy could exist under the *Haroco* rule.[57] Thus, the defendant could be reached under section 1962(c).

In *United States v. Benny*[58] the Ninth Circuit broke new ground and became only the second circuit to deal with the sole proprietorship issue. The defendant, Benny, argued that because he was a sole proprietorship, he could not "associate with" that sole proprietorship under section 1962(c); one cannot associate with oneself any more than one can conspire with oneself.[59] Benny based his argument on the *Computer Sciences* and *Haroco* line of cases, which held that under section 1962(c), a corporate defendant cannot also be the related "enterprise," that is, a

47. 757 F.2d 142 (7th Cir. 1985).

48. For a good analysis of the interplay between *Haroco* and *McCullough* see United States v. Dicaro, 772 F.2d 1314, 1319-20 (7th Cir. 1985) (if Suter had not had employees, then *Haroco* would have precluded liability for him under § 1962(c)).

49. 757 F.2d at 144.

50. *Id.* at 143. Defendant Suter, under the name National Investment Publishing Company, advised and bought coins on clients' behalf. Suter received $23,000 to invest and in return sent coins worth only $10,000. He pleaded guilty to two counts of mail fraud. *Id.*

51. *See infra* note 62.

52. 757 F.2d at 144. *See* Woodbridge, *supra* note 9, at 518. The author notes that the deep-pocket theory is what makes publicly held corporations open to accusation as defendants. On the other hand, closely held or one-person operations do not often get accused as RICO defendants. Therefore, *McCullough* is a unique case.

53. 757 F.2d 142, 144.

54. *Id.*

55. *See supra* note 9.

56. 757 F.2d 142, 144.

57. *Id. See supra* text accompanying notes 41-2.

58. 786 F.2d 1410 (9th Cir. 1986).

59. *Id.* at 1415.

division of a corporation cannot associate with that corporation.[60]

In response, the *Benny* court distinguished the cases upon which the defendant relied.[61] The court said those cases factually resemble a sole proprietorship without employees.[62] That is, a sole proprietorship can no more associate with himself than a corporation can associate with itself. The court found the facts of *Benny* distinguishable in that the proprietorship had employees.[63] Benny, together with his employees, as a group "associated in fact," formed an "enterprise" operating under the name of one of the employees. Because the indictment separated defendant Benny, an individual, from the enterprise, the charge actually complied with the *Haroco* rule.[64]

The *Benny* court thus adopted the Seventh Circuit's rule in holding that a sole proprietorship may be the "enterprise" with which the proprietor "associates" if the proprietorship is formally incorporated or has other employees.[65] The *Benny* court reasoned that this rule avoids the untenable result of interpreting RICO to make liable an individual who associates with himself or herself.[66] Simultaneously, the rule helps retain the "teeth" necessary to effectuate the statute's purpose of deterring and punishing criminal activity.[67]

The *Benny* court's analysis of the sole proprietorship issue is persuasive. The court was correct in analogizing the *Computer Sciences* and *Haroco* line of cases to a situation involving a sole proprietorship without employees.[68] A contrary holding would subject the true "one man

60. *See supra* notes 31-34, 41-2 and accompanying text.

61. 786 F.2d 1410, 1415. *Benny* relied on Rae v. Union Bank, 725 F.2d 478, 481 (9th Cir. 1984); United States v. DiCaro, 772 F.2d 1314, 1319-20 (7th Cir. 1985); Haroco v. American National Bank, 747 F.2d 384, 399-400 (7th Cir. 1984), *aff'd on other grounds*, 473 U.S. 606 (1985); United States v. Computer Sciences, 689 F.2d 1181, 1190 (4th Cir. 1982), *cert. denied*, 459 U.S. 1105 (1983).

62. 786 F.2d 1410, 1415-16.

63. *See supra* note 7.

64. 786 F.2d 1410, 1415. *See supra* notes 41-2.

65. *Id.* The facts of *Benny* required only the part of the rule regarding a proprietorship with other employees. The court delineated that if the sole proprietor had no employees but operated under the corporate form, he too could be reached under § 1962(c). The court reasoned that the sole proprietor in that situation does receive some protection from the corporate form, and this is the "sort of legal shield for illegal activity that Congress intended RICO to pierce." *Id.* at 1416.

66. *Id.*

67. *Id. See supra* note 14. For a discussion of RICO penalties and their effects, see Woodbridge, *supra* note 9, at 520. *See also* K. BRICKEY, *supra* note 14, §§ 7:20-26.

68. *See* Tarlow, *supra* note 33, at 345-46.

show" operator to unjust culpability for a section 1962(c) offense.[69]

The court was justified in upholding the conviction of the defendant Benny. To hold otherwise would lead to results the drafters of the RICO statute never anticipated.[70] The head of a crime ring engaged in a pattern of racketeering activity would merely have to operate as a sole proprietorship to avoid prosecution under section 1962(c). In adopting the Seventh Circuit's rule regarding the sole proprietorship issue, the Ninth Circuit convincingly affirmed that holding and signaled the way for other courts to follow.

S.E.G.

69. *See supra* notes 53-4, 66 and accompanying text.

70. *See supra* notes 16-17 and accompanying text.