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Second Circuit Decision Potentially Broadens RICO Proximate Cause Element

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The Second Circuit Court of Appeals recently issued an opinion that potentially broadens the proximate cause element of claims brought under the Racketeer Influenced and Corrupt Organizations Act (RICO). RICO's proximate cause element requires a plaintiff to allege facts plausibly establishing that there is a "direct relationship" between the claimed injury and the defendant's conduct in violation of RICO. By suggesting a possibly more expansive interpretation of this element, the Second Circuit may have made it easier for future plaintiffs to bring and plead civil RICO claims, particularly against their business competitors.

The case, *Alix v. Mckinsey & Co.,* involved a claim by Alix Partners against McKinsey & Co., Alix's dominant competitor in the high-end corporate bankruptcy advising market (bankruptcy cases involving assets over $ 1 billion). McKinsey is the dominant player in the market, but Alix historically received 24% of the engagements not assigned to McKinsey. In the lawsuit, Alix alleged that McKinsey violated RICO and improperly received bankruptcy engagements by (1) submitting false applications to the U.S. Bankruptcy Court that omitted conflicts of interest that should have led to McKinsey's disqualification, and (2) engaging in a "pay-to-play" scheme in which McKinsey introduced its clients to bankruptcy attorneys in exchange for lucrative referrals of bankruptcy assignments from the attorneys. Alix claimed that these illegal activities by McKinsey deprived it of bankruptcy court engagements that it otherwise would have obtained absent McKinsey's misconduct.

The district court granted McKinsey's motion to dismiss, finding that Alix failed to plead the proximate cause element of RICO. The court held that there were independent intervening decisions of the U.S. Bankruptcy Trustee and the Bankruptcy Court regarding the retention of consultants that rendered the causal connection between McKinsey's actions and Alix's failure to win more bankruptcy assignments "too remote, contingent and indirect" to sustain a RICO claim. In other words, the court found that the direct cause of Alix's injury arose from independent decisions of the various debtors' trustees not to hire Alix, rather than McKinsey's alleged misconduct of improperly securing engagements for itself.

The Second Circuit reversed and remanded the matter. While it acknowledged that the district court had rendered a "careful opinion navigating a body of case law that, charitably speaking, is less than pellucid," the Second Circuit criticized the district court's decision because the conduct alleged in Alix's complaint directly undermined the integrity of the federal courts: "[W]e believe the district court gave insufficient consideration to the fact that McKinsey's alleged misconduct targets the federal judiciary. As a consequence, this case requires us to focus on the responsibilities that Article III courts must shoulder to ensure the integrity of the Bankruptcy Court and its processes." With this background, the Second Circuit opted for a more flexible application of the proximate causation requirement.

For example, the court distinguished significant U.S. Supreme Court precedent on RICO causation — *Anza v. Ideal Steel Supply Corp*.[1] — stating "Anza would … be more like this case if the defendants had allegedly defrauded one of the courts we oversee." The court disregarded other precedents because "none of these prior cases involved allegations of fraud on a court whose operations we oversee." And more generally, the court bridged the causation gap by finding that "fraud on the Bankruptcy Court committed in the manner alleged by Alix causes direct harm to litigants who are entitled to a level playing field and calls into play our unique supervisory responsibilities."

One of the more curious aspects of the court's opinion was the determination that causation was satisfied because Alix was "better situated" to redress the alleged misconduct than either the U.S. Trustee or the Bankruptcy Court itself, despite that courts' inherent power to investigate and remedy fraud on the tribunal. The Second Circuit's rationale — that neither the U.S. Trustee nor the Bankruptcy Court (or, for that matter, the U.S. attorney) would be in a superior position to find out what McKinsey did and impose a remedy — was simply stated as an *ipse dixit*, without referring to any precedents or data to support it.

It is clear that the Second Circuit's interpretation of RICO causation in this decision is more expansive than that applied by other courts. And it remains to be seen what impact this decision has on the overall RICO jurisprudence in the Second Circuit and elsewhere. Nonetheless, there are several key takeaways from this case of which businesses and RICO practitioners should be aware.

1. The scope of this decision may not be as narrow as the court projects.

There is no question that the Second Circuit believed this particular RICO case deserved special attention because it implicated potential fraud on a court, even going as far to say that its decision was *sui generis* and of "little, if any, application to 'ordinary' RICO cases where these [supervisory] responsibilities are not front and center." However, the court did not use its customary tools for limiting the precedential value of a decision — *e.g.,* marking it "not for publication," or issuing a summary order or *explicitly* limiting its disposition to the peculiar facts of the case. As a result, it would not be surprising to see future plaintiffs offer similar theories of causation in reliance on this decision. The court's heavy focus on the potential fraud on the court also may serve as a separate avenue to encourage RICO suits by creative plaintiffs who can plausibly connect alleged fraudulent activity to the judicial system or, by analogy, to other public or governmental entities.

2. The decision opens the door for plaintiffs to allege causation based on market share.

In asserting proximate causation, Alix relied heavily (if not exclusively) on an analysis of its historical share of the high-end corporate bankruptcy market, namely, its claim that is received 24% of the engagements that did not go to McKinsey. The Second Circuit explicitly overruled the district court's dismissal of this argument, noting that "it is also a reasonable inference that … [Bankruptcy Courts] would likely have awarded assignments to eligible firms in approximately the same ratio they had been using in the past." Put simply, the court agreed with Alix that causation was sufficiently alleged because if McKinsey had not defrauded the Bankruptcy Court, those improperly awarded engagements would have been awarded to other firms in the same proportion to their historical market share. This type of causation analysis will likely encourage businesses to bring RICO claims against competitors for stealing business through allegedly fraudulent conduct by lending credence to the use of historical market share data to satisfy causation, at least at the pleading stage.

3. RICO's proximate cause element remains flexible enough to encourage more RICO suits.

Even if other courts limit the application of this decision to RICO cases that allege fraud on the court (as discussed above), if nothing else, the Second Circuit's opinion underscores the flexible nature of proximate cause in a RICO case, and it encourages a case-specific analysis of even the most creative causation arguments. This concept, which is baked into RICO jurisprudence, was clearly a driver of the Second Circuit's decision: "As the Supreme Court explained, proximate cause is a 'flexible concept' that is 'generally not amenable to bright-line rules.'" The more flexible an approach courts are willing to take in assessing proximate causation, the more likely RICO plaintiffs are to assert novel claims and unique causation theories (as Alix did here), and the more likely RICO attorneys will take on such cases, particularly where the plaintiff is a business that can point to significant lost revenue. While such cases may have previously been susceptible to motions to dismiss, the effectiveness of those arguments will wane if more courts adopt either the Second Circuit's holding in *Alix* or even its deference to the "flexibility" of proximate causation.

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[1] 547 U.S. 451, 126 S.Ct. 1001, 164 L.Ed.2d 720 (2006). In *Anza*, the plaintiff alleged it lost sales because its competitor failed to pay sales taxes and could sell product at lower prices. The court held that causation was not pleaded because there were many possible reasons for lowering prices that would be intervening events.

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