An Assessment of Derivative RICO Actions by Stockholders, Limited Partners and Trust Beneficiaries

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An Assessment Of Derivative RICO Actions by Stockholders, Limited Partners and Trust Beneficiaries

Thomas J. Bamonte*

I. INTRODUCTION

Section 1964(c) of the Racketeer Influenced and Corrupt Organizations Act ("RICO") provides a private cause of action to "[a]ny person injured in his business or property" from a pattern of racketeering activity.\(^1\) In an effort to limit the broad scope of RICO, courts have imposed standing requirements designed to limit RICO plaintiffs to those parties directly injured by a pattern of racketeering activity.\(^2\) Most notably, courts have concluded that section 1964(c) does not relax common law standing requirements.\(^3\)

At common law a stockholder does not have standing as an individual to sue for an injury inflicted upon the corporation, even if the value of the stockholder's shares falls as a result of the injury.\(^4\) Consequently, courts repeatedly have dismissed RICO actions brought by stockholders for lack of standing on the ground that the stockholders have been only indirectly injured by a pattern of racketeering activity directed at the corporation.\(^5\) The common law, however, provides a mechanism by which stockholders can bring suit in a representative capacity to vindicate the rights of a corporation that has been a victim of wrongdoing. Such derivative actions by stockholders have been a fixture of the law of corporations for over a century. No court has yet considered in-depth whether RICO standing principles bar stockholder derivative RICO actions. There is a risk that in their aggressive use of standing requirements to limit the scope of RICO, courts will overlook the derivative action mechanism and hold that only the corpora-

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2. See infra notes 7-22 and accompanying text.
3. See infra note 16 and accompanying text.
4. See infra note 17 and accompanying text.
5. Id.
tion victimized by a pattern of racketeering activity has standing to bring a RICO action against the wrongdoer.6

This Article examines whether RICO standing doctrines can be squared with stockholder derivative RICO actions. After surveying the judicial response to RICO suits by stockholders and after describing the derivative action mechanism, this Article suggests that courts should permit stockholder derivative RICO actions. It also examines the analogous rights of limited partners and trust beneficiaries to bring derivative RICO actions and concludes that these groups, like stockholders, should be able to maintain such actions.

II. THE STANDING LIMITS ON RICO ACTIONS BY STOCKHOLDERS

In their effort to restrict the broad scope of RICO, many courts have imposed standing requirements designed to limit the right to pursue a RICO action to only those parties “directly injured” by a RICO violation.7 Other courts have rejected a strict direct/indirect injury dichotomy as the test of RICO standing but have imposed standing requirements nearly as restrictive.8 Thus, courts have held that union members have no standing to bring RICO


7. The United States Supreme Court in Sedima, S.P.R.L. v. Imrex Co., 473 U.S. 479 (1985) laid the foundation of the standing doctrine in RICO actions. The Sedima Court held that recoverable RICO damages are those which “flow from the commission or predicate acts.” Id. at 497 (emphasis added). Lower courts have interpreted Sedima as requiring a “direct injury.” See Marshall & Ilsley Trust Co. v. Pate, 819 F.2d 806, 809 (7th Cir. 1987); Morast v. Lance, 807 F.2d 926, 932-33 (11th Cir. 1987); Nodine v. Textron, Inc., 819 F.2d 347, 348-49 (1st Cir. 1987); see also Town of Kearney v. Hudson Meadows Urban Renewal Corp., 829 F.2d 1263, 1268 (3d Cir. 1987); Klapper v. Commonwealth Realty Trust, 657 F. Supp. 948, 953 (D. Del. 1987) (“the requirement of direct injury is the gravamen of RICO standing”). In Carter, 777 F.2d at 1176, the court stated “that the directly injured party should receive a complete recovery, no matter what; an indirectly injured party should look to the recovery of the directly injured party, not to the wrongdoer, for relief.”

8. See, e.g., Zervas v. Faulkner, 861 F.2d 823, 832-35 (5th Cir. 1988) (rejecting direct/indirect dichotomy in favor of “proximate cause” approach); see also Branderburg v. Seidel, 859 F.2d 1179, 1187 (4th Cir. 1988); Sperber v. Boesky, 849 F.2d 60, 64 (2d Cir. 1988).
actions to redress a pattern of racketeering inflicted upon their union.\textsuperscript{9} Guarantors have no standing to bring a RICO suit against a pattern of racketeering aimed at their obligors.\textsuperscript{10} Creditors lack standing to complain of RICO violations committed against the debtor.\textsuperscript{11} Employees have no standing to bring RICO actions complaining that they were fired for "whistle-blowing" or for refusing to participate in a pattern of racketeering.\textsuperscript{12} Governmental bodies do not have standing to bring RICO claims in a \textit{parens patriae} capacity.\textsuperscript{13}

As part of this effort to limit RICO standing, courts consistently have barred stockholders from bringing RICO actions in their individual capacity for injuries inflicted upon a corporation through a pattern of racketeering activity. In an important early case, \textit{Warren v. Manufacturers National Bank},\textsuperscript{14} for example, the stockholder of a corporation bankrupted allegedly by a creditor's interest rate overcharges brought a RICO action in his capacity as a stockholder. Looking to general principles of corporate law, the court found that only the corporation had a right of action against

\begin{footnotesize}
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\item[9.] See \textit{Adams-Lundy v. Association of Professional Flight Attendants}, 844 F.2d 245, 258 (5th Cir. 1988); \textit{Bass v. Campagnone}, 838 F.2d 10, 12 (1st Cir. 1988).
\item[11.] See \textit{National Enter., Inc. v. Mellon Fin. Servs. Corp.}, 847 F.2d 251, 254-55 (5th Cir. 1988) ("To be sure, today we will not say that the creditor . . . can never have standing under RICO . . . We suppose that such standing is imaginable" but in the usual case the creditor lacks standing) (emphasis in original); \textit{Barnett v. Stern}, 93 Bankr. 962, 967 (N.D. Ill. 1988). \textit{But see Bankers Trust Co. v. Rhoades}, 859 F.2d 1096, 1100-01 (2d Cir. 1988), \textit{cert. denied}, 109 S. Ct. 1642 (1989) (creditor had RICO standing because direct victim of bankruptcy fraud).
\item[12.] See \textit{Burdick v. American Express Co.}, 865 F.2d 527, 529 (2d Cir. 1989); \textit{Norman v. Niagara Mohawk Power Corp.}, 873 F.2d 634, 637 (2d Cir. 1989); \textit{Cullom v. Hibernia Nat'l Bank}, 859 F.2d 1211, 1215 (5th Cir. 1988); \textit{Morast v. Lance}, 807 F.2d 926, 932-33 (11th Cir. 1987); \textit{Nodine v. Textron, Inc.}, 819 F.2d 347, 349 (1st Cir. 1987); \textit{Pujol v. Shearson/American Express, Inc.}, 829 F.2d 1201, 1205 (1st Cir. 1987).
\item[13.] See \textit{State of Illinois v. Life of Mid-America Ins. Co.}, 805 F.2d 763, 766 (7th Cir. 1986). Courts have been unsuccessful in other attempts to limit the scope of RICO through restrictive standing requirements. For example, in \textit{Sedima, S.P.R.L. v. Imrex Co.}, 473 U.S. 479, 495-97 (1985), the Supreme Court rejected the Second Circuit's attempt to impose a "racketeering injury" standing requirement. The Court also recently rejected a requirement that the predicate acts for a RICO action must be characteristic of organized crime. \textit{H.J. Inc. v. Northwestern Bell Tel. Co.}, 109 S. Ct. 2893 (1989). Other attempts to limit RICO likewise have been rejected. See \textit{Bunker Ramo Corp. v. United Business Forms, Inc.}, 713 F.2d 1272, 1287 (7th Cir. 1983) (rejecting "competitive injury" standing requirement); \textit{USACO Coal Co. v. Carbomin Energy, Inc.}, 689 F.2d 94, 94 n.1 (6th Cir. 1982) (rejecting prior RICO conviction requirement).
\item[14.] 759 F.2d 542, 543 (6th Cir. 1985).
\end{itemize}
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the creditor and dismissed the RICO claim.  

The court in Warren concluded that nothing in the language of the RICO statute indicates that Congress intended to relax the common law rule barring stockholders from suing in their individual capacity for injuries inflicted upon the corporation:

Whether RICO should or should not be interpreted to 'federalize' common law fraud is an issue distinct from whether it should be interpreted to materially expand the standing requirement applicable to such claims. Allowing every shareholder, employee and creditor a cause of action for injuries derivative of those suffered directly by a corporation does not just permit a vast amount of litigation to be brought in federal court that previously could only have been brought in state court, but creates a potential avalanche of suits that previously could not have been brought at all. Like Warren, other courts have refused to allow stockholders to individually proceed with RICO suits to redress injuries from a pattern of racketeering activity directed against the corporation.  

The stockholder RICO actions filed after the Federal Deposit Insurance Corporation ("FDIC") has taken over a failed financial institution are typical. Stockholders in such cases file individual actions against the directors of the failed financial institution for two reasons. Shareholders file such actions in an effort to get a larger recovery than they would receive as a result of the FDIC's liquidation or reorganization of the financial institution and in order to avoid the burdensome procedural requirements associated with stockholder derivative actions. The courts generally look to state law to determine if the stockholder's claimed injury is unique, i.e., direct to the stockholder and thus of the type for which the

15. Id. at 544.
16. Id. at 545 (emphasis in original); see also Gallagher v. Canon U.S.A., Inc., 588 F. Supp. 108, 110 (N.D. Ill. 1984) ("there is no indication whatever Congress intended courts to disregard the corporate entity in interpreting Section 1964(c)").
19. See infra notes 35-44 and accompanying text (for a discussion of the procedural requirements of derivative actions).
stockholder can sue in an individual capacity. 20 The courts use the same state law standards to determine stockholder standing in RICO actions as they use to evaluate the standing of stockholders who bring other types of federal and state law claims. 21

The FDIC's litigation capabilities, and its incentive as the receiver of a failed financial institution to vigorously pursue RICO claims belonging to the institution, may have lulled some courts into making pronouncements that only a corporation has standing to bring a RICO claim for injuries suffered from a pattern of racketeering directed at the corporation. 22 To date, however, the decisions in stockholder RICO actions have failed to address whether stockholders may bring derivative RICO actions when the corporation is unable or unreasonably fails to pursue RICO claims that belong to the corporation.

III. STOCKHOLDER DERIVATIVE ACTIONS

Stockholder derivative actions are a creation of equity and have been a well recognized feature of American jurisprudence for over 150 years. 23 In a derivative action, the corporation is the real party in interest. 24 The stockholder bringing the action is only the nominal plaintiff 25 because the substantive claims raised in a derivative action belong to the corporation rather than the stockholder. 26

The derivative action mechanism originated as the principal defense of minority stockholders against abuses of the majority stockholders. 27 As the base of equity ownership in corporations

20. See Leach, 860 F.2d at 1274; Crocker, 826 F.2d at 349; see also Mid-State Fertilizer Co. v. Exchange Nat'l Bank, 877 F.2d 1333, 1335 (7th Cir. 1989); Ocean Energy II, Inc. v. Alexander & Alexander, Inc., 868 F.2d 740, 744-45 (5th Cir. 1989).

21. See Sparling, 864 F.2d at 640-41 (standing to bring fraud claim); Crocker, 826 F.2d at 349-52 (standing to bring misrepresentation claim). See generally FED. R. CIV. P. 17(b).


25. Ross, 396 U.S. at 538.

26. Koster v. Lumbermens Mut. Casualty Co., 330 U.S. 518, 522 (1947). The Rand court stated that "[a] RICO action . . . is a corporate asset, and shareholders cannot bring it in their own names without impairing the rights of prior claimants to such assets." 794 F.2d at 849. See also Mid-State Fertilizer Co. v. Exchange Nat'l Bank, 877 F.2d 1333, 1335 (7th Cir. 1989). For further discussion of Mid-State, see infra note 53 and accompanying text.

broadened, resulting in a growing separation of equity ownership from day-to-day control of the typical corporation, the derivative action took on an “important role in protecting stockholders of corporations from the designing schemes and wishes of insiders who are willing to betray their company’s interests in order to enrich themselves.”

The derivative action “developed in equity to enable shareholders to sue in the corporation’s name when those in control of the company refused to assert a claim belonging to it.”

In order to maintain a derivative action, a stockholder must allege that the corporation has a cause of action. For example, fraud or breaches of fiduciary duty perpetrated against the corporation by insiders, the wrongful acts of third parties against the corporation, and ultra vires acts by the corporation all can give rise to a stockholder derivative action. In addition, the stockholder must show that he will be harmed by, for example, a decline in the value of the corporation’s stock, if the corporation fails to assert its legal rights.

In contrast, a stockholder may maintain an individual action against a corporation when the stockholder has sustained a “special injury.” The special injury requirement is satisfied when the alleged wrong has been inflicted upon a stockholder in his individual capacity, independent of any duty owed the corporation. For instance, stockholders have standing to sue when the alleged wrong is directed at the contractual rights of stockholders such as their right to vote.

34. See Schnell v. Chris-Craft Indus., Inc., 285 A.2d 437, 439 (Del. 1971); Moran, 490 A.2d at 1070-71; Condec Corp. v. Lunkenheimer Co., 230 A.2d 769, 775 (Del. Ch. [Vol. 21]
Parties who bring derivative actions must meet several procedural requirements designed to protect the corporation against abuse of the derivative action mechanism. Most notably, before pursuing a derivative action, the stockholder must make a demand upon the corporation to rectify the alleged wrong. The demand requirement allows the directors of the corporation the opportunity to take corrective action without the cost and delay of litigation. The demand requirement also protects the corporation against strike suits. In exercising their business judgment after demand has been made, the directors may dismiss the derivative action as unfounded or otherwise not in the best interests of the corporation. Generally, courts have taken a deferential posture toward decisions to dismiss derivative actions purportedly made by independent special committees of boards of directors.

The courts, however, do waive the demand requirement in instances demand would be futile when, for example, an obvious conflict of interest of the corporation's board of directors exists, or the corporation is under the control of the persons who have committed or threaten to commit the complained of wrongs. Derivative actions may also go forward when corporate insiders wrongfully fail to take action on behalf of the corporation after demand has been made.


37. Aronson, 473 A.2d at 811-12.


40. Koster v. Lumbermens Mut. Casualty Co., 330 U.S. 518, 522 (1947); Aronson, 473 A.2d at 814; see also Norlin Corp. v. Rooney, 744 F.2d 255, 261-62 (2d Cir. 1984) (board participated in "wrongful transactions"); Pogostin v. Rice, 480 A.2d 619, 627 (Del. 1984) (demand is excused when "allegations detail the manipulation of corporate machinery by directors for sole or primary purpose of perpetuating themselves in office").

41. See Zapata, 430 A.2d at 788-89. Zapata establishes a two-step analysis to be applied to a motion to dismiss a derivative action: (1) whether the board or special committee made a reasonable investigation, and acted independently and in good faith; (2) if
Stockholders bringing a derivative action must surmount other procedural obstacles in addition to meeting the demand requirement. Stockholder derivative plaintiffs must establish that they were stockholders at the time of the alleged wrong, and they must maintain stockholder status throughout the litigation. In addition, the stockholder bringing the derivative action must be a fair and adequate representative of the stockholders who are enforcing the corporation's right. Finally, settlements and dismissals of derivative actions require court approval after notice to the stockholders.

IV. AN ASSESSMENT OF STOCKHOLDER DERIVATIVE RICO ACTIONS

The reported decisions discussing stockholder standing to bring RICO actions have arisen when the stockholder is suing in an individual capacity. These cases have turned on whether the stockholder has demonstrated a “special injury” under the applicable state law such that the stockholder has standing to bring an action in an individual capacity. The sweeping language in some of these opinions imply that only the injured corporation has standing to bring a RICO action. The standing doctrines applied in those cases, however, do not foreclose stockholder derivative RICO actions if a derivative action is appropriate under applicable rules governing derivative actions.

No court, in fact, has directly faced whether section 1964(c) imposes stricter standing requirements for stockholder derivative RICO actions than common law derivative action rules, or if the corporation satisfies this first burden, the court may exercise its own business judgment to determine if the derivative suit should be dismissed. Compare Kaplan v. Wyatt, 499 A.2d 1184, 1191-92 (Del. 1985) (approving recommendation by special committee of directors that derivative action be dismissed) with Lewis v. Fugua, 502 A.2d 962, 967 (Del. Ch. 1989) (denying motion to dismiss derivative action under two-step Zapata analysis); see also Joy v. North, 692 F.2d 880, 888 (2d Cir. 1982), cert. denied, 460 U.S. 1051 (1983) (derivative action should not have been dismissed because special committee members were not independent); Mills v. Esfandi, Inc., 544 F. Supp. 1275, 1284 (N.D. Ill. 1982).

44. FED. R. CIV. P. 23.1; DEL. CH. CT. R. 23.1. See generally In re Ortiz Estate, 27 A.2d 368, 374 (Del. Ch. 1942).
45. See supra note 17 and accompanying text.
46. See, e.g., Carter v. Berger, 777 F.2d 1173, 1175 (7th Cir. 1985) ("only the firm may vindicate the [RICO] rights at issue").
whether section 1964(c) altogether bars stockholder derivative actions on the ground that only the directly injured party can be a RICO plaintiff. There are several reasons why the courts should neither bar stockholder derivative RICO actions nor impose more burdensome standing requirements on such actions than those already imposed by the common law.

First, the RICO statute's language does not reveal any Congressional intent to displace common law standing rules and to bar stockholder derivative RICO actions. Section 1964(c) gives "any person injured in his business or property" standing to bring a RICO action. In fact, the language of section 1964(c) can be read broadly as relaxing the common law bar against individual stockholder actions directed at the party which inflicted an injury on the corporation. Section 1964(c), after all, appears to give the stockholder ("any person") whose stock ("property") has declined in value due to a pattern of racketeering activity perpetrated against the corporation, standing to bring a RICO action against the wrongdoer. To similar effect is the statutory directive that RICO be liberally construed.

Second, when considering an individual stockholder's RICO suit, courts have pointed to Congressional silence in the RICO statute as evidence of Congressional intent to not relax common law standing requirements for such actions. The same logic can be applied to determine whether Congress intended to preclude or restrict derivative RICO actions. Presumably, when enacting the RICO statute, Congress knew of the shareholder derivative action's function and operation. Therefore, Congress' silence with regard to shareholder derivative RICO actions evidences its intent to neither preclude nor restrict shareholder derivative actions.

Third, courts long have recognized that stockholders can bring derivative actions raising federal as well as state law claims. Stockholders, for example, may pursue securities law claims in a derivative capacity. Most notably, courts allow stockholder derivative actions raising federal antitrust law claims. Congress looked to

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the antitrust laws as a model in drafting the RICO statute and presumably was aware that the courts likely would allow stockholder derivative RICO actions unless directed otherwise. The absence of an express bar to stockholder derivative RICO actions indicates Congressional acceptance of such actions.

Fourth, as noted above, one of the derivative action’s key functions has been to allow stockholders to vindicate the corporation’s rights when the corporation is unable or unreasonably fails to assert its rights against an exploitative insider or a third-party wrongdoer. Allowing stockholders to pursue RICO actions on behalf of their corporation in such situations comports with the common law and statutory framework of the derivative action. Stockholder derivative RICO actions require no modification or abrogation of state law rules governing the circumstances in which stockholders can bring actions in their individual capacity. Nor must existing procedural requirements associated with stockholder derivative actions be changed to accommodate stockholder derivative RICO actions. In fact, courts on occasion have applied, with no evident difficulty, rules governing derivative actions to shareholder derivative RICO actions.

Fifth, RICO claims belonging to a corporation are likely to arise in the very situations that disable the corporation from protecting its legal rights. This is true, for example, when the perpetrator of a pattern of racketeering activity against the corporation controls the
denied, 401 U.S. 974 (1971); Gottesman v. General Motors Corp., 414 F.2d 956 (2d Cir. 1969); Rogers v. American Can Co., 305 F.2d 297, 317 (3d Cir. 1962); Ramsburg v. American Inv. Co., 231 F.2d 333, 339 (7th Cir. 1956); Fanchon & Marco, Inc. v. Paramount Pictures, Inc., 202 F.2d 731, 734-35 (2d Cir. 1953); see also Stein v. United Artists Corp., 691 F.2d 885, 897 (9th Cir. 1982).


53. See Mid-State Fertilizer v. Exchange Nat’l Bank, 877 F.2d 1333, 1335 (7th Cir. 1989) (“the rules established in anti-trust cases for identifying the proper plaintiffs should be applied to RICO . . .”).

54. See supra notes 27-29 and accompanying text.

corporation.\(^{56}\) RICO's well recognized core purpose is to prevent "racketeers" from gaining control of legitimate companies through a pattern of racketeering activity.\(^{57}\) When coupled with the existing barriers to RICO actions by creditors, guarantors, employees and others with a stake in the corporation, the practical effect of a prohibition on stockholder derivative RICO actions would be to insulate from civil RICO actions those parties who perpetrated a pattern of racketeering against a company over which they had control. Ironic indeed would be a rule that leaves the decision of whether a company will bring a RICO action to the very parties who may have perpetrated a pattern of racketeering activity against the corporation.

Finally, the procedural requirements that stockholders must meet before bringing a derivative action alleviate the purported threat of an "avalanche" of stockholder RICO suits so feared by the courts.\(^{58}\) There is no evidence that the demand requirement and the other procedural rules associated with derivative actions will be less effective with respect to RICO claims than with other types of claims.\(^{59}\)

V. DERIVATIVE ACTIONS BY LIMITED PARTNERS

The law is less well developed with respect to derivative actions brought by limited partners on behalf of a partnership. The existence and scope of the limited partner's right to bring a derivative action is determined by applicable state law.\(^{60}\) Courts are split as to whether limited partners have the capacity to bring a derivative

\(^{56}\) See, e.g., Rubin v. Posner, 701 F. Supp. 1041, 1044 (D. Del. 1988) (corporation president engaged in racketeering against corporation in order to benefit another entity he controlled); see also Lochhead v. Alacano, 697 F. Supp. 406, 408-09 (D. Utah 1988) (directors fraudulently adopted and executed a stock option plan that resulted in their receiving additional stock at the time of a merger). In Carter v. Berger, 777 F.2d 1173, 1178 (7th Cir. 1985), a case often cited as support for a bar of RICO suits by parties indirectly injured by a pattern of racketeering activity, the court nevertheless recognized that "[d]oubtless indirectly injured parties could recover under RICO when they show that the directly injured party was under the continuing control or influence of the defendant or his henchmen."


\(^{58}\) See Warren v. Manufacturers Nat'l Bank, 759 F.2d 542, 545 (6th Cir. 1985).


\(^{60}\) FED. R. CIV. P. 17(b). See also Allright Missouri, Inc. v. Billeter, 829 F.2d 631, 635 (8th Cir. 1987). For further discussion of Allright, see infra notes 71-73 and accompanying text.
suit. 61

Courts allowing limited partners to bring derivative actions do so for three major reasons. First, they analogize limited partners to stockholders and view limited partners as having a similar need to protect the investment vehicle when the designated managers wrongfully do not. 62 Second, the two traditional remedies for a limited partner, namely, dissolution of the partnership and an action for accounting, are often ineffective. 63 Dissolution may force the limited partner to terminate a profitable investment or suffer adverse tax consequences. 64 An action for accounting is often ineffective when there is ongoing wrongdoing by management or the wrongs are committed by a third party. 65 Third, courts upholding derivative actions by limited partners have recognized that disruption to the partnership from such suits will be minimized by requiring the plaintiffs to meet the same procedural requirements as stockholder derivative plaintiffs. 66

In contrast, the rationale for denying derivative suits by limited partners is based on the premise that restricted management rights are the quid pro quo for the economic advantages of limited liability enjoyed by limited partners. Allowing limited partners to bring derivative actions, the argument goes, grants them more management rights without a corresponding increase in liability. 67 Thus, derivative actions by limited partners should not be allowed unless expressly authorized by statute. 68


63. Id. at 299.

64. See Allright, 829 F.2d at 636.


66. Allright, 829 F.2d at 639.


The weight of authority, however, favors derivative actions by limited partners. The Revised Uniform Limited Partnership Act provides for derivative actions by limited partners “if general partners with authority to do so have refused to bring the action or if an effort to cause the general partners to bring the action is not likely to succeed.”69 Most states have incorporated into their limited partnership statutes provisions allowing derivative actions by limited partners.70

In the leading case that allows a limited partner to bring a derivative RICO action, Allright Missouri, Inc. v. Billetter,71 the limited partner sued the general partners and other parties in connection with alleged fraud in the conveyance of partnership property to another partnership controlled by the general partners.72 The Eighth Circuit’s opinion thoroughly and persuasively analyzed the reasons limited partners should be allowed to bring derivative actions. Its analysis, however, did not focus on whether the rules governing derivative actions by limited partners should differ when a RICO claim is involved. This was not an error in the court’s analysis, rather, it reflects the absence of any reason why RICO claims should be treated differently with respect to the availability of a derivative action.73 If anything, derivative RICO actions by limited partners should be favored because the same pattern of racketeering activity that forms a RICO claim’s basis causes the parties controlling a partnership to fail to vindicate the partnership’s rights.74

V. DERIVATIVE ACTION BY TRUST BENEFICIARIES

The law with respect to derivative actions by trust beneficiaries

69. Uniform Limited Partnership Act § 1001 (1976). Under the Revised Uniform Partnership Act § 1002 (1985), the plaintiff must be a partner at the time he brings the derivative action, and he must have (i) been a partner at the time of the action being complained of or (ii) obtained partnership status by operation of law or pursuant to the partnership agreement from a person who was a partner at the time of that transaction. In addition, the derivative plaintiff must set forth with particularity the effort made to persuade the general partner to take action or the reasons for not making such an effort. Id. at § 1003. Successful plaintiffs are entitled to reasonable expenses, including attorney’s fees. Id. at § 1004.


71. 829 F.2d 631 (8th Cir. 1987).

72. Id. at 633-34.

73. See supra notes 46-59 and accompanying text (for a discussion of stockholder derivative RICO actions).

74. Cf. supra notes 55-56 and accompanying text.
is even more unsettled than the law with respect to derivative actions by limited partners.\textsuperscript{75} Yet, given the vast amount of stock and other property held in trust and the large number of trust beneficiaries, resolving the question of trust beneficiaries' standing to bring derivative RICO actions is extremely important.\textsuperscript{76}

At common law, the general rule is that only the trustee has standing to bring an action on behalf of the trust because the trustee has legal title to the trust property.\textsuperscript{77} Courts, however, do allow trust beneficiaries to step in the shoes of the trustee when the trustee fails to bring an action on behalf of the trust for no good reason.\textsuperscript{78}

The ability of trust beneficiaries to bring stockholder derivative actions is governed by state statute. Some states have adopted derivative action statutes based on section 49 of the Model Business Corporation Act, which provides that no derivative action "shall be brought . . . by a shareholder . . . unless the plaintiff was a holder of record of shares . . . at the time of the transaction of which he completes."\textsuperscript{79} In these states, trust beneficiaries cannot maintain stockholder derivative actions because the trustees, and not the trust beneficiaries, hold the stock in trust.\textsuperscript{80}

Other state statutes allow parties who have a "beneficial interest" in stock to bring a stockholder derivative action.\textsuperscript{81} Courts have construed these statutes as allowing trust beneficiaries to bring stockholder derivative actions.\textsuperscript{82} Still other states have modeled their derivative action statutes after Rule 23.1 of the Federal Rules of Civil Procedure, which provides that "the complaint . . . shall allege . . . that the plaintiff was a shareholder . . . at the time of the transaction of which he complains or that his share . . . thereafter devolved on him by operation of law."\textsuperscript{83} The courts are divided as to the ability of individual trust beneficiaries to bring stockholder

\textsuperscript{76} See, e.g., Diduck v. Kaszycki & Sons Contractors, Inc., 874 F.2d 912, 912 (2d Cir. 1989) (RICO claim by participant in ERISA plan).
\textsuperscript{77} See G.G. Bogert, Trust & Trustees § 869 (2d ed. rev. 1982).
\textsuperscript{78} Id. at 90-94.
\textsuperscript{79} Model Business Corp. Act Ann. § 49 (1971) (emphasis added).
derivative actions under Rule 23.1.\textsuperscript{84}

The better approach is to treat actions by trust beneficiaries as a form of double derivative action. Double derivative actions typically occur when a holding company’s stockholder brings a derivative action on behalf of the holding company which is in fact for the subsidiary corporation’s benefit. The theory behind double derivative actions is that, given the close link between holding companies and subsidiaries, the failure of both the holding company and the subsidiary to take corrective steps justifies a derivative action by the holding company’s stockholders.\textsuperscript{85} To bring a derivative action for wrongs committed against the subsidiary, the stockholder must show a wrongful failure by the management of both the holding company and the operating company to take corrective action.\textsuperscript{86}

The trust beneficiary is similar to the stockholder in the holding company. Thus, to maintain a derivative action, a trust beneficiary should be required to show that a third party is harming the property interest held by the trust, the trustee has wrongfully failed to take corrective measures and is or will be unresponsive to any demand for improvement.\textsuperscript{87} Courts generally have upheld double derivative actions,\textsuperscript{88} and there is no reason why they should ban derivative actions by trust beneficiaries who meet similar procedural requirements.

Moreover, there are no reasons unique to RICO that should bar RICO derivative actions by trust beneficiaries. As with all derivative actions, a derivative action by a trust beneficiary is for the benefit of the entity, the trust, that is being harmed by the actions of insiders or third parties. Thus, trust beneficiaries who bring deriv-
ative RICO actions are no more suing for "indirect" injuries than other RICO derivative plaintiffs.

VI. CONCLUSION

Numerous courts have held that stockholders cannot bring RICO actions in their individual capacity for injuries to their corporation that have resulted from a pattern of racketeering activity. These decisions, however, do not foreclose derivative actions by stockholders that raise RICO claims belonging to the corporation. Stockholder derivative RICO actions further the purposes of the RICO statute and will be regulated satisfactorily by the existing procedural rules associated with derivative actions.

Derivative actions by limited partners and trust beneficiaries are less common and less well-established than derivative actions by stockholders. Nevertheless, when limited partners and trust beneficiaries satisfy the procedural requirements for maintaining a derivative action, there is nothing unique about the RICO statute that should bar those parties from maintaining a derivative RICO action.

A growing number of cases in which courts have dismissed RICO actions brought by plaintiffs in their individual capacity attest to the need for greater utilization of the derivative action mechanism. Although the procedural requirements for derivative actions are rigorous, they are not insurmountable. Plaintiffs in many cases will benefit by meeting these requirements rather than losing their RICO claim altogether.