SUPREME COURT OF THE UNITED STATES

No. 91–886

BOB REVES, ET AL., PETITIONERS *v.* ERNST & YOUNG

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

[March 3, 1993]

JUSTICE SOUTER, with whom JUSTICE WHITE joins, dissenting.

In the word "conduct," the Court today finds a clear congressional mandate to limit RICO liability under 18 U. S. C. §1962(c) to participants in the "operation or management" of a RICO enterprise. *Ante*, at 6–9. What strikes the Court as clear, however, looks at the very least hazy to me, and I accordingly find the statute's "liberal construction" provision not irrelevant, but dispositive. But even if I were to assume, with the majority, that the word "conduct" clearly imports some degree of direction or control into §1962(c), I would have to say that the majority misapplies its own "operation or management" test to the facts presented here. I therefore respectfully dissent.

The word "conduct" occurs twice in §1962(c), first as a verb, then as a noun.

> "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 activity or collection of unlawful debt." 18 U. S. C. §1962(c).

Although the Court is surely correct that the cognates should receive consistent readings, see *ante*, at 7, and correct again that "context is important" in coming to understand the sense of the terms

intended by Congress, *ibid.*, the majority goes astray in quoting only the verb form of "conduct" in its statement of the context for divining a meaning that must fit the noun usage as well. Thus, the majority reaches its pivotal conclusion that "in the context of the phrase `to conduct . . . [an] enterprise's affairs,' the word indicates some degree of direction." *Ibid.* (footnote omitted). To be sure, if the statutory setting is so abbreviated as to limit consideration to the word as a verb, it is plausible to find in it a suggestion of control, as in the phrase "to conduct an orchestra." (Even so, the suggestion is less than emphatic, since even when "conduct" is used as a verb, "[t]he notion of direction or leadership is often obscured or lost; e.g. an investigation is *conducted* by all those who take part in it." 3 Oxford English Dictionary 691 (2d ed. 1989) (emphasis in original).)

In any event, the context is not so limited, and several features of the full subsection at issue support a more inclusive construction of "conduct." The term, when used as a noun, is defined by the majority's chosen dictionary as, for example, "carrying forward" or "carrying out," Webster's Third New International Dictionary 473 (1976), phrases without any implication of direction or control. The suggestion of control is diminished further by the fact that §1962(c) covers not just those "employed by" an enterprise, but those merely "associated with" it, as well. And associates (like employees) are prohibited not merely from conducting the affairs of an enterprise through a pattern of racketeering, not merely from participating directly in such unlawful conduct, but even from indirect participation in the conduct of an enterprise's affairs in such a manner. The very breadth of this prohibition renders the majority's reading of "conduct" rather awkward, for it is hard to imagine how the "operation or management" test would leave the statute with the capacity to reach the indirect participation of someone merely associated with an enterprise. I think, then, that this contextual examination shows

"conduct" to have a long arm, unlimited by any requirement to prove that the activity includes an element of direction. But at the very least, the full context is enough to defeat the majority's conviction that the more restrictive interpretation of the word "conduct" is clearly the one intended.[1]

What, then, if we call it a tie on the contextual analysis? The answer is that Congress has given courts faced with uncertain meaning a clear tie-breaker in RICO's "liberal construction" clause, which directs that the "provisions of this title shall be liberally construed to effectuate its remedial purposes." Pub. L. 91–452, §904(a), 84 Stat. 947, note following 18 U. S. C. §1961. We have relied before on this "express admonition" to read RICO provisions broadly, see *Sedima, S. P. R. L.* v. *Imrex Co.*, 473 U. S. 479, 497–498 (1985), and in this instance, the "liberal construction" clause plays its intended part, directing us to recognize the more

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[1]The Court attempts to shore up its interpretation with an examination of relevant legislative materials. See *ante*, at 9–13. The legislative history demonstrates only that when members of Congress needed a shorthand method of referring to §1962(c), they spoke of prohibiting "the operation" of an enterprise through a pattern of racketeering activity. As Arthur Young points out, "operation" is essentially interchangeable with "conduct"; each term can include a sense of direction, but each is also definable as "carrying on" or "carrying out." Brief for Respondent 22. There is no indication that the congressional shorthand was meant to attend to the statutory nuance at issue here. As the Court concedes, "[T]he fact that members of Congress understood §1962(c) to prohibit the operation or management of an enterprise through a pattern of racketeering activity does not necessarily mean that they understood §1962(c) to be limited to the operation or management of an enterprise." *Ante*, at 12.

inclusive definition of the word “conduct,” free of any restricting element of direction or control.[2] Because the Court of Appeals employed a narrower reading, I would reverse.

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[2]The majority claims that without an element of direction, the word ``conduct,'' when it appears as a noun, becomes superfluous. *Ante*, at 8. Given the redundant language Congress has chosen for §1962(c), however, any consistent reading of ``conduct'' will tend to make one of its two appearances superfluous.

Even if I were to adopt the majority's view of §1962(c), however, I still could not join the judgment, which seems to me unsupportable under the very "operation or management" test the Court announces. If Arthur Young had confined itself in this case to the role traditionally performed by an outside auditor, I could agree with the majority that Arthur Young took no part in the management or operation of the Co-op. But the record on summary judgment, viewed most favorably to Reves,[3] shows that Arthur Young created the very financial statements it was hired, and purported, to audit. Most importantly, Reves adduced evidence that Arthur Young took on management responsibilities by deciding, in the first instance, what value to assign to the Co-op's most important fixed asset, the White Flame gasohol plant, and Arthur Young itself conceded below that the alleged activity went beyond traditional auditing. Because I find, then, that even under the majority's "operation or management" test the Court of Appeals erroneously affirmed the summary judgment for Arthur Young, I would (again) reverse.

For our purposes, the line between managing and auditing is fairly clear. In describing the "respective responsibilities of management and auditor," Arthur Young points to the Code of Professional Conduct developed by the American Institute of Certified Public Accountants (AICPA). Brief for Respondent 31. This auditors' code points up management's ultimate responsibility for the content of financial statements:

"The financial statements are management's

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[3]In ruling on a motion for summary judgment, "[t]he evidence of the nonmovant is to be believed, and all justifiable inferences are to be drawn in his favor." *Anderson* v. *Liberty Lobby, Inc.*, 477 U. S. 242, 255 (1986). My description of the facts, based primarily on the District Court's view of the evidence at summary judgment, conforms to this standard.

> responsibility. The auditor's responsibility is to express an opinion on the financial statements. Management is responsible for adopting sound accounting policies and for establishing and maintaining an internal control structure that will, among other things, record, process, summarize, and report financial data that is consistent with management's assertions embodied in the financial statements. . . . The independent auditor may make suggestions about the form or content of the financial statements or draft them, in whole or in part, based on information from management's accounting system." 1 CCH AICPA Professional Standards, SAS No. 1, §110.02 (1982).

In short, management chooses the assertions to appear in financial statements; the auditor "simply expresses an opinion on the client's financial statements." Brief for Respondent 30. These standards leave no doubt that an accountant can in no sense independently audit financial records when he has selected their substance himself. See In re Thomas P. Reynolds Securities, Ltd., Exchange Act Release No. 29689, 1991 SEC Lexis 1855, *6–*7 (Sept. 16, 1991) ("A company may, of course, rely on an outside firm to prepare its books of account and financial statements. However, once an accounting firm performs those functions, it has become identified with management and may not perform an audit").

The evidence on summary judgment, read favorably to Reves, indicates that Arthur Young did indeed step out of its auditing shoes and into those of management, in creating the financial record on which the Co-op's solvency was erroneously predicated. The Co-op's 1980 financial statement gave no fixed asset value for the White Flame gasohol plant (although the statement did say that the Co-op had advanced the plant $4.1 million during

1980, App. in No. 87–1726 (CA8), pp. 291, 295), and there is no indication that a valuation statement occurred anywhere else in the Co-op's records at that time. When Arthur Young accepted the job of preparing the Co-op's financial statement for 1981, the value to be given the plant was a matter of obvious moment. Instead of declaring the plant's valuation to be the Co-op's responsibility, and instead even of turning to management for more reliable information about the plant's value, Arthur Young basically set out to answer its own questions and to come up with its own figure for White Flame's fixed asset value. In doing so, it repeatedly made choices calling for the exercise of a judgment that belonged to the Co-op's management in the first instance.

Arthur Young realized it could not rely on White Flame's 1980 financial statement, which had been prepared by a convicted felon (who also happened to be the Co-op's former accountant),[4] see *Arthur Young & Co.* v. *Reves*, 937 F. 2d 1310, 1316–1317 (CA8 1991), and an internal memo that appears in the record shows that Arthur Young had a number of serious questions about White Flame's cost figures for the plant. See App. in No. 87–1726 (CA8), pp. 1189–1191. Nonetheless, Arthur Young "essentially invented" a cost figure that matched, to the penny, the phoney figure that Kuykendall, White Flame's convicted accountant, had created. App. 138–140. With this "invented" cost figure in hand, Arthur Young

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[4]Gene Kuykendall, the Co-op's previous "independent auditor," was involved in keeping the Co-op's books in addition to preparing and "auditing" financial statements for White Flame. See *Arthur Young & Co.* v. *Reves*, 937 F. 2d 1310, 1316–1317 (CA8 1991); *United States* v. *White*, 671 F. 2d 1126 (CA8 1982); *Robertson* v. *White*, 633 F. Supp. 954 (WD Ark. 1986). Thus, the Co-op had a history of relying on "outside" auditors for such services.

then proceeded to decide, again without consulting management, when the Co-op had acquired White Flame. Although the Co-op's 1980 financial statement indicated an acquisition of White Flame in February 1980, as did a local court decree, see App. in No. 87–1726 (CA8), pp. 295, 1212–1214, Arthur Young "adopted a blatant fiction—that the Co-op [had] owned the entire plant at its inception in May, 1979—in order to justify carrying the asset on [the Co-op's] books at its total cost, as if the Co-op had built it from scratch." App. 137. Apparently, the idea that the Co-op had owned the gasohol plant since 1979 was reflected nowhere in the Co-op's books, and Arthur Young was solely responsible for the Co-op's decision to treat the transaction in this manner.[5]

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[5]If Arthur Young had decided otherwise, the value of White Flame on the Co-op's books would have been its fair market value at the time of sale—three to four million dollars less. See *ante*, at 3. The "blatant fiction" created by Arthur Young maintained the Co-op's appearance of solvency and made Jack White's management "look better." App. 137–138. The District Court noted some plausible motives for Arthur Young's conduct, including a desire to keep the Co-op's business and the accountants' need "to cover themselves for having testified on behalf of White and Kuykendall in [their] 1981 criminal trial." App. 136.

The majority asserts, as an ``undisputed'' fact, ``that Arthur Young relied upon existing Co-Op records in preparing the 1981 and 1982 audit reports.'' *Ante*, at 16. In fact, however, the District Court found that Reves had presented evidence sufficient to show that Arthur Young ``essentially invented'' a cost figure for White Flame (after examining White Flame records created by Kuykendall). See App. 138–140. Since the Co-op's 1980 financial statement indicated that the Co-op had advanced White Flame only $4.1 million through the end of

Relying on this fiction, the unreality of which it never shared with the Co-op's Board of Directors,[6] let alone the membership, Arthur Young prepared the Co-op's 1981 financial statement and listed a fixed asset value of more than $4.5 million for the gasohol plant. App. in No. 87–1726 (CA8), p. 238. Arthur Young listed a similar value for White Flame in the Co-op's financial statement for 1982. *Id.*, at 261. By these actions, Arthur Young took on management responsibilities, for it thereby made assertions about the fixed asset value of White Flame that were derived, not from information or any figure provided

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1980, see *supra*, at 5–6, Arthur Young could not have relied on the Co-op's records in concluding that the plant's value was nearly $4.4 million at the end of 1980. See 937 F. 2d, at 1317. The District Court also found sufficient evidence in the record to support the conclusion that Arthur Young had created the ``blatant fiction'' that the Co-op had owned White Flame from its inception, despite overwhelming evidence to the contrary in the Co-op's records. See App. 137–138; see also 937 F. 2d, at 1317 (``In concluding that the Co-op had always owned White Flame, [Arthur Young] ignored a great deal of information suggesting exactly the opposite''). The evidence indicates that it was creative accounting, not reliance on the Co-op's books, that led Arthur Young to treat the Co-op as the plant's owner from the time of its construction in 1979 (a conclusion necessary to support Arthur Young's decision to value the plant at total cost). Not even the decree procured in the friendly lawsuit engineered by White and his lawyers treated the Co-op as building the plant, or as owning it before February 1980. See *ante*, at 2.

[6] See 937 F. 2d, at 1318. In fact, Note 9 to the 1981 financial statement continued to indicate that the Co-op “acquired legal ownership” of White Flame in February 1980. App. in No. 87–1726 (CA8), p. 250.

by the Co-op's management, but from its own financial analysis.

Thus, the District Court, after reviewing this evidence, concluded that petitioners could show from the record that Arthur Young had "created the Co-op's financial statements." App. 199. The court also took note of evidence supporting petitioners' allegation that Arthur Young had "participated in the creation of condensed financial statements" that were handed out each year at the annual meeting of the Co-op. *Ibid.* Before the Court of Appeals, although Arthur Young disputed petitioners' claim that it had been functioning as the Co-op's *de facto* chief financial officer, Supplemental Reply Brief on Remand for Appellant in No. 87–1726 (CA8), p. 2, it did not dispute the District Court's conclusion that Reves had presented evidence showing that Arthur Young had created the Co-op's financial statements and had participated in the creation of condensed financial statements. Supplemental Brief on Remand for Appellant in No. 87–1726 (CA8), p. 20. Instead, Arthur Young argued that "[e]ven if, as here, the alleged activity goes beyond traditional auditing, it was neither an *integral* part of the management of the Co-op's affairs nor part of a *dominant*, active ownership or managerial role." *Id.*, at 21 (emphasis added).

It was only by ignoring these crucial concessions, and the evidence that obviously prompted them, that the Court of Appeals could describe Arthur Young's involvement with the Co-op as "limited to the audits, meetings with the Board of Directors to explain the audits, and presentations at the annual meetings." 937 F. 2d, at 1324. And only then could the court have ruled that, "as a matter of law, Arthur Young's involvement with the Co-op did not rise to the level required for a RICO violation," which it described (quoting *Bennett* v. *Berg*, 710 F. 2d 1361 (CA8 1983)) as requiring only "some participation in the operation

or management of the enterprise itself." *Ibid.* (internal quotes omitted).

But petitioners' evidence and respondent's concessions of activity going beyond outside auditing can neither be ignored nor declared irrelevant. As the Court explains today, "`outsiders' may be liable under §1962(c) if they are `associated with' an enterprise and participate in the conduct of *its* affairs —that is, participate in the operation or management of the enterprise itself . . . ." *Ante*, at 15 (emphasis in original). Thus, the question here is whether Arthur Young, which was "associated with" the Co-op, "participated" in the Co-op's operation or management. As the Court has noted, "participate" should be read broadly in this context, see *ante*, at 8 (citing *Russello* v. *United States*, 464 U. S. 16, 21–22 (1983)), since Congress has provided that even "indirect" participation will suffice. Cf. *Sedima, S. P. R. L.* v. *Imrex Co.*, 473 U. S., at 497–498 ("Congress' self-consciously expansive language" supports the conclusion that "RICO is to be read broadly").

The evidence petitioners presented in opposing the motion for summary judgment demonstrated Arthur Young's "participation" in this broad sense. By assuming the authority to make key decisions in stating the Co-op's own valuation of its major fixed asset, and by creating financial statements that were the responsibility of the Co-op's management, Arthur Young crossed the line separating "outside" auditors from "inside" financial managers. Because the majority, like the Court of Appeals, affirms the grant of summary judgment in spite of this evidence, I believe that it misapplies its own "operation or management" test, and I therefore respectfully dissent.