

UNITED STATES DISTRICT COURT
DISTRICT OF MAINE

S.D. WARREN COMPANY,)	
)	
	Plaintiff)
)
v.) Civ. No. 88-0327 P
)
WILLIAM ENGELMAN, et al.,)	
)
	Defendants)	

RECOMMENDED DECISION ON MOTION TO DISMISS

The plaintiff, S.D. Warren Company, brings this action against several individual and corporate defendants alleging that the defendants violated the Racketeer Influenced and Corrupt Organizations Act ("RICO"), 18 U.S.C. ' ' 1961-1968,¹ and also committed various state law torts.

¹RICO provides a private right of action for treble damages to "[a]ny person injured in his business or property by reason of a violation of [18 U.S.C.] section 1962." 18 U.S.C. ' 1964(c). Section 1962 of RICO provides in part:

- (a) It shall be unlawful for any person who has received any income derived, directly or indirectly, from a pattern of racketeering activity . . . to use or invest [such income in any enterprise that affects interstate or foreign commerce].
- (b) It shall be unlawful for any person through a pattern of racketeering activity . . . to acquire or maintain, directly or indirectly, any interest in or control of any enterprise [that affects interstate or foreign commerce].
- (c) 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 enterprise's affairs through a pattern of racketeering

The plaintiff claims that the defendants used the United States mail and interstate wires to engage in a kickback scheme in which the defendants Modern Research Corporation ("Modern") and ABC Chemical Corporation ("ABC") sold goods to the plaintiff at fraudulently inflated prices and/or quantities, resulting in losses to the plaintiff of over one million dollars. All of the defendants other than Jack Martin ("Engelman defendants") have moved to dismiss the complaint for failure to state a claim pursuant to Fed. R. Civ. P. 12(b)(6).²

The Engelman defendants argue that the plaintiff's allegations of the predicate acts of mail and wire fraud underlying its RICO claims, as well as its state law fraud allegations, are not sufficient to meet the requirements of Fed. R. Civ. P. 9(b). In addition, they argue that the complaint does not

-
- activity. . . .
- (d) It shall be unlawful for any person to conspire to violate any of the provisions of subsections (a), (b), or (c) of this section.

Racketeering activity is defined to include, inter alia, acts indictable under certain federal statutes prohibiting wire fraud and mail fraud. 18 U.S.C. ' 1961(1).

²The complaint was filed in the Eastern District of Pennsylvania. The Engelman defendants responded by filing with that court a motion to dismiss or to transfer the case. Judge Broderick ordered the case transferred to the District of Maine and denied the motion to dismiss without prejudice. The defendants have filed a new motion to dismiss in this court.

sufficiently allege a "pattern of racketeering activity" as required to sustain the plaintiff's civil RICO claims.

Rule 9(b)

Fed. R. Civ. P. 9(b) provides:

In all averments of fraud or mistake, the circumstances constituting fraud or mistake shall be stated with particularity.³ Malice, intent, knowledge, and other condition of mind of a person may be averred generally.

³Rule 9(b)'s particularity requirement serves three purposes: "(1) to place the defendants on notice and enable them to prepare meaningful responses; (2) to preclude the use of a groundless fraud claim as a pretext to discovering a wrong or as a 'strike suit'; and (3) to safeguard defendants from frivolous charges which might damage their reputations." New England Data Servs, Inc. v. Becher, 829 F.2d 286, 289 (1st Cir. 1987).

Rule 9(b) requires that plaintiffs asserting civil RICO claims based on mail and wire fraud "go beyond a showing of fraud and state the time, place and content of the alleged mail and wire communication perpetrating that fraud." New England Data Services, Inc. v. Becher, 829 F.2d 286, 291 (1st Cir. 1987). If this requirement is not satisfied, dismissal is not automatic; instead, in appropriate cases, such as where the allegations of the complaint suggest a likelihood that the defendants used interstate mail or telecommunications facilities but the specific information needed is likely in the exclusive control of the defendants, the court should determine whether to allow discovery and an opportunity to amend the complaint. Id. at 290. In this case, the allegations⁴ of the complaint inform as to the general nature of the fraudulent scheme by which the plaintiff was victimized. It covered a period of time commencing in or before the winter of 1985 and continuing through early 1987. It involved the use of interstate wire communication and/or the United States mail on at least two separate occasions. It included "kickbacks" to one of the plaintiff's employees and his wife in exchange for which that employee agreed to and did purchase on behalf of the plaintiff roofing supplies and materials at inflated prices and/or in unnecessary quantities. Complaint 22.

More specifically, the complaint details the manner in which the "kickbacks" were made. The defendant Jack Martin, on behalf of himself and the other defendants, made an agreement with one of the plaintiff's employees and the employee's wife to place the wife on the payroll of the defendant Lincoln Technical Service, Inc. ("Lincoln") which was owned, operated and controlled by the defendants Engelman, Chernow and Modern and which issued checks and paid monies to her

⁴In reviewing a 12(b)(6) motion to dismiss, the court is required to accept the truth of the well-pleaded allegations of the complaint. Miree v. DeKalb County, 433 U.S. 25, 27 n.2 (1977); Knight v. Mills, 836 F.2d 659, 664 (1st Cir. 1987).

through the United States mail even though she was not required to perform any services for that corporation or any of the other defendants. Complaint 18, 24.

While the complaint satisfies the "content" requirement of Becher, it falls short of providing the necessary specification as to "time" and "place." Designation of the time period as "commencing in or before the winter of 1985, and continuing through early 1987" is too vague and general to satisfy the salutary purposes underlying Rule 9B(b). See n.3, supra. This is especially true given the requirement that details regarding when and where the mails or wires were used be specifically pleaded in a RICO wire and mail fraud case. Becher, 829 F.2d at 290. The complaint contains no information whatever as to where the mails or wires were used or where other acts constituting key elements of the fraud took place.⁵

In deciding a motion to dismiss, a court generally considers only the allegations in the complaint; however, items appearing in the record of the case may be taken into account without transforming the motion into one for summary judgment. Mack v. South Bay Beer Distributors, Inc., 798 F.2d 1279, 1282 (9th Cir. 1986); Phillips v. Bureau of Prisons, 591 F.2d 966, 969 (D.C. Cir. 1979); C. Wright & A. Miller, 5 Federal Practice & Procedure ' 1357 (1969). The record in this case includes the Memorandum and Order of Judge Broderick of the Eastern District of

⁵The plaintiff's reliance on this court's decision in United Fish Co. v. Barr, 627 F. Supp. 732 (D. Me. 1986), is misplaced. United Fish was decided before the First Circuit Court of Appeals ruled in Becher as to how Rule 9(b) applies to RICO claims based on mail and wire fraud. Moreover, it is apparent from United Fish that the complaint there contained more specification as to time, place and content than does the one here.

Pennsylvania, dated October 28, 1988, see n.2, supra, which established that proper venue lies in the District of Maine. That decision was based on materials submitted by the parties, including the affidavit of David Hilt, a copy of which the Engelman defendants have attached to their memorandum in opposition to the motion to dismiss.

The Hilt affidavit contains factual statements which supply the "time" and "place" detail lacking in the complaint as well as augment the already sufficient "content" specification.⁶ As an item appearing in the record of the case, it is appropriate for the court to consider the affidavit to the extent it properly supplements the complaint. The affidavit is made on the basis of Hilt's oath that the facts contained therein are true and correct to the best of his knowledge, information and belief. It does not differentiate as to which statements are made on Hilt's personal knowledge and which are made on information and belief. Yet, a fair reading of the affidavit leads inescapably to the conclusion that all but a few of the factual statements are made on the basis of Hilt's personal

⁶The affidavit discloses that Hilt himself is the employee involved in the fraudulent scheme. In it, Hilt recites that he initiated contact with the defendants from Maine after having become aware of them through advertising he received in Maine; that the defendant Jack Martin (a/k/a Lieberman) represented himself to Hilt to be a salesman for the defendant Modern of various roofing supplies and other materials; that Martin called Hilt in Maine by telephone numerous times to discuss the fraudulent "kickback" scheme; that three of the interstate calls were placed by Martin to Hilt in Westbrook, Maine from Florida on January 30 and 31, 1985; that Martin flew to Portland, Maine on June 25, 1985 to meet with Hilt to finalize the arrangement to put Hilt's wife on the payroll of the defendant Lincoln, although she was not required to perform any services for Lincoln or any of the other defendants; that the arrangement was finalized in Maine by Martin and Hilt that day; that an application for employment with Lincoln was filled out in Hilt's wife's name in Maine; that Hilt's wife was placed on the books of Lincoln as an employee effective June 26, 1985; that from June 26, 1985 until sometime in early 1987 Hilt's wife received payroll checks in Maine from Lincoln bearing a Troy, Michigan address in the gross amount of ten per cent of the plaintiff's purchases from Modern; that four of those checks were dated July 3, 1985 and January 9, 16 and 23, 1987; that from June 26, 1985 through March 31, 1987 Lincoln paid Hilt's wife a total of \$117,227.18 all of which was received in Maine; and that Hilt's wife also received W-2 forms from Lincoln in Maine.

knowledge. There is doubt only as to those regarding the point of origin of the three specified telephone calls made on January 30 and 31, 1985 and the effective date of Hilt's wife's placement on the books of Lincoln as an employee. Because the law in this circuit is clear that "allegations based on 'information and belief' . . . do not satisfy the particularity requirement [of Rule 9(b)] unless the complaint sets forth the facts on which the belief is founded," Becher, 829 F.2d at 288 (citing Wayne Investment, Inc., 739 F.2d at 13-14), these two statements must be excluded from consideration. The exclusion, however, leaves no gaping hole; the affidavit otherwise contains an adequate specification of "time" and "place" regarding the key elements of the fraudulent scheme, including the use of the United States mail and interstate wire.

I conclude that the complaint and those portions of the Hilt affidavit which the court may properly consider together sufficiently plead the plaintiff's RICO wire and mail fraud and common law fraud claims to satisfy the purposes underlying Rule 9(b) and, therefore, the Rule itself.

Pattern Requirement

The defendants also claim that the plaintiff has failed to allege a pattern of racketeering activity as required for a RICO claim. RICO defines "pattern of racketeering activity" to include at least two acts of racketeering activity. 18 U.S.C. ' 1961(5). But "while two acts are necessary, they may not be sufficient" to satisfy the pattern requirement. Sedima, S.P.R.L. v. Imrex Co., 473 U.S. 479, 496 n.14 (1985). What is required is "more than one 'racketeering activity'" coupled with the "threat of continuing activity"; "[i]t is this factor of continuity plus relationship which combines to produce a pattern." Id., quoting S. Rep. No. 91-617, 91st Cong., 1st Sess. 158 (1969) (emphasis added by the Supreme Court). In other words, "[t]he constituent elements must be sufficiently

related to one another and threaten to be more than an isolated occurrence." Roeder v. Alpha Industries, Inc., 814 F.2d 22, 30 (1st Cir. 1987).

The First Circuit has decided that the existence of a pattern does not depend solely on whether or not the activity is characterized as a single scheme or episode. Id. at 31. The court explained that no one characteristic of a case is controlling, citing approvingly Morgan v. Bank of Waukegan, 804 F.2d 970, 975 (7th Cir. 1986). Roeder, 814 F.2d at 31. Morgan lists several factors deemed relevant to a determination of whether a pattern exists: "the number and variety of predicate acts and the length of time over which they were committed, the number of victims, the presence of separate schemes and the occurrence of distinct injuries." 804 F.2d at 975.

In this case, in addition to the allegations of the "kickback" scheme of which it is the victim, the plaintiff claims, upon information and belief, that the defendants have participated in similar mail and wire schemes to defraud other purchasers of roofing supplies and materials from Modern and ABC. Complaint 23. Without these allegations of additional instances of fraud involving other customers, the complaint cannot be read to allege a pattern of racketeering activity. Although carried out with more than one payment and more than one purchase over approximately two years, the "kickback" scheme which defrauded the plaintiff constituted a single racketeering activity, involved the bribing of one employee and resulted in one injury to one victim.⁷ A single instance of

⁷The plaintiff attempts to bolster its claim of a pattern of racketeering activity by alleging that the Internal Revenue Service was an additional victim of the fraudulent scheme because the kickback payments were improperly reported as a business expense on Lincoln's tax returns. This alleged fact,

bribery does not constitute a pattern even if the bribe was paid in a number of installments. See
Roeder, 814 F.2d at 31.

however, does not deserve significant weight in determining whether improper actions have sufficient continuity and relationship to form a pattern, since illegal tax reporting is frequently a consequence of isolated fraudulent acts.

The critical question, therefore, is whether the court can consider the allegations contained in paragraph 23 of the complaint. The Engelman defendants argue that the paragraph 23 allegations cannot be accepted as true for purposes of this motion to dismiss because "allegations based on 'information and belief' . . . do not satisfy the particularity requirement unless the complaint sets forth the facts on which the belief is founded." Becher, 829 F.2d at 288, (citing Wayne Investment, Inc., 739 F.2d at 13-14). It is clear that all of the purposes of Rule 9(b) would not be served if allegations of the time, place and content of the predicate acts of mail and wire fraud in a RICO action could be made solely on the basis of information and belief. Nonetheless, Rule 9(b) does not require that a pattern of racketeering activity be alleged with particularity. See C. Wright & A. Miller, 5 Federal Practice & Procedure ' 1297 at 403 (1969) (Rule 9(b) applies to circumstances of fraud, not elements of fraud claim); Hayduk v. Lanna, 775 F.2d 441, 443 (1st Cir. 1985) (Rule 9(b) requires that the circumstances of the fraud must be stated with particularity; in diversity cases, state law governs question whether elements of fraud are sufficiently pled). Because Rule 9(b) is not implicated in the "pattern" issue, allegations made on information and belief to establish the existence of a pattern may be considered.⁸ See 5 C. Wright & A. Miller, Federal Practice & Procedure ' 1224 at 157 (1969).

⁸It is worth noting that such allegations are subject to the strictures of Fed. R. Civ. P. 11 which should provide sufficient protection against totally groundless claims of a pattern of racketeering activity.

I conclude that the paragraph 23 allegations that the defendants have engaged in similar fraudulent schemes with other customers should be considered and that the complaint read as a whole sufficiently alleges a pattern of racketeering activity.⁹

For the foregoing reasons, I recommend that the Engelman defendants' motion to dismiss be DENIED.

NOTICE

A party may file objections to those specified portions of a magistrate's report or proposed findings or recommended decisions entered pursuant to 28 U.S.C. ' 636(b)(1)(B) for which de novo review by the district court is sought, together with a supporting memorandum, within ten (10) days after being served with a copy thereof. A responsive memorandum shall be filed within ten (10) days after the filing of the objection.

Failure to file a timely objection shall constitute a waiver of the right to de novo review by the district court and to appeal the district court's order.

DATED at Portland, Maine, this 29th day of March, 1989.

⁹While no motion to amend has been filed, the plaintiff argues that it could amend the complaint to supply more details of the "kickbacks" made to agents of other customers; for example, it would allege that a toaster oven was sent to the home of a NASA employee, money was sent to an employee of U.S.D.A. and money sent to someone at San Jose Catholic Church. Memorandum of Law in Support of Plaintiff S.D. Warren Company's Objection to the Motion to Dismiss the Complaint of all Defendants other than Jack Martin p.17 & n.10. Even if the allegations of additional schemes were deemed to be insufficient, given that the complaint together with the Hilt affidavit present strong claims that are likely not frivolous, the plaintiff should be granted leave to amend its complaint to allege additional schemes with particularity.

David M. Cohen
United States Magistrate