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No. 08-969

In The
Supreme Court of the United States

HEMI GROUP, LLC, and KAI GACHUPIN,
Petitioners,
v.

CITY OF NEW YORK,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Second Circuit

PETITIONERS' REPLY BRIEF

RANDOLPH H. BARNHOUSE
Counsel of Record
LUEBBEN JOHNSON & BARNHOUSE LLP
7424 4TH STREET NW
LOS RANCHOS DE ALBUQUERQUE, NM 87107
(505) 842-6123
dbarnhouse@luebbenlaw.com
Counsel for Petitioners

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Becker Gallagher · Cincinnati, OH · Washington, D.C. · 800.890.5001

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ARGUMENT

I. Respondent's "Counter-Statement of the Case" Does Not Alter RICO's Injury to "Business or Property" Standing Limitation.

Respondent dedicates a quarter of its response to a "Counter-Statement of the Case" filled with ad hominem attack against Petitioner Hemi. Amici's brief is replete with similar rhetoric, yet devoid of a single record citation.[1] Together they weave a web of hypothetical evils including "contraband" cigarettes, smuggling, corruption of government officials and terrorism, all of which they claim will run rampant if RICO's hammer cannot be used to collect taxes, trebled no less, from a business that never owed them. But Respondent did not allege these recent claims in its original complaints, and of the multitude of claims it did allege, all have been decided against Respondent save for the one before this Court.

Respondent's only specific remaining complaints are that Hemi maintains its sales did not implicate the Jenkins Act requirement that it provide customer lists

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[1] Amici describe Hemi's repeatedly successful defense of its business as "shameful". Brief of the States of Indiana, et al. in Support of Respondent corrected by filing dated September 29, 2009 ("amici brief") at 3. Similar vilification has not succeeded in connection with other overreaching civil RICO claims. *Compare Procter & Gamble Co. v. Amway Corp.*, 242 F.3d 539 (5th Cir. 2001) (affirming dismissal of civil RICO claims against Amway) *with* http://www.amquix.info/blakey.html (expert report in support of Procter & Gamble at pages 1 and 2: "It is my opinion that the Amway business is run in a manner that is parallel to that of major organized crime groups, in particular the Mafia").

to the state of New York,[2] and that Hemi's websites contained statements that "sales are 'tax free'" (*e.g.,* Response at 1, 7) or that "no tobacco tax" was payable on the purchase (*e.g.*, Response at 7)[3]. But Hemi did not owe Respondent reports listing which City residents bought cigarettes.[4] Instead, "[t]he City was at best an expectant gratuitous donee of information from the State" *City of New York v. Smokes-Spirits.com*, 541 F.3d 425, 460 (2d Cir. 2008)(Winter, J., dissenting).[5] And Respondent concedes that Hemi's

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[2] Conspicuously absent from the list of governments participating as amicus are the State of New York and the Federal Government.

[3] Only some of the cited pages are from Petitioner's websites.

[4] The Amended Complaint's specific allegations are particularly telling: "Defendants' failure to file Jenkins Act reports is materially deceptive and misleading to New York City consumers." Amended Complaint ¶ 107, Second Circuit Court of Appeals Joint Appendix ("Cir. Jt. App".) A913. Yet Jenkins Act reports are not directed to consumers nor to the City (Complaint ¶¶ 45-47, Cir. Jt. App. A810-11), nor even seen by them. Therefore, the filing or non-filing of such reports cannot be deceptive or misleading to them. Hemi also disputes that the Jenkins Act applied to its on-reservation sales.

[5] "Absent the Jenkins Act, appellees would have owed no duty to disclose their sales to anyone, and their failure to disclose could not conceivably be deemed fraud of any kind. Appellees owe no taxes to the City. The tax evasion is by the purchasers of the tobacco products. Even with the Jenkins Act, which requires reporting only to state authorities, appellees have no duty to disclose anything to the City. Indeed, conspicuously absent from the City's pleadings is any claim brought pursuant to the Jenkins Act itself, rather than RICO, seeking enforcement of the Jenkins Act, effectively an admission that the Act does not protect the City." *City of New York*, 541 F.3d at 460 (Winter, J., dissenting).

"sales" were tax free,[6] and "no tobacco taxes" were payable on sales.[7] Only the City possessory tax is at issue: a tax owed not by Hemi, but by non-litigant third parties.[8] As to those taxes, Petitioner Hemi's websites advised purchasers to contact state authorities.[9] Indeed, it would be unreasonable for any customer, much less Respondent, to argue city residents are absolved of tax obligations based on a vendor's Internet web site. *Cf. United States v. Boyle*, 469 U.S. 241, 252 (1985)("The failure to make a timely filing of a tax return is not excused by the taxpayer's reliance on an agent, and such reliance is not 'reasonable cause' for a late filing"). Hemi competed in

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[6] Response at 49: "Hemi has admitted that prices are lower because State and City taxes are not and will not be included in the price;" and at 50 n.24: "the City has never disputed that it is the purchasers who owe the tax."

[7] Response at 4: "Under federal law, sellers located out-of-state may not be required to purchase and apply New York tax stamps;" *see also* note 8.

[8] "It is intended that the ultimate incidence of and liability for the tax shall be upon the consumer," N.Y.C. Admin. Code § 11-1302(a)(3).

[9] *E.g.,* Cir. Jt. App. A853-54: "It is the responsibility of the visitor/customer of CigarettesSpecials.com to comply with any laws regarding the purchase and use of any cigarettes in their State. In order to determine the applicable limits on purchases or taxing responsibilities, if any, imposed by your particular state, you may want to contact your state authorities." (Emphasis in original); *see also* Cir. Jt. App. A850, A936 and A1059 (same notice appears on FreeCigs4U.com and BuyDiscountCigarettes.com).

the market.[10] It did so charging prices unaffected by New York City because Hemi did not owe, and did not pay, any of the taxes at issue. In these circumstances, principles of competition:

> [s]uggest that RICO does not permit private action based solely upon this competitive type of harm, *i.e.*, harm a plaintiff suffers only because the defendant was able to attract customers through normal competitive methods, such as lower prices, better products, better methods of production, or better systems of distribution. In such cases, the harm falls outside the limits that RICO's private treble-damages provision's 'proximate-cause' requirement imposes. In such cases the distance between the harm and the predicate acts that funded (or otherwise enabled) such ordinary competitive activity is too distant. The harm is not 'direct.'

Anza v. Ideal Steel Supply Corp., 547 U.S. 451 at 482-483 (Breyer, J., concurring).

The District Court dismissed all of Respondent's claims.[11] The Second Circuit affirmed the majority of

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[10] Annice E. Kim et al., Smokers Beliefs and Attitudes about Purchasing Cigarettes on the Internet, 121 PUB. HEALTH REP. 594-602 (Sept./Oct. 2006) at 595 (73% of smokers who purchase online do so for the convenience).

[11] Respondent never alleged violation of NY CLS Pub Health § 1399-ll, which regulates shipment and delivery of cigarettes, not

the district court's holdings on RICO and state law claims.[12] The New York State Court of Appeals, on the Second Circuit's certification of two remaining state law claims, ruled unanimously in favor of Hemi, confirming that Respondent's claims were "entirely derivative" of injuries allegedly suffered by others. No court has ever held that Hemi's business model was fraudulent or illegal.

Yet even if taken as true, Respondent's ad hominem attacks do not magically transform Respondent's alleged loss of sovereign "opportunity" into a RICO injury to "business or property." It is not Hemi's business model that brings the parties before this Court. Instead, it is Respondent's attempt to expand legislation beyond its scope and the intention of its drafters that has forced petitioner Hemi and its owner to defend its operations before this Court, the United States Court of Appeals, the New York State Court of Appeals, and in the United States District Court.

Internet sales. *See Brown & Williamson Tobacco Corp. v. Pataki,* 320 F.3d 200 (2d Cir. 2003).

[12] Respondent incorrectly claims that the Court of Appeals "reinstated the majority of the federal RICO claims" (Response at 10). The Court of Appeals affirmed dismissal of half of Respondent's RICO claims. *City of New York*, 541 F.3d at 451 (2d Cir. 2008)("we affirm the District Court's finding that the City failed to sufficiently allege a functioning unit with respect to the Hemi Group association-in-fact enterprise").

II. RICO's "Injury to Business or Property" Limitation Precludes Recovery for Injury to a Sovereign Tax Collection Interest.

A. Respondent does not dispute the historic context and legislative history of RICO's "injury to business or property" limitation.

Respondent and amici do not deny that RICO's injury to "business or property" requirement was taken directly from the Antitrust Acts. *Anza*, 547 U.S. 451 (2006)(discussing RICO's roots in antitrust law). They nevertheless urge the Court to ignore RICO's roots; RICO's specific language; canons of construction applied when Congress incorporates language from prior law; this Court's use of antitrust precedent to interpret RICO; the language's context in RICO; and the historical context of this restriction's adoption by Congress.

Instead, Respondent and amici propose that the Court simply apply RICO's "liberal construction clause." Yet the "liberal construction clause" is not a free pass permitting all claims. Instead it is a "tie breaker" applied only if the statute is unclear, and the context does not resolve the interpretation issue. *Reves v. Ernst & Young*, 507 U.S. 170, 189 (1993)(Souter, J., dissenting)("Congress has given courts *faced with uncertain meaning* a clear tiebreaker in RICO's 'liberal construction' clause" (emphasis supplied)). This Court consistently has rejected the "all claims are allowed" analysis even given the liberal construction clause. *E.g., Holmes v. Sec. Investor Prot. Corp.*, 503 U.S. 258, 266 (1992)(noting the "unlikelihood that Congress meant to allow all factually injured plaintiffs to recover").

The Court need not reach the RICO "tie breaker" to interpret the meaning of "business or property." It was clear at the time Congress adopted the phrase from antitrust law into RICO. *Hawaii v. Standard Oil Co.*, 405 U.S. 251, 264 (1972); *accord Reiter v. Sonotone Corp.*, 442 U.S. 330, 339 (1979)(in the antitrust laws, "[t]he phrase 'business or property' also retains restrictive significance . . . . Congress must have intended to exclude some class of injuries by the phrase 'business or property'"). Moreover, contrary to Respondent's and amici's assertions, the *Hawaii* decision was not some "paradigm shift" in law that surprised legal scholars and legislators alike.[13] Instead, it demonstrates the interpretation of "business or property" existing at exactly the time Congress considered and passed RICO: "[u]nless the concepts of business or property are expanded well beyond traditional usage, the general economy of a region cannot be regarded as property in possession of the residents individually or publicly." *Hawaii v. Standard Oil Co.*, 431 F.2d 1282, 1285 (9th Cir. 1970); *accord Hawaii*, 405 U.S. at 264 (if "business or property" is to include sovereign interests "we should insist upon a clear expression of a congressional purpose to make it so") and at 262 ("Congress had many means at its disposal to penalize violators. It could have, for example, required violators to compensate federal, state, and local governments for the estimated damage to their respective economies caused by the violations. But, this remedy was not selected").

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[13] *E.g.*, amici brief at 15 n.3 (accusing Petitioners of "playing 'gotcha'").

Had Congress not intended to limit RICO standing, it would have allowed standing for any "injured" individual or entity. Instead, Congress limited "person" to "any individual or entity capable of holding a legal or beneficial interest in property."[14] It then limited standing to any "person injured in his business or property." As amici recognize, "'business or property' means just what it says, and nothing more or less." Amici brief at 7. Ignoring this wisdom, amici say "business" means "government," and they join Respondent in arguing "property" means everything. Congress knew better.

B. Antitrust case law guides RICO interpretation.

The RICO language at issue here came straight out of antitrust law, unchanged. As this Court has confirmed:

> [C]ongressional use of the [Sherman Act] § 7 language in § 4 [of the Clayton Act] presumably carried the intention to adopt 'the judicial gloss that avoided a simple literal interpretation' . . . . The reasoning applies just as readily to § 1964(c). We may fairly credit the 91st Congress, which enacted RICO, with knowing the interpretation federal courts had given the words earlier Congresses had used first in § 7 of the Sherman Act, and later in the Clayton Act's § 4. It used the same words, and we can only assume it intended them to have the same meaning that courts had already given them.

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[14] 18 U.S.C. § 1961(3).

Holmes, 503 U.S. at 268 *citing Associated Gen. Contractors of Cal., Inc. v. Carpenters*, 459 U.S. 519, 534 (1983)(internal citations omitted). Antitrust precedent confirms that injury to sovereign interests falls outside the range of injuries cognizable under RICO. Respondent's and amici's argument that this Court should ignore its historic reliance on antitrust law to guide RICO interpretation must be rejected.

C. A sovereign interest in uncollected taxes owed by non-litigant third parties is neither "business" nor "property."

1. The phrase "business or property" must be read in the disjunctive.

Respondent does not dispute that the disjunctive "or" in the phrase "business or property" requires both "business" and "property" to be given their independent and ordinary significance. *Cf. Reiter*, 442 U.S. at 338-39.

2. Uncollected taxes owed by third parties are not an injury to business.

Respondent all but concedes that it alleged no injury to its "business:" it does not separately address the issue and refers throughout its brief primarily to alleged injury to its "property" alone. *E.g.*, Response at 15, 16, 21, 24, 25.[15] Amici (citing only the Oxford English Dictionary) include a one paragraph argument that "a governmental entity engages in 'business' when

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[15] But see Response at 1.

it performs its ordinary work." Amici brief at 7. Neither addresses Petitioners' case citations in the opening brief. *E.g., Waldron v. British Petroleum Co*., 231 F. Supp. 72, 86 (S.D.N.Y. 1964). Moreover, this Court consistently has distinguished between government as sovereign and government acting in a business capacity. *E.g.*, *Camps Newfound / Owatonna v. Town of Harrison,* 520 U.S. 564, 594 (1997)("Maine's tax exemption . . . must be viewed as action taken in the State's sovereign capacity rather than a proprietary decision"); *Chattanooga Foundry & Pipe Works v. City of Atlanta*, 203 U.S. 390, 396 (1906)(city "was injured in its property, at least, if not in its business of furnishing water"). Had Congress understood "business" to mean "government," it surely would have said so. *Cf. Hawaii*, 405 U.S. at 264 (if "business or property" is to include sovereign interests "we should insist upon a clear expression of a congressional purpose to make it so").

3. Uncollected taxes owed by third parties are not an injury to property.

Respondent admits taxation is an incident of sovereignty and not a property right. Response at 25.[16] Amici's "19th Century" claims notwithstanding, this Court continues to recognize the distinction. *Cleveland v. United States*, 531 U.S. 12, 23-24 (2000)(distinguishing between federal government's role as sovereign and as property holder).

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[16] *Bresson v. Comm'r*, 213 F.3d 1173, 1178 (9th Cir. 2000)("the right to collect taxes is among the most basic attributes of sovereignty").

The injury Respondent seeks to vindicate is not an interest in money, a choate tax obligation, or even an unperfected tax lien, but instead the sovereign "opportunity" to collect taxes. Response at 16 (the "ability to collect" tax revenue is "the City's property"); City of New York Br. Opp'n to Petition for Writ of Certiorari at 15 ("Petitioners did not owe the City taxes, rather, they defrauded the City out of an opportunity to collect taxes from those who did owe them"). Nevertheless, Respondent argues that because sovereign tax authority can be exercised *to create* a property right, the sovereign opportunity to tax *is itself* RICO "property." Respondent is incorrect.

The sovereign "opportunity" to collect a tax can be used to create a tax "debt" by means of an assessment. Michael I. Saltzman, *IRS Practice And Procedure, Liens And Levies*, Para. 14.01, (2nd ed., Warren Gorham & Lamont 2002) ("*Assessment creates* quite a different kind of debt from the one a debtor owes to the general creditor" (emphasis supplied)). Assessment is "the calculation or recording of a tax liability." *United States v. Galletti*, 541 U.S. 114, 122 (2004). In *Galletti*, Justice Thomas, writing for a unanimous Court, discussed assessment methods, including self-assessment (required under Respondent's cigarette possession tax):

> The Federal tax system is basically one of self-assessment, whereby each taxpayer computes the tax due and then files the appropriate form of return along with the requisite payment. . . . Where the taxpayer fails to file the form of return or miscalculates the tax due, as in this case, the Secretary can assess all taxes (including interest, additional amounts,

> additions to the tax, and assessable penalties), by recording the liability of the taxpayer in the office of the Secretary. In other words, where the Secretary rejects the self-assessment of the taxpayer or discovers that the taxpayer has failed to file a return, the Secretary calculates the proper amount of liability and records it in the Government's books.

Id. at 122 (internal quotations and citations omitted). *See also Hibbs v. Winn*, 542 U.S. 88, 117 (2004)(Kennedy, J., dissenting)(The recordkeeping that equates to the determination of taxpayer liability on the State's tax rolls is the assessment, whatever the method").

The assessment is not the sovereign (non-property) "opportunity" to tax. Instead, it is the mechanism used to create a property interest:

> Some machinery must be provided for applying the rule [of taxation] to the facts in each taxpayer's case, in order to ascertain the amount due. The chosen instrumentality for the purpose is an administrative agency whose action is called an assessment . . . . Once the tax is assessed the taxpayer will owe the sovereign the amount when the date fixed by law for payment arrives.

Bull v. United States, 295 U.S. 247, 259 (1934); *cf. United States v. New Britain*, 347 U.S. 81, 86 (1954)(rejecting the notion that "a State could affect the standing of federal liens, contrary to the established doctrine, simply by causing an inchoate lien to attach at some arbitrary time even before the

amount of the tax, assessment, etc., is determined"). Until assessment, the sovereign interest is inchoate. *New Britain*, 347 U.S. 81, 84 (1954)). An inchoate interest "affords no definite or enforceable property right." *Austin v. Bisbee*, 855 F.2d 1429, 1436 (9th Cir. 1988)(citation omitted); *cf. United States v. Pioneer Am. Ins. Co.*, 374 U.S. 84, 89 (1963)(the sovereign's interest in tax income is inchoate until "there is nothing more to be done to have a choate lien--when the identity of the lienor, the property subject to the lien, and the amount of the lien are established").

Manning v. Seeley Tube & Box Co., 338 U.S. 561 (1950) is not to the contrary. There the Court held that the point at which the Commissioner could charge interest on a tax deficiency is the date of self-assessment when "the original return was to be filed." *Id*. at 565. The Court was not addressing sovereign "opportunity" to tax, but rather a complex section of the federal carry-back provisions.[17] In *Manning*, the self-assessment created a debt upon which interest could accrue, with the amount of interest determined "when the Commissioner assesses a deficiency."

Assessment, for purposes of a possessory tax, does not occur upon taking of possession. As this Court has recognized:

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[17] *Id.* at 567-68 ("Although it is true that for many purposes the carry-back is equivalent to a *de novo* determination of the tax, our conclusion that this section does not retroactively alter the duty of a taxpayer to pay his full tax promptly is amply supported by § 3771 (e) of the Code. That section, an integral part of the carry-back provision, prohibits a taxpayer who does pay a tax which is subsequently abated by a carry-back from claiming interest from the Government for the intervening period").

> Although [Montana's tax] purports to be a species of property tax--that is, a 'tax on the possession and storage of dangerous drugs,' -- it is levied on goods that the taxpayer neither owns nor possesses when the tax is imposed. Indeed, the State presumably *destroyed* the contraband goods in this case before the tax on them was assessed.

Department of Revenue v. Kurth Ranch, 511 U.S. 767, 783 (1994)(citations omitted emphasis in original). Instead, assessment takes place upon either self-assessment, or government action to assess. The possessory tax law at issue here provides for both. *See* Section II(C)(4), *infra*.

No one disputes Respondent's sovereign power to impose possessory taxes on its residents. But until that power is exercised through assessment, no "property" interest is created. *Cf. Cleveland*, 531 U.S. at 23 (2000)("Even when tied to an expected stream of revenue, the State's right of control does not create a property interest"). This analysis applies to Respondent's argument by analogy to the Contraband Cigarette Trafficking Act ("CCTA"). 18 U.S.C. § 2341 *et seq*. Specifically, Respondent claims that by including the CCTA as a RICO predicate offense, Congress included injury to sovereign interests in RICO's existing "injury to business or property" standing limitation. Yet CCTA does not impose payment of taxes due as a penalty. 18 U.S.C. § 2344. And contrary to Respondent's claim, CCTA's legislative history confirms it was added as a RICO offense not to remedy injury to sovereign "opportunity," but instead to provide "additional statutory basis for the Department of Justice to interdict organized cigarette

racketeering." H.R. Rep. 95-1629 at 5 (1978). Much more instructive on the issue is that Congress has never included "tax evasion" as a RICO predicate crime. 18 U.S.C. § 1961.

Respondent's citation to *Pasquantino v. United States*, 544 U.S. 349 (2005) is similarly flawed. In *Pasquantino* this Court "express[ed] no view on the related question whether a foreign government, based on wire or mail fraud predicate offenses, may bring a civil action under the Racketeer Influenced and Corrupt Organizations Act (RICO) for a scheme to defraud it of taxes." *Id*. at 355 n.1. Courts that have addressed the issue have dismissed such RICO claims. *Attorney General of Canada v. R. J. Reynolds Tobacco Holdings, Inc*., 268 F.3d 103, 106 (2d Cir. 2001)(Canada cannot bring civil RICO suit for scheme to defraud it of taxes); *Republic of Honduras v. Philip Morris Cos*., 341 F.3d 1253, 1255 (11th Cir. 2003)(same with respect to other foreign governments).[18] Instead, *Pasquantino* was a criminal RICO prosecution for smuggling brought by federal prosecutors against individuals who did not pay Canadian taxes. It was not an attempt to rectify lost sovereign "opportunity" to collect taxes from non-litigant third parties, and civil RICO's "injury to business or property" limitation was not an issue.[19] As Respondent notes, in *Pasquantino* (decided in 2005) the Court cited in a

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[18] The decisions in *Canada* and *Honduras* were based on the revenue rule, which bars enforcement of foreign tax laws. Neither addressed RICO claims to collect taxes from a party who never owed them to begin with.

[19] *Cf. City of New York*, 541 F.3d at 459 n.2 (Winter, J., dissenting).

parenthetical the definition of property in Black's Law Dictionary Fourth Edition (1951): "extend[ing] to every species of valuable right and interest." 544 U.S. at 356. However, the first definition of "property" in the Eighth Edition of Black's Law Dictionary (1999) is: "The right to possess, use, and enjoy a determinate thing . . .; the right of ownership," noting:

> The law of property is the law of proprietary rights *in rem*, the law of proprietary rights *in personam* being distinguished from it as the law of obligations. According to this usage a freehold or leasehold estate in land, or a patent or copyright, is property; but a debt or the benefit of a contract is not.

Id. citing John Salmond, *Jurisprudence* 432-24 (Glanville L. Williams ed., 10th ed. 1947).[20] This distinction is consistent with the uniform rejection of personal injury claims as not being "property" for purposes of RICO standing. *Magnum v. Archdiocese of Phila.*, 253 Fed. Appx. 224 (3rd Cir. 2007); *Evans v. City of Chicago*, 434 F.3d 916 (7th Cir. 2006); *Diaz v. Gates*, 420 F.3d 897 (9th Cir. 2005)(*en banc*); *cf. Reiter*, 442 U.S. at 339 ("The phrase 'business or property'

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[20] Respondent also cites Websters (at 21). Webster's Third New International Dictionary, Unabridged, 2002 (available on the Internet) contains a definition consistent with the 1999 definition of property in the current Black's Law Dictionary: "2 a : something that is or may be owned or possessed: wealth, goods; specifically: a piece of real estate" and "2 c : something to which a person has a legal title: an estate in tangible assets (as lands, goods, money) or intangible rights (as copyrights, patents) in which or to which a person has a right protected by law."

also retains restrictive significance. It would, for example, exclude personal injuries suffered").[21]

Similarly flawed is amici's attempted reliance on a pending yet unrelated case in which amicus Indiana "used the federal RICO statute to sue former East Chicago Mayor Robert Pastrick." Amici brief at 1, 29-30. The propriety of this argument is questionable. *Dow Chemical Co. v. United States*, 2002 U.S. Dist. LEXIS 11657, at *3-4 (E.D. Mich. May 24, 2002)(amicus "ought not to be permitted to relitigate its own lawsuit").[22] Moreover, Indiana's alleged RICO predicate crime involved theft of money, not lost sovereign "opportunity" to collect that money.[23] Amici brief at 30. Nothing in this case will impair any sovereign from bringing civil RICO claims for "public corruption" that otherwise meet RICO's standing requirements. *Cf. Wilkie v. Robbins*, 551 U.S. 537, 564

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[21] Respondent and amici do not address the argument (Opening brief at 25) that "opportunity" to collect taxes is nothing more than an "expectation" interest that does not qualify as injury to "business or property." *Holmes*, 503 U.S. at 279 (O'Connor, J., concurring in part)("the requirement of injury in one's 'business or property' limits the availability of RICO's civil remedies to those who have suffered injury in fact"); *McLaughlin v. Am. Tobacco Co.*, 522 F.3d 215, 228 (2d Cir. 2008); *Heinold v. Perlstein*, 651 F. Supp. 1410, 1412 (E.D. Pa. 1987).

[22] *See also American Satellite Co. v. United States*, 22 Cl. Ct. 547, 549 (Cl. Ct. 1991)(amicus "is thus not a disinterested stranger offering to illuminate a legal issue. . . . [T]he implication is that [amicus'] real interests are as a litigant, not as a friend of the court").

[23] *Indiana v. Pasterick*, No. 3:04-cv-00506-JTM-CAN (N.D. Ind.). Doc. 1 (complaint) at 39, Paragraph VII (B) entitled: "The Predicate Crimes – Violations of 18 U.S.C. Section 2314."

(2007) (extortion involves harm of public corruption by the sale of public favors for private gain). Moreover, amicus Indiana's fear that judgments in its unrelated case "would be vulnerable to attack" misses the point: if based on misapplication of law they should be "vulnerable to attack." Yet that collateral issue is not properly before the Court. Instead, the issue properly before the Court is Respondent's lack of standing to sue a business that never owed it taxes, based on allegations that a sovereign "opportunity" to tax could have yielded unassessed future funds in unspecified amounts from unknown non-party taxpayers for unidentified possession of unknown quantities of cigarettes.

4. The sovereign "opportunity" to collect taxes is not property under New York law.

Respondent confirms that property interests are created and defined by state law, then argues that under New York law, "money is property," quoting the following:

> A city or village *holds the proceeds of taxation* as its *corporate property*. It may use *the moneys received* as it pleases for purposes of local government or for any other purpose *within its corporate powers*.

Response at 24 *citing and quoting Village of Kenmore v. County of Erie*, 252 N.Y. 437, 442 (1930)(emphasis supplied). No one disputes that money received from an assessed tax debt is property. Instead, it is the sovereign "opportunity" to tax, which is not "property" under federal or New York state law that is at issue.

As noted in Section II(C)(3), assessment is required to create a property interest. Respondent's possessory tax requires self-assessment.[24] When a person does not self-assess, there is no assessment and no "property" interest. Yet the government does not assess at this point. Instead, "the commissioner of taxation and finance shall determine the amount of tax due." N.Y. Tax Law § 478; *see also* N.Y. COMP. CODES R. & REGS. tit. 20 § 79.1 (a)-(b). There follows a lengthy process including taxpayer rights to petition for a hearing and further appeal. *Id.* Not until this process is completed is the assessment final and the tax "choate" under New York law. *Cf. Board of Managers v. Pickett*, 159 Misc. 2d 1076, 1078 (N.Y. Sup. Ct. 1994)("A state lien is considered 'choate' when it is perfected in the sense that there is nothing more to be done to have a choate lien" (*citing and quoting New Britain*, 347 U.S. 81, 84 (1954)). Where, as here, state law is specific as to the assessment process, that process must be completed before the tax becomes choate:

> As a result of these state law provisions, we hold that the amounts of the state tax liens at issue here were not established on the date the returns were filed and that state tax liens were therefore not perfected and choate on that date. The returns filed by the taxpayer had not been examined, the taxes owed had not been determined by the commissioner, and the delinquency penalties and interest had not been

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[24] N.Y. COMP. CODES R. & REGS. tit. 20 § 74.5 (b)(2) (2009); *see also* N.Y. Tax Law §§ 471-a - 471-c.

> computed and added to the amount of the tax, all of which is required under state law.

Minnesota v. United States, 184 F.3d 725, 730 (8th Cir. 1999).

Not only were Respondent's potential tax claims never choate, and therefore never "property," state law confirms Respondent's "opportunity" to collect also is not property. *State v. Barclays Bank of N.Y., N.A.*, 76 N.Y.2d 533, 540-541 (1990)(where taxpayer's accountant misappropriated checks payable to State for taxes, "[t]he checks were never actually or constructively delivered to plaintiff. It therefore never acquired a property interest in them and cannot be said to have suffered a loss")(opening brief at 24, ignored by Respondent and amici).

D. A municipality is not a "person" as defined by RICO when the municipality seeks to recover for injury, not to "business or property," but instead to a sovereign interest.

Instead of addressing whether it is a "person" for purposes of a RICO claim *based on injury to sovereign interest*, Respondent argues that the issue is "belated," and in any event irrelevant because Respondent sometimes can be a "person" as defined in RICO. Both arguments are incorrect.

First, Respondent's lack of RICO standing cannot be waived. *United States v. Hays*, 515 U.S. 737, 742 (1995). Second, "the source of parties' standing to bring the actions must coincide with the basis on which subject-matter jurisdiction is asserted." *White*

Mountain Apache Tribe v. Williams, 810 F.2d 844, 865 n.16 (9th Cir. 1985), *cert. denied*, 479 U.S. 1060 (1987). Petitioners do not argue that government is never a "person" with RICO standing. The argument, which Respondent fails to address, is that because Congress limited "person" to individuals or entities capable of owning "property," Respondent is only a "person" for RICO standing when seeking to recover for an injury to "property." It is not a "person" when it alleges injury to a non-property sovereign interest.

E. Amici's "commercial injury" argument is misplaced.

Amici claim to "focus [their] brief on the reasons why RICO should not be read to require a 'commercial' injury," arguing that such a reading would make RICO inapplicable to losses from government bank accounts through "misappropriation, conversion and embezzlement." Amici brief at 5. To the contrary, "non-commercial" in the context of the issue presented here relates to sovereign (non-property) as opposed to corporate (property) interests. *See United States v. Laton*, 352 F.3d 286, 312 (6th Cir. 2003)("a public and sovereign service . . . will rarely (if ever) be deemed 'actively' 'commercial' in any traditional sense of the terms"). It is beyond dispute that government acts both in a "sovereign," and in a commercial non-sovereign, capacity. *United States v. California*, 507 U.S. 746, 757 (1993). Addressing this "commercial versus sovereign" distinction, this Court has stated:

> Even when tied to an expected stream of revenue, the State's right of control does not create a property interest any more than a law licensing liquor sales in a State that levies a

> sales tax on liquor. Such regulations are paradigmatic exercises of the States' traditional police powers.

Cleveland, 531 U.S. at 23 (2000); *see also Hawaii*, 405 U.S. at 264-65.[25]

That distinction does not affect RICO claims arising from misappropriation, conversion and embezzlement, however, as none involves taking of sovereign "opportunities." *E.g.*, *Agency Holding Corp. v. Malley-Duff & Assoc. Inc.*, 483 U.S. 143, 149 (1987)(noting RICO "racketeering activity" includes state law felonies and violations of federal statutes prohibiting bribery, embezzlement, obstruction of justice, and interstate transportation of stolen property).

F. Petitioners Did Not Advance a "Floodgates" Argument.

Amici dedicate a significant portion of their argument to propping up, then knocking down a RICO "floodgates" argument that Petitioners never advanced.[26] Nevertheless, placing amici's floodgates

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[25] "Support for this reading of § 4 is found in the legislative history of 15 U. S. C. § 15a, which is the only provision authorizing recovery in damages by the United States, and which limits that recovery to damages to 'business or property.' The legislative history of that provision makes it quite plain that the United States was authorized to recover, not for general injury to the national economy or to the Government's ability to carry out its functions, but only for those injuries suffered in its capacity as a consumer of goods and services."

[26] Although Judge Winter criticized the inappropriate expansion of mail and wire fraud concepts inherent in the decision now

argument in context, nineteen States have told this Court that if it allows RICO standing for injury to sovereign interests, they stand ready to press such claims. If ever a floodgates argument were to gain traction this would be the appropriate case.

III. New York City Does Not Have RICO Standing Because Its Alleged Injury Is Indirect.

A. Only directly injured parties have civil RICO standing.

Standing under RICO is determined by proximate causation, not actual "but for" causation. *Holmes*, 503 U.S. at 265-66. Indirect claims do not confer standing. *Anza*, 547 U.S. at 460.

B. Injury to government in its sovereign capacity is always indirect.

The only response offered to this section of the opening brief is Respondent's incorrect claim that it is "a rehash" of the "injury to business or property" argument. Response at 42. Therefore, the argument in the opening brief needs no supplementation, other than to note that Respondent tendered no response to Petitioners' discussion of the "zone of interests" analysis articulated by Justice Scalia in his concurring opinion in *Holmes*:

> The phrase "any person injured in his business or property by reason of" the unlawful activities

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before this Court, that is not a RICO "floodgates" issue. *City of New* York, 541 F.3d at 459-60.

> makes clear that the zone of interests does not extend *beyond* those injured in that respect – but does not necessarily mean that it includes *all* those injured in that respect. Just as the phrase does not exclude normal judicial inference of proximate cause, so also it does not exclude normal judicial inference of zone of interests.

503 U.S. at 288 (Scalia, J., concurring in the judgment)(emphasis in original).

C. New York City's derivative injuries are speculative and too indirect to meet RICO standing requirements.

Respondent alleges that Petitioners injured its "opportunity" to collect taxes in two ways: (1) City residents were misled as to their possessory tax obligations because websites stated "sales are tax free" and "no tobacco taxes;" and (2) the City did not get lists of residents who bought cigarettes because no lists were sent by Hemi to the State. Response at 1, 5, 42.[27] As recognized by Judge Winter, and confirmed by the New York Court of Appeals under the same factual allegations, neither source of injury is direct, and both are speculative.

As to the first alleged injury, commercial speech as to sales and tobacco taxes cannot be a direct cause of

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[27] This second "source" of injury transforms Respondent's claimed RICO predicate act to one based on the Jenkins Act, which is not a criminal statutory predicate act under RICO. *See City of New York*, 541 F.3d at 459 (Winter, J., dissenting).

a taxpayer's failure to honor possessory tax obligations. *Cf. United States v. Boyle*, 469 U.S. 241, 252 (1985)("The failure to make a timely filing of a tax return is not excused by the taxpayer's reliance on an agent, and such reliance is not 'reasonable cause' for a late filing"). Moreover, the response itself confirms the indirect and speculative nature of the City's first alleged source of injury. Footnote 8 on page 8 of the response confirms that even "in instances when the City had received information that identified Internet cigarette purchases," it collected less than 55 cents on every dollar of taxes allegedly owed, receiving responses from only two-thirds of the City residents from whom it tried to collect. The law also contains payment exemptions.[28] As a result, it is improper to assume, as Respondent argues (at 40) and as opined by the Second Circuit Court of Appeals, that Respondent's damages are not speculative because they simply are "a specific dollar amount for each pack of cigarettes sold." That calculation ignores Respondent's admitted inability to collect all taxes, and the cost of tax collection. As Judge Winter noted:

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[28] Contrary to Respondent's claim, New York City's use tax exemption for possession of less than four hundred cigarettes does not contain an exclusion if the cigarettes were "shipped into the City by mail." Response at 49. Instead, the exemption applies to 400 cigarettes "on or in the possession of, any person." N.Y.C. Admin. Code § 11-1302(b)(1). Any other reading would mean a person could have an unlimited number of exempt cigarettes "on or in their possession" so long as they were only "brought into the city" 400 at a time. *People v. McKelvey*, 234 N.Y.L.J. 121 (N.Y. Crim. Ct. 2005)(dismissing misdemeanor charge because "anyone in possession of less than four hundred cigarettes has committed no crime under the offense charged here").

> A concern of taxing authorities everywhere is balancing the costs of collection against the recoverable revenue, a matter of great significance where the taxpayers are, as here, anything but inclined toward voluntary compliance. Moreover, the state appears uninterested in enforcing the Jenkins Act and may not collate or maintain accurate records of reports from out-of-state vendors or reliably pass them along. City customers, large numbers of individuals owing relatively small amounts in taxes, may be hard to trace, may assert various defenses in cases based solely on Jenkins Act reports, and may easily use non-City addresses. Finally, as to *Holmes* factor (iii), the City hardly has greater incentive to enforce the Jenkins Act through RICO than Anza-like competitors who lose sales because of their rivals' sales tax evasion.

City of New York, 541 F.3d at 461 (Winter, J., dissenting); *see Holmes*, 503 U.S. at 273 ("the district court would first need to determine the extent to which their inability to collect . . . was the result of the alleged conspiracy . . . as opposed to, say, . . . poor business practices").

Respondent also confirms the exposure in this case to the type of multiple, duplicative recoveries condemned by this Court. Again in its footnote 8, Respondent concedes that "some" City residents wrote to indicate they were "misled" by the websites of other defendants (not petitioners). There would be nothing to prevent individual customers (even if not "misled" because reliance is not required) from themselves seeking to recover possessory tax payments, penalties

and interest from RICO defendants duplicative to those claimed by Respondent. Potential claims by competitors must also be added to the mix, all resulting in lawsuits, including class actions, threatening duplicative judgments as cautioned against by this Court in *Anza*. Moreover, the evidentiary nightmare identified in *Hawaii* would come to pass with individual tax debtors, competitors, state and local government all required to demonstrate their own damages, costs of collection or payment, collection or payment rates (here fifty five cents on the dollar), and that none of the sales were tax exempt. Defendants would be exposed to multiple recovery, perhaps trebled, if individual taxpayers, competitors and sovereigns succeeded.

These same defects infect Respondent's allegations of injury from its inability to get lists of resident customers from the State. In this respect, Respondent's claims rest not on mail and wire fraud, but on alleged violations of the Jenkins Act.[29] Moreover, this Court's decision in *Anza* is dispositive of this second alleged source of injury. There, this Court concluded that the plaintiff's injuries were not proximately caused by the defendants' actions because "[t]he cause of Ideal's asserted harms . . . is a set of actions (offering lower prices) entirely distinct from the alleged RICO violation (defrauding the State)." *Anza* at 458. That is exactly the same cause of harm asserted by Respondent here. Moreover, this alleged source of injury is even less proximate than the first,

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[29] "The only fraudulent acts alleged that sound in fraud, therefore, are the violations of the Jenkins Act." *City of New York*, 541 F.3d at 459 (Winter, J., dissenting). *See* footnote 4, *supra*.

because 1) even if the State had received those names, there is no certainty they would have been given to the City, and 2) even when the City has received names, it collected only pennies on the dollar as noted above. This is not a reliance issue, as Respondent incorrectly argues, but instead a proximate cause issue, which Respondent cannot avoid. Indeed, in holding RICO does not include a reliance element, this Court specifically underscored the continued vitality of the proximate cause requirement. *Bridge v. Phoenix Bond & Idem. Co.*, 128 S. Ct. 2131, 2142 (2008).

Finally, standing based on lost sovereign "opportunity" would result in exactly the harm cautioned against by Justice Breyer in his concurring opinion in *Anza*: "the source of the savings is, in my view, beside the point as long as the price cut itself is legitimate." 547 U.S. 487-88. *See also id*. at 486 ("I would read into the private treble-damages provision a 'proximate-cause' limitation that places outside the provision harms that are traceable to an unlawful act only through a form of legitimate competitive activity."). Hemi's "prices are lower because State and City taxes are not and will not be included in the price." Response at 49. But because Hemi did not owe or pay those taxes, they should not be included in the price. Respondent's tax collection from third parties does not impact Hemi's prices by a penny.

Instead, Justice Breyer's warning has come to pass. The fifty-two defendants listed on the Second Circuit's Opinion have won on every claim brought by Respondent save for the single issue before this Court. Yet today petitioner Kai Gachupin and his company stand alone in opposing Respondent. *Cf. Sedima v. Imrex Co*., 473 U.S. 479, 520 (1985)(Marshall, J.,

dissenting)(RICO cases against legitimate businesses, "take their toll; their results distort the market by saddling legitimate businesses with uncalled-for punitive bills and undeserved labels"); and at 526 (Powell, J., dissenting)("RICO has been interpreted so broadly that it has been used more often against respected businesses with no ties to organized crime, than against the mobsters who were the clearly intended target of the statute").

D. The New York Court of Appeals has confirmed that New York City's alleged injuries are indirect.

The New York Court of Appeals, based on the exact record before this Court, held Respondent's state consumer law claim was entirely derivative and therefore bared. Unable to distinguish this unanimous holding, Respondent raises a hypothetical argument regarding the New York State Attorney General, and a reliance argument based on *Bridge.* Neither addresses the New York Court of Appeals' unanimous holding that Respondent's "claimed injury, in the form of lost tax revenue, is entirely derivative of injuries that it alleges were suffered by misled consumers who purchased defendants' cigarettes over the Internet." *City of New York v. Smokes-Spirits.com, Inc.*, 12 N.Y. 3d 616, 622 (2009). Specifically, the New York Attorney General does have standing to sue under the state law at issue, as does the United States Department of Justice under criminal RICO and the Jenkins Act. Tellingly, no such suits have been brought. As to Respondent's second argument, the New York Court of Appeals' decision was not based on lack of reliance: the court specifically used the words "entirely derivative." Respondent's proximate cause

argument to this Court is based on exactly the same alleged injuries held to be "entirely derivative" by the New York State Court of Appeals.

IV. Conclusion.

The holding of the Second Circuit Court of Appeals that the City of New York has standing to pursue its RICO claims should be reversed.

Respectfully Submitted,

RANDOLPH BARNHOUSE
Counsel of Record
Luebben Johnson & Barnhouse LLP
7424 4th Street NW
Los Ranchos de Albuquerque, NM 87107
(505) 842-6123 (telephone)
(505) 842-6124 (facsimile)

Counsel for Petitioners