

RICO Report* — RICO and Foreign Arbitration Enforcement*HOST: CAL STEIN****GUEST: ARMEEN SHROFF****RECORDED: 7/25/23****Cal Stein:**

Hello and welcome back for this installment of the *RICO Report*. Today is an exciting episode because we are going to be talking about a recent Supreme Court opinion involving the RICO statute, specifically a way to use the RICO statute to enforce and collect on a foreign arbitration award. The Supreme Court, of course, has weighed in on the RICO statute countless times before and we have discussed many of those opinions here on the *RICO Report*, but this one is unique and as I said, somewhat exciting because it just happened. So today, we are going to discuss the Supreme Court case, the facts and the procedural posture.

And of course, the decision itself and also going to analyze its likely impact on future RICO cases, but before we do that, let's do some quick introductions. As you know, my name is Cal Stein and I'm a partner in the white collar and litigation practice groups at Troutman Pepper. I represent clients in white collar criminal and government investigation matters, and in complex civil lawsuits, particularly RICO litigation. I am joined here today with one of my colleagues, Armeen Shroff. I will, of course, let Armeen introduce herself, but I would be remiss if I did not mention that Armeen and I recently completed an international arbitration together, which included a RICO claim. As we'll see today, that experience is actually quite fitting giving the subject matter of the Supreme Court decision we will be discussing. With that intro, Armeen, why don't you introduce yourself?

Armeen Shroff:

Thanks so much, Cal, and I appreciate you having me on the show. As Cal said, my name is Armeen Shroff. I'm an associate in the firm's business litigation group. I split my practice pretty evenly between general commercial litigation and recently, I've been pivoting more towards international dispute resolution, and like Cal said, we recently tried a case that involved some RICO issues and that was fascinating in more ways than one.

Cal Stein:

Yeah. That was a real fun case we did together, Armeen. I'm glad you're not sick of me just yet.

Armeen Shroff:

Not quite yet.

Cal Stein:

I'm glad to hear it. Okay. So let's get into the meat of our episode here today, and as I said, we're going to be talking about a recent Supreme Court decision that presented the following question, can an individual litigant use the RICO statute to enforce a foreign arbitration award that he had previously obtained? The question seems straightforward enough, but the case proposed a unique way for a litigant to use the RICO statute.

And in doing so, the case implicated a specific element of RICO, that of the domestic injury, and we're going to talk about this domestic injury requirement in some detail, but briefly, it is a component of standing under RICO that requires a plaintiff to be able to show that he or she suffered a domestic injury, i.e. one in the United States. Let's talk about the case in question, and Armeen, you have been the one who has really been following this closely. Why don't you start us off by telling us about the facts of this Supreme Court case?

Armeen Shroff:

This is an interesting case. We're dealing with two consolidated appeals that came up to the US Supreme Court from the Ninth Circuit and the premise of these appeals was enforcement of an \$84 million arbitration award from the London Court of International Arbitration, which is a large, very well known international arbitration tribunal. Back in 2014 in December, a California federal court had confirmed this award from the London Court of International Arbitration and entered judgment against an individual named Ashot Yegiazaryan for \$92 million.

So that's basically the award of 84 million plus interest. The court also issued a temporary protective order freezing Yegiazaryan's assets in California. As a lot of these cases sometimes go, after Yegiazaryan continued refusing to pay the award, the claimant, essentially the individual who had won the arbitral award before the LCIA, a man named Mr. Vitaly Ivanovich Smagin, filed a civil RICO action, and what he alleged was that Yegiazaryan and the other defendants had conducted a RICO enterprise to prevent Smagin from enforcing his arbitral award.

And this is where it gets kind of interesting. In addition to the amount of its LCIA arbitral award, he also sought all of his attorney's fees and treble damages as is authorized under RICO. When Smagin appeared before the Central District of California, the district court dismissed his complaint for lack of domestic injury and in deciding that, the district court found it, and I quote this, "most significant" that Smagin is a resident and a citizen of Russia and thus could not be the subject of a domestic injury.

Cal Stein:

Thanks, Armeen. It's important to have a handle on the facts of this case to put everything into context and there are a lot of moving pieces here, but let's switch gears now from the facts to talk about the law, and let's start with the domestic injury requirement, which as Armeen just mentioned, was central to this case, and to understand the domestic injury requirement, we need a little bit of a RICO history lesson here, so we're going to try to go through that right now. As listeners of the *RICO Report* will know, RICO is somewhat notorious for its numerous elements and therefore, it's rigorous pleading standards.

But even beyond the elements that we have talked about on this show, there is an additional step for individual plaintiffs who are not US residents or who are not corporate plaintiffs that have their principle place of business in the United States. For these types of, we'll call them foreign RICO plaintiffs. In order to establish standing under RICO, that foreign plaintiff must demonstrate that it suffered a domestic injury and that is a domestic injury to its business or property. Again, one that was suffered in the United States and not abroad. Now, about that history lesson I mentioned a moment ago, the Supreme Court first addressed this domestic injury requirement in the RJR Nabisco case.

This was not all that long ago, only back in 2016. In that case, foreign plaintiffs filed a RICO suit against the tobacco company RJR Nabisco alleging predicate acts of international money

laundering. The Supreme Court established that for foreign plaintiffs asserting a RICO claim, there is a presumption against extraterritoriality and that presumption requires a plaintiff to prove a domestic injury in support of its standing to bring the RICO action in the United States. The court found that RICO is not limited solely to domestic schemes, but it remains that "not every foreign enterprise will qualify under the RICO statute."

And just like that, the domestic injury requirement was born. Like I said, the RJR case was not that long ago, only 2016, which means this domestic injury requirement has not been a real key component of RICO jurisprudence for all that many years, but that is not to say it has not been the subject of a fair bit of scrutiny. It absolutely has with multiple circuit courts picking up on the RJR decision and offering their own spins on the domestic injury requirement. Armeen, proceeding with our brief history lesson here, the first Circuit Court to weigh in on the domestic injury requirement after the RJR case was the Second Circuit. Can you tell us a bit about that case?

Armeen Shroff:

Yeah, absolutely. A year later in 2017, the Second Circuit addressed this domestic injury issue in a case called *Bascunan v. Elsaca*, and in that case, the plaintiff was a resident of Chile and that plaintiff alleged RICO claim based on allegations that his cousin stole millions of dollars from his US bank account. The district court concluded that there was no domestic injury because the plaintiff, who was a resident of Chile, suffered economic damages that he only felt in his place of residence, which was not the United States. On appeal, however, the second court reversed his decision and held that where injury is to tangible property.

So in this case, if we're dealing with money in a US bank account, absent some extraordinary circumstance, the injury is domestic if the plaintiff's property was located in the United States when it was stolen or harmed. So even if the plaintiff himself resides abroad, like in this case with the plaintiff residing in Chile, the injury happened to a bank account that was located in the United States and because there was a domestic injury to tangible property, the US bank account, the Second Circuit's decision allowed the plaintiff in *Bascunan* to have his RICO claim.

I think this is relatively straightforward when it comes to something like a literal US bank account that's sitting in the United States, but unfortunately, neither *Bascunan* nor the RJR Nabisco case that you mentioned, Cal, really dealt with how to deal with this presumption against extraterritoriality when we're applying it to intangible property and bringing it back to what the Supreme Court recently decided, an example of intangible property would be a foreign arbitral award. So the question becomes where is that foreign arbitral award located?

Cal Stein:

Thanks, Armeen. So the Second Circuit weighed in on this domestic injury requirement in 2017. Proceeding forward the very next year, the Seventh Circuit decides to weigh in in a case called *Armada PTE Limited v. Amcol International Corp*, and in that case, the Seventh Circuit affirmed a district court judgment that recognized a foreign arbitration award as "intangible property." Per the decision in this Armada case, the location of an injury to the intangible property had to be the foreign claimant's home abroad, i.e. outside of the United States. So the plaintiff in *Armada*, which was a Singaporean shipping company, was awarded more than \$70 million in two awards in ad hoc arbitrations out of London.

The Southern District of New York recognized those awards and entered a judgment, and the plaintiff sought to enforce those judgments by filing maritime attachment proceedings. Those

efforts, of course, were unsuccessful. So the plaintiff filed a RICO action alleging that it suffered an injury to its property, i.e. its recognized judgment, and that the defendants by means of racketeering activity injured that property by divesting their assets, thereby making the judgment and other claims against the defendants uncollectible.

The Seventh Circuit held that the foreign plaintiff's "principal place of business was Singapore," so any harm to the plaintiff's intangible bundle of litigation rights was suffered in Singapore. Therefore, the court found there was no domestic injury to the plaintiff's intangible property and the plaintiff failed to plead a plausible claim under civil RICO. This was an interesting decision, but it wasn't the only RICO domestic injury case in the year 2018. Armeen, the next circuit court to step up to the plate and address domestic injury was the Third Circuit also in 2018. Tell us about that one.

Armeen Shroff:

Absolutely. So we're moving over to Third Circuit now. This was after the *Armada* case from the Seventh Circuit, but later that year, and we're dealing with a case now called *Humphrey v. GlaxoSmithkline*. The plaintiffs in *Humphrey* were American co-founders of investigation firm based in China, and the issue in this case was that there was a Chinese regulatory investigation that, unfortunately for these plaintiffs, resulted in the arrest, conviction, and deportation of the plaintiffs back to the United States. Once they were back home, the plaintiffs sued for civil RICO, alleging that their business was destroyed and their prospective business ventures were also destroyed.

The district court found there wasn't a domestic injury because the plaintiff's business was in China, their offices were in China, there was no work done outside of China, and the plaintiffs resided in China when this injury happened. Therefore, according to the district court, any destruction of plaintiff's business occurred while the plaintiffs were imprisoned in China by Chinese authorities. On appeal, the Third Circuit affirmed this decision. In doing so though, it rejected the residency based rule that Cal just told us about in *Armada*, and they opted instead for a multi-factor test to determine when injury to intangible property is a domestic injury. So for the Third Circuit, the focus was primarily upon where the effects of the predicate acts were experienced.

The *Humphrey* court didn't have a bright line rule, but they basically said there are several factors that are relevant for a court to consider in deciding whether there was a domestic injury. We're talking about things like where the injury arose, the plaintiff's residence or principal place of business, where any alleged services were provided, where the plaintiffs received or expected to receive benefits of those services, where any business agreements were entered into, the laws binding those agreements, and the location of the activities in the underlying dispute, and applying all of these factors, the Third Circuit concluded that there was no domestic injury because the alleged harm to the plaintiff's business occurred mainly abroad.

Cal Stein:

Thanks, Armeen. So that all brings us to the present and really ends our history lesson about the domestic injury requirement. Of course, all of those cases follow what has become a familiar pattern with jurisprudence and really much, much other jurisprudence as well. The Supreme Court issues a decision, various circuit courts then take it and come up with different standards, sometimes conflicting standards, and then when it's all a big mess, the Supreme Court steps back in and says which one it likes the best.

And in a way, all of the cases we just mentioned set the stage for the Supreme Court's June 22nd, 2023 decision in the Yegiazaryan and CMB Monaco cases that we're here today to talk about. So let's talk about that decision, which of course, was the consolidated decision for both of them, and the case reached the Supreme Court from the Ninth Circuit. So Armeen, before we get into what the Supreme Court said, why don't you tell us a little bit about the procedural posture of the case? What was the Ninth Circuit decision that the Supreme Court ended up reviewing?

Armeen Shroff:

Absolutely. From the beginning of the podcast, we talked briefly about the facts of this case. So we had a Russian resident who was attempting to enforce his London Arbitral Award in the United States, and he had a judgment from a California federal court to enforce that award. The Ninth Circuit adopted what they called a context specific approach to deciding whether there was a domestic injury and applying that approach, the Ninth Circuit concluded that Smagin, who was the plaintiff here, had pleaded a domestic injury and their reasoning was this.

Smagin was trying to execute on a California judgment in the state of California against a California residence, and what he alleged was that his efforts to collect on that judgment were foiled by a pattern of racketeering activity that occurred in and was targeted at California and also was designed to subvert the enforcement of that judgment in California. So taking these facts together, the Ninth Circuit concluded there was a domestic injury and that Smagin's.

And I quote now, "central allegation is that those predicate acts injured his right to seek property in California from a California resident under the California judgment." So what the Ninth Circuit did was rejected the Seventh Circuit's rule from *Armada*, that bright line residency rule, and they've embraced the Third Circuit's factor based approach in the Humphrey case. In concluding, the Ninth Circuit held that whether a plaintiff has alleged a domestic injury is a context specific inquiry that turns largely on the particular facts alleged in a complaint.

Cal Stein:

Great. Thanks, Armeen. Okay. So now let's talk about what the Supreme Court actually said here, and let's go back to January. On January 13th, 2023, the Supreme Court granted the petitions for cert and consolidated the cases, and then on April 25th, we had oral argument on it, and this is really important because there was a lot of things that were said during oral argument by the justices that gave a window into what they were thinking. Chief Justice Roberts and Justice Sotomayor during the argument seemed to favor affirming the Ninth Circuit's decision with Chief Justice Roberts noting.

And I'm quoting here, "the plaintiff obtained a California judgment to collect California property against someone living in California based on conduct in California, right? Why can't we consider with all those connection, that a domestic injury?" Fairly straightforward line of reasoning from the Chief Justice. For her part, Justice Kagan seemed uncomfortable with how this foreign dispute came before the Supreme Court, and I'm going to quote her as well. "It is a little bit odd, yes, there's a California judgment and alleged acts taken to avoid the judgment, but all of that is derivative on a dispute that was fundamentally foreign in nature between foreign parties involving foreign conduct initially adjudicated in another foreign country.

So the fact that this has migrated, if you will, to the United States comes about only with respect to enforcing the first judgment." Again, a pretty linear, straightforward line of thinking here. You can see why there was disagreement. In the end, however, the justices affirmed the Ninth

Circuit and permitted Smagin to pursue his RICO claim to try to enforce his \$92 million foreign arbitration judgment. Justice Sotomayor authored the majority opinion from the court, which was issued on June 22nd. The court ultimately held that Smagin's allegations showed that he alleged racketeering activity that occurred in or was targeted at California.

Thereby creating a domestic injury sufficient to establish RICO standing even for a foreign plaintiff. In doing so, the court rejected the bright line residency rule from *Armada* that we talked about a little bit earlier. Instead, opting to follow the Ninth Circuit's context specific inquiry. The majority opinion reasoned, "depending on the allegations what is relevant in one case to assessing whether the injury arose may not be pertinent in another. While a bright line rule would no doubt be easier to apply, fealty to the statute's focus requires a more nuanced approach."

The court emphasized the facts surrounding the California judgment and Yegiazaryan's "domestic actions taken to avoid enforcement." The rights that the California judgment provide to Smagin exist only in California and the court noted the alleged RICO scheme thwarted those rights, thereby undercutting the orders of the California district courts and Smagin's efforts to collect Yegiazaryan's assets in California. Looking to what the court viewed as the relevant factors, the Supreme Court ultimately concluded there was a domestic injury. Now of course, to the surprise of absolutely no one given the makeup of the court these days, the decision in this case was not unanimous. In fact, three justices dissented. I actually found the dissents to be fascinating. Armeen, can you tell us a little bit about the dissents?

Armeen Shroff:

Yeah, they were fascinating. I think in some ways, Cal, the dissent was perhaps a slightly spicier read than the majority opinion. We have Justice Alito who was joined fully in his dissent by Justice Thomas and partly by Justice Gorsuch, three justices dissenting in total, and their concern was that this context specific inquiry really doesn't give a lot of help to future courts who might be grappling with this issue. I thought this was an interesting quote. In the dissent opinion, it states, "of course, under the majority's all factors considered approach, many other features of this very suit could be relevant."

So according to the dissent, it was unclear from the majority's opinion which factors are relevant and in what context. There was also another, what I thought was an interesting concern from the dissenting justices about overreach. They noted that this decision gives foreign plaintiffs with arbitral awards arguably a lot of power, and here's another quote, "a thrust of our international comedy jurisprudence is that we should not lightly give foreign plaintiffs access to US remedial schemes that are far more generous than those available in their home nations. We know RICO is an unusually plaintiff friendly remedy." So that concern, according to the dissent, applies in spades here.

Cal Stein:

Yeah. Thanks, Armeen. I note the irony a little bit of the dissents worrying about the Supreme Court's decision not offering much help to future courts and grappling with the issue. Someone more cynical than I might point out that that has been a staple of Supreme Court jurisprudence, particularly in the RICO context in the past, but I don't think we'll go there right now. Okay. So we've covered a lot. We've really discussed this case in detail from the procedural posture to the majority opinion to the dissents, but let's now focus on the practical. What does this decision really mean going forward for litigants and what are the key takeaways, and let me start with the first one that at least I believe.

My first key takeaway has to do with foreign arbitral awards being property. The Supreme Court has recognized for the first time that a United States judgment confirming a foreign arbitration award is property within the meaning of RICO. Therefore, a plaintiff who can allege an injury to that foreign arbitral award can satisfy the damages requirement of the RICO statute, i.e. injury to one's business or property. This holding gives claimants who are successful in international arbitration proceedings a powerful new weapon to enforce those awards against reluctant defendants with US-based assets. That is, of course, one of the things the dissenting justices were concerned about, but the majority opinion does provide that opportunity. That was one key takeaway, at least to my eyes. Armeen, what's another one?

Armeen Shroff:

The Supreme Court's given Smagin the green light, right? He said, you can go ahead with your RICO claim, and that's basically opened this path for Smagin to recover attorney's fees and trouble damages so he can significantly increase the value of his arbitration victory, and as we've seen in other areas, plaintiffs are often very eager to use RICO whenever possible to take advantage of these provisions. So I wouldn't be surprised at all to see other plaintiffs try and emulate Smagin's success. We might suddenly see an uptick of lawsuits in US courts where we see foreign arbitral award enforcement under the cover of civil RICO.

Cal Stein:

Yeah, that's a really good point, Armeen, and that actually leads to, I think, the third key takeaway, which has to do with the application of this decision going forward by lower courts. Given the context specific approach that the Supreme Court endorsed here, it really would not be surprising at all to see other federal courts try to place limitations and/or guardrails on the application of this decision. Courts will still require foreign plaintiffs to meet the rigorous civil RICO standards, including established predicate criminal offenses and the connection to an enterprise depending on which subsection of the RICO statute the claim is brought under.

And while the threat alone of treble damages and attorney's fees may motivate debtors to pay up when they otherwise might be reluctant to do so, the context specific analysis in the Supreme Court's opinion does leave those potential defendants some escape hatches that a bright line rule, had it been endorsed, likely would not have, and Armeen, practically speaking, these hypothetical restrictions and guardrails that we're speculating other federal courts might seek to impose are consistent with exactly the concerns the dissenting justices expressed, right?

Armeen Shroff:

Yeah, they absolutely are. Smagin might have gotten his blessing. He's able to pursue his private RICO action, but remember that the defendant in this particular case that was before the Supreme Court is a California resident with assets in California. That context-based analysis that the Supreme Court talked about changes considerably if the defendant, for example, does not reside in California or did not even have assets in California. If these circumstances are changed even slightly, I think that may prove to be enough for other federal courts to distinguish such a case and not be bound by this Supreme Court precedent.

Cal Stein:

Yeah, I completely agree. Really, really fascinating stuff, and it's, of course, too early to really tell the true practical impact of the Supreme Court's decision, but regardless, beyond the question of enforcing foreign arbitration awards against US-based assets, this decision will be of interest to everyone who is seeking clarity on when and under what circumstances non-US plaintiffs may invoke RICO and its, as you noted, Armeen, plaintiff friendly remedies, and with that, we are out of time here today.

So I want to bring this discussion to a conclusion. I really want to thank you, Armeen, for joining me here today to discuss this very interesting and very new Supreme Court RICO case, and I also want to thank everyone for listening. If you have any thoughts or any comments about this series or today's episode on the Supreme Court decision, I invite you to contact me directly at calen.stein@troutman.com. You can subscribe and listen to other Troutman Pepper podcasts wherever you listen to podcasts, including on Apple, Google, and Spotify. Thank you for listening and stay safe.

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