Boiler Room Fraud: An Operational Plan Utilizing the Injunction against Fraud Pursuant to 18 U.S.C. §1345

Robert M. Twiss

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Boiler Room Fraud: An Operational Plan
Utilizing the Injunction Against Fraud
Pursuant to 18 U.S.C. § 1345

Robert M. Twiss*

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I. INTRODUCTION

This paper addresses the impact of boiler room operations on both the public and law enforcement agencies and discusses a coordinated criminal and civil approach to the problem. Boiler rooms involve both regulated and unregulated investments. The products which may be promoted via boiler rooms are limited only by the imagination of the boiler room operator. Federal, state and local agencies at both the criminal and regulatory administrative level are involved in the investigation and prosecution of boiler room fraud.

II. SCOPE OF THE BOILER ROOM PROBLEM

In early 1982, the Permanent Subcommittee on Investigations of the United States Senate Committee on Governmental Affairs (the Subcommittee) held hearings during which it was disclosed that thousands of Americans are victimized each year by operators of boiler rooms engaged in commodity fraud.1 Witnesses before the Subcommittee estimated the annual consumer loss from such operations at approximately $200 million. The scope of the Subcommittee's investigation extended beyond the narrow area of commodities as defined in the Commodity Exchange Act2 into the areas of securities and business practices regulated by the Securities and Exchange Commission (SEC) and the Federal Trade Commission (FTC), as well as the unregulated investment market.

Following the enactment of the Futures Trading Act of 1982,3 the Subcommittee held a second round of hearings on commodity investment fraud.4 At that time, the staff of the Subcommittee reaffirmed

its 1982 finding that the public was losing more than $200 million per year in commodity investment fraud schemes, accounting for losses of over $1 billion between 1975 and 1982.\(^5\) Senator Warren Rudman stated that: "[A]fter chairing these hearings for a couple of days and last year, . . . my own estimate at this point is that people of this country are being cheated out of a sum of money somewhere in excess of a half billion dollars annually."\(^6\) Witnesses estimated that as of 1984, there were some 8,000 boiler rooms in active operation nationwide, 200 of which are located in Dade and Broward Counties, Florida.\(^7\)

Witnesses also uniformly concluded that civil and administrative remedies were ineffective to curtail boiler room operators and that criminal prosecution was the only effective tool in this area.\(^8\) Witnesses also documented cases in which the cash hoards collected by boiler room promoters were moved into offshore bank accounts and real estate holdings in the Cayman Islands and in the Turks and Caicos Islands.\(^9\)

The Subcommittee further discovered that the majority of commodity fraud schemes are contrived by an identifiable cadre of recidivists who systematically generate fraudulent operations throughout the country. Principals and salesmen move freely from one operation to the next while avoiding prosecution and earning huge incomes. More stationary firms operating for only a short period of time may still succeed in bilking investors out of hundreds of thousands of dollars.\(^10\)

III. NATURE OF BOILER ROOM SCHEMES

Boiler room salesmen pitch (sell) anything and everything, from oil and gas leases to parcels of land, from tax shelters to industrial chemicals and specialty items.\(^11\) Since 1978 their most popular products have been gold, silver, platinum and copper.\(^12\) Precious metals promotions have developed as one significant area of fraud costing the public millions of dollars. The perpetrators of precious metals

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5. Commodity Investment Fraud II, supra note 4, at 145.
6. Id. at 88.
7. Id. at 22.
8. Id. at 17, 80, 83, 84, 87, 177.
9. Id. at 17, 44.
10. Id. at 145 (Staff Statement of the Permanent Subcommittee on Investigations of the Senate Committee on Governmental Affairs).
11. Id. at 177.
12. Id. at 173.
scams profess to offer valuable investments in gold, silver, or other metals in the form of bullion or coins, but typically such individuals are "precious metal dealers" in name only. Unlike reputable bullion dealers, these dealers do not possess the precious metals which they purport to sell nor do they have the ability or intention to obtain such metals to fulfill their obligations.

While programs utilized by different precious metals swindlers vary, the most common types of promotions involve either delayed delivery contracts or leverage-type contracts. In the former, customers pay for their order in full via credit card, wire transfer, or by mailing cash, checks, or money orders. More often, however, customers buy metals on leverage or installment contracts for future delivery. In the most legitimate of these fraudulent schemes, the dealer sells the gold at a set price per ounce with delivery set at some date in the future. The buyer is led to believe that the dealer completed the purchase on that day and is holding the buyer's gold. The dealer will hope for a falling market in gold so he can cover the purchase at a lower price in the spot market at the time of delivery. The dealer would then pocket the difference between the sales price and the cover price. If the price of the gold increases between the day of purchase and the day of delivery, the dealer goes bankrupt. In the more typical case, however, the dealer sells gold for future delivery and simply steals 100% of the purchase price. Because of the time delay between the purchase date and scheduled delivery date, the dealer can make his money and be long gone before victims become aware that they have been defrauded.

A second area of fraud very popular with boiler room swindlers involves oil and gas leases. The Bureau of Land Management of the United States Department of the Interior administers public auctions at which it sells drilling and mineral rights to certain parcels of public land. These sales involve land which the government has determined to be either unlikely to contain valuable minerals or to contain minerals which cannot feasibly be captured. The statistical likelihood of any individual investor winning the lease rights to a valuable parcel is extremely small. A number of promoters represent to investors that for a fee the promoter can substantially increase, or even guarantee the chances of winning such a worthwhile lease. Promoters often represent that the parcel is immediately adjacent to a proven reserve, when in fact, it is miles from any established reserve. The promoters frequently represent that major oil companies will be climbing over each other competing to buy the parcels from the investors, when they know that the major oil companies have no interest whatsoever in the affected parcels. Such promoters will also sell interests in land which they do not own, or sell the same parcel many times over. In one particular case, a promoter formed a limited part-
nership among investors to drill for coal and other minerals on a parcel of land which he had leased from the government. Unfortunately, in his lease with the government, all rights to coal and other minerals were retained by the United States.\textsuperscript{13}

A third area of fraud conducted by boiler rooms is the sale of inexpensive and defective goods not conforming to the seller's description which induced the buyer to make the purchase. A typical example involves boiler room salespeople contacting business people and advising them that they have been selected to win a valuable prize for which only business people are eligible. In order to establish that the winner really was a business person, one would only need to buy a quantity of ball point pens with the business name and telephone number printed thereon. After receipt of the victim's payment, the promoter might send nothing, or send a prior victim's pens, or even send cheap pens with the victim's name and telephone number. Usually, the victims will not receive the prize which induced them to buy the pens in the first place. If a victim does receive a prize, the value of the prize and the pens together will not equal the amount which the victim paid.

The prior discussion describes only three contemporary examples of popular fraudulent schemes. They only serve to illustrate the type of activity conducted by boiler room operators. There is no limit to the products which might form the basis for the operator's promotions. Usually, promoters will target any product which the media has recently discussed as a good investment. The only limit upon the products which serve as the basis for boiler room operations is the imagination of the con artist running the boiler room.

IV. OPERATION OF THE BOILER ROOM

A boiler room transaction is nothing more than a fraudulent sale of an investment to the public by high pressure telephone sales techniques. Boiler rooms are typically operations which are created and managed by career con artists and designed to prey upon the investing public. The modi operandi of a boiler room operation are: 1) the communication of false and fraudulent representations concerning the value or existence of the investment, product and/or service sold

... to the public; 2) the use of high-pressure sales techniques over the telephone; 3) the solicitation of victims outside the jurisdiction of the operation's situs; and 4) the ability to relocate quickly to avoid prosecution.

Setting . . . up [a boiler room] is cheap and it is simple. All it takes are desks, file cabinets, and a bank of telephones. Sales personnel work hours on the phones and they make huge sums of money.

The methodology is simple: Fast talk and extremely high sales pressure tactics. Inside the boiler room the din is numbing. Sales people are crammed into close quarters. The music is often blaring. And most of these operations, these fraudulent boiler room operations, are operated on the basis of what is known again in the vernacular in law enforcement as a Ponzi scheme.

It is very simple. Victims are talked into investing through promises of high profits and then they are strung along through delaying tactics, such as the issuance of small dividends or rebates. Only the most vocal complainants receive any money or metals.

The companies begin with prospect lists that they buy or that they may advertise. And the salesmen start with what is called the front speech. It is designed, simply put, to fan curiosity, interest, perhaps greed. The prospects that seem hot are then papered. That is to say they are sent a sales brochure with exaggerations frequently and misrepresentations. Next comes the follow-up call, usually a week or so later, then the drive call, then the takeover call, and finally the close, which is designed to get the check in the mail quickly.

The customers that they seek are customers whom they can derive repeat sales from. When the boiler room nears its breaking point, the salespeople make what are referred to as drop calls. That is to say they offer discounts and premiums such as free trips. And then comes the common scenario, what we again call in the vernacular the bust-out. The owner leaves town or perhaps he just moves down the block and opens up under a new name and starts up a scam all over again.14

Typically, the boiler room is a highly organized operation with management level personnel and a sales force which receives incentives such as money and/or drugs based upon the volume of sales. The salesmen are generally provided with written scripts, or "pitch-sheets" which are designed to entice the investor and provide persuasive answers to any questions the potential customer might have. These oral representations may be supplemented with professionally made written materials and glossy brochures which lend the operation an added appearance of respectability. Some boiler room operations are so large and profitable that they operate branch offices and others have become so sophisticated that they have turned to computerization of their financial records and customer lists.

A. Locations of Boiler Rooms

While no place is immune from boiler room operations, South Flor-
ida and Southern California are the capitals for such fraud for reasons including an abundance of willing and experienced "boiler room" salesmen, fair weather, low rents, wealthy investors and a fast lifestyle. Easy access to offshore banking and drugs coupled with competing claims to law enforcement resources due to high levels of violent crime and drug trafficking make South Florida an especially attractive haven for precious metals schemes.\textsuperscript{15}

Boiler room operators tend to solicit out-of-state customers so that there are no local complainants. When customers realize that they have been victimized, the agencies to which they complain generally find that the con artist is not present within the agency's jurisdiction. The boiler room operator counts upon the local law enforcement agency's natural hesitancy to pursue criminal activity in another state as well as the inability of the victim to locate the correct law enforcement agency within the operator's state in order to file a complaint. Thus, by spreading his fraudulent operations among a number of jurisdictions, the boiler room operator decreases the likelihood that any one law enforcement agency will recognize the magnitude of the fraud.

V. IMPACT OF THE REGULATORY AGENCIES

A number of federal, state, and local agencies have a regulatory interest in boiler rooms and commodity investment fraud. At the federal level, the agencies primarily involved are the Commodity Futures Trading Commission (CFTC), the Securities and Exchange Commission (SEC), the Federal Trade Commission (FTC), and to a lesser extent, the Internal Revenue Service (IRS). At the state level, the regulatory agencies which are involved tend to be the State Securities Commission, the State Corporations Commission and the Secretary of State's office.

The investigation and hearings conducted by the Permanent Subcommittee on Investigations from 1982 through 1984 demonstrated that boiler rooms have flourished because they have been able to take advantage of gaps in the federal-state law enforcement structure. At the state level, many of the regulatory agencies do not have jurisdiction over the type of activity conducted by boiler rooms. The criminal justice agencies are frequently hesitant to act because only isolated victims are found within their respective jurisdictions. As a

\textsuperscript{15} See \textit{id.} at 149 (Staff Statement of the Permanent Subcommittee on Investigations of the Senate Committee on Governmental Affairs).
result, the local agency often does not see the full extent of the criminal behavior. Even if the scheme is detected, the agency may hesitate to expend scarce prosecutorial and investigative resources on an out-of-state defendant. At the federal level, some of the principal agencies do not have a jurisdictional base from which to proceed against boiler rooms and others do not have the resources and/or expertise to proceed effectively.

A. Commodity Futures Trading Commission

The Commodity Exchange Act of 1974 created the CFTC as an independent regulatory agency to oversee the trading of commodity futures contracts. Prior to that time, the trading of futures contracts on agricultural commodities was regulated by the Department of Agriculture’s Commodity Exchange Authority. The CFTC has exclusive regulatory jurisdiction with respect to accounts, agreements (including any transaction which is of the character of, or is commonly known to the trade as, an “option”, “privilege”, “indemnity”, “bid”, “offer”, “put”, “call”, “advance guarantee”, or “decline guarantee”), and transactions involving contracts of sale of a commodity for future delivery, traded or executed on a contract market designated pursuant to section 7 of . . . title [7, U.S.C.] or any other board of trade, exchange, or market, and transactions subject to regulation by the Commission pursuant to section 23 of . . . title [7, U.S.C.] . . . .

“Commodity” is broadly defined in Title 7 of the United States Code, section 2 to include “all . . . goods and articles . . . and all services, rights, and interests in which contracts for future delivery are presently or in the future dealt in . . . .” The term “commodity” has “come to embrace a variety of financial instruments, precious metals, and natural resource items, such as petroleum, as well as domestic and international agricultural products.” The term “future delivery” as used in the definition of “commodity” does “not include any sale of any cash commodity for deferred shipment or delivery.”

In deciding whether a contract is one involving the sale of a commodity for future delivery, over which the CFTC has exclusive regulatory jurisdiction, or a purchase of a cash commodity for deferred delivery, over which the CFTC does not have jurisdiction, “no bright

17. Id. § 2 (1982). See also CFTC v. Co Petro Mktg. Group, Inc., 680 F.2d 573 (9th Cir. 1982) (agency agreements are not “cash forward contracts” within the meaning of the phrase “transactions involving contracts of sale of a commodity for future delivery” as used in 7 U.S.C. § 2).
18. Co Petro Mktg., 680 F.2d at 577 n.3.
20. Co Petro Mktg., 680 F.2d at 577 (for a deposit of a percentage of the purchase price, the customer appointed the company as agent to buy and later sell specified types and quantities of fuel for a set price).
line definition or list of characterizing elements is determinative.”21
The transaction must be analyzed under a “totality of the facts and
circumstances with a critical eye towards its underlying purpose.”22
The key issue is whether there is an expectation of delivery of the
actual commodity by the seller to the original contracting buyer. The
exclusion from CFTC jurisdiction will generally not apply if the com-
modities are sold merely for speculative purposes and there is no
expectation of actual delivery of the commodity to the original
contracting party.23

In some areas, it is not entirely clear whether an item is a commod-
ity future within the meaning of Title 7 of the United States Code, or
a security within the meaning of Title 15. The grant of exclusive ju-
risdiction to the CFTC over futures contracts involving intangible in-
terests created an “inevitable jurisdictional conflict with the SEC.”24
“The investment vehicle which would create the greatest jurisdic-
tional problem would be a contract of sale for future delivery of
broad-based stock indices, colloquially known as a ‘stock index fu-
ture.’ The CFTC’s new authority to regulate such investments was a
direct incursion on the SEC’s regulatory turf.”25

In 1981, the CFTC and SEC reached an agreement giving the
CFTC exclusive jurisdiction over the trading of futures contracts on
boards of trade. The agreement made the SEC the sole regulator of
securities options markets26 and the Futures Trading Act of 1982
codified the agreement between the two agencies.27 This statutory

21. Id. at 581.
22. Id.
23. Id. at 579. See also Merrill Lynch, Pierce, Fenner & Smith v. Curran, 456 U.S.
353, 387 (1982) (exclusive CFTC jurisdiction is not intended to affect implied causes of
action as well as other causes of action); Mallen v. Merrill Lynch, Pierce, Fenner &
Smith, 605 F. Supp. 1105, 1109-10 (N.D. Ga. 1985) (discretionary commodity account
giving broker authorization to speculate in “stock index futures” involves a “commod-
ity” rather than a “security” for purposes of administrative jurisdiction); NRT Metals,
1983) (cash forward contracts contemplate physical transfer of actual commodities and
not merely offsetting purchases). See generally Johnson, The Commodity Futures
Trading Commission Act: Preemption as Public Policy, 29 VAND. L. REV. 1, 11-16
(1976); Van Wart, Preemption and the Commodity Exchange Act, 58 CHI.-KENT L. REV.
657, 660-64 (1982).
25. Id.
27. 7 U.S.C. § 2(a) (1982) provides:
Notwithstanding any other provision of law—
1. This chapter shall not apply to and the [Commodity Futures Trading]}
split in jurisdiction means that in some cases it will be necessary to
determine whether to look to the CFTC and the commodities laws,
or to the SEC and the securities laws to determine which alternatives
to the fraud injunction pursuant to 18 U.S.C. § 1345 are available.

Sections 6 through 6p of the Commodity Exchange Act\(^28\) outline
what constitutes violations of the Act. Of particular interest in the
context of boiler room operations are the following: sections 6d of the
Act,\(^29\) which prohibits a person from engaging as a futures commis-
sion merchant or introducing a broker unless registered with the
CFTC; section 6n,\(^30\) which makes it unlawful for any commodity
trading adviser or commodity pool operator to make any use of the
mails or any means or instrumentality of interstate commerce in con-
nection with his/her business unless registered with the CFTC; and
section 6o,\(^31\) which makes it unlawful for a commodity trading advi-
sor, commodity pool operator, and any of their associates to use the
mails or any means or instrumentality of interstate commerce to use
any device or scheme to defraud any client or participant or to en-
gage in any transaction, practice, or course of business which operates
as a fraud or deceit upon any client or participant. Section 6o is simi-
lar to the mail and wire fraud provisions of the criminal code,\(^32\) the
anti-fraud provisions of the Securities Exchange Act of 1934,\(^33\) and
Rule 10b-5 of the Securities and Exchange Commission.\(^34\)

The CFTC is authorized to seek an injunction prohibiting conduct
which violates any provision of the Act or rule of the Commission:

Whenever it shall appear to the Commission that any contract market or
other person has engaged, is engaging, or is about to engage in any act or prac-
tice constituting a violation of any provision of this chapter [Commodity Ex-
change Act] or any rule, regulation, or order thereunder, or is restraining
trading in any commodity for future delivery, the Commission may bring an
action in the proper district court of the United States . . . to enjoin such act
or practice, or to enforce compliance with this chapter, or any rule, regulation

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\(^{29}\) Id. § 6d.
\(^{30}\) Id. § 6.
\(^{31}\) Id. § 6o.
\(^{34}\) 17 C.F.R. § 240.10b-5 (1983).
or order thereunder, and said courts shall have jurisdiction to entertain such actions ... Any action under this section may be brought in the district wherein the defendant is found or is an inhabitant or transacts business or in the district where the acts or practice occurred, is occurring, or is about to occur, and process in such cases may be served in any district in which the defendant is an inhabitant or wherever the defendant may be found. In lieu of bringing actions itself pursuant to this section, the Commission may request the Attorney General to bring the action ... 35

Under the Commodity Exchange Act, when the CFTC agrees to such a procedure, the Department of Justice or the United States Attorney can choose between the injunctions pursuant to Title 18 of the United States Code, section 1345,36 and Title 7 of the United States Code, section 13a-1,37 as a remedy for unlawful conduct by boiler room operators.

Once a violation of the Act has been shown, the party moving for injunctive relief need only show the existence of some reasonable likelihood of future violations.38 This determination is based upon the totality of the circumstances, including the defendant's past unlawful conduct.39 In actions "brought to enforce the requirements of remedial statutes such as [the Commodity Exchange] Act, the district court has broad discretion to fashion appropriate relief,"40 including relief ancillary to injunction, to effectuate the statutory purpose and policy of the Act. Among the types of ancillary relief which have been granted as a result of commodities violations are the appointment of a receiver,41 the temporary freezing of the violator's assets,42

39. Id. at 942-43 (injunction proper where unregistered commodities broker operated fraudulent pyramid scheme); see also CFTC v. Morgan, Harris & Scott, Ltd., 484 F. Supp. 669, 676 (S.D.N.Y. 1979) (injunctive relief under 7 U.S.C. § 13a-1 does not require showing of irreparable harm or lack of adequate remedy at law as does relief in private injunctive actions). Cf. CFTC v. Commodities Fluctuations Sys., Inc., 583 F. Supp. 1382, 1386 (S.D.N.Y. 1984) (injunction denied when evidence failed to show reasonable likelihood of continued violations).
40. CFTC v. Co Petro Mktg. Group, Inc., 680 F.2d 573, 583-84 (9th Cir. 1982); Morgan, Harris & Scott, 484 F. Supp. at 677 (quoting CFTC v. Muller, 570 F.2d 1296, 1300 (5th Cir. 1978)); see also CFTC v. Hunt, 591 F.2d 1211, 1223 (7th Cir.), cert. denied, 442 U.S. 921 (1979) (district court has power to compel disgorgement of profits from illegal commodities transactions and to enjoin publication of trading positions); Kelly v. Carr, 567 F. Supp. 831, 838-40 (W.D. Mich. 1983) (judgment ordering disgorgement and appointment of receiver in addition to permanent injunction in case of boiler room commodities fraud on "massive scale"); CFTC v. United States Metals Depository Co., 468 F. Supp. 1149, 1161-62 (S.D.N.Y. 1979) (granting of pre-sentence motion to withdraw guilty plea is within the sound discretion of the trial court).
41. Co Petro Mktg., 680 F.2d at 583-84; Morgan, Harris & Scott, 484 F. Supp. at 677; see also CFTC v. American Commodity Group Corp., 753 F.2d 862 (11th Cir. 1984)
and an accounting for any disgorgement of profits accumulated as a result of the unlawful conduct.43

B. Securities and Exchange Commission

The SEC was created by the Securities Exchange Act of 193444 as an independent, bipartisan, quasi-judicial agency of the United States Government. The laws administered by the Commission relate in general to the field of securities and finance, and seek to provide protection for investors and the public in securities transactions. Among the laws administered by the SEC are two which impact directly upon the operation of boiler rooms. They are the Securities Act of 193345 (Securities Act) and the Securities Exchange Act of 1934 (Exchange Act).46

The Securities Act has two basic objectives: (a) to provide investors with financial and other information concerning securities offered for public sale; and (b) to prohibit misrepresentation, decept, and other fraudulent acts and practices in the sale of securities.47 The Exchange Act extended the concept of investor protection by requiring disclosure of all relevant information about securities listed and registered for public trading on the national stock exchanges. The 1964 amendments to these Acts applied the disclosure and reporting provisions to the over-the-counter market.48

In testimony before the Subcommittee, Mr. John Fedders, former Director of the Enforcement Division of the SEC, indicated that the SEC does not have jurisdiction over most boiler rooms, and particularly not over those involving precious metals.

Though the Commission can bring enforcement actions in appropriate cases, restrictions on its jurisdiction would, in most instances, preclude its action. The Commission, as a general rule, does not have jurisdiction over precious metals dealers. Though dealers may in some instances sell the metals as part of a package that constitutes a "security"—most typically an "investment contract"—the Commission generally has no authority to regulate precious metals dealers, and can determine whether it has jurisdiction over a particular dealer only after a careful examination of that dealer's marketing plan. Consequently, there is no basis for systematic Commission regulation of metals

| 42. Sec. e.g., CFTC v. Skorupskas, 605 F. Supp. 923 (E.D. Mich. 1985); Morgan, Harris & Scott, 484 F. Supp. at 669. |
| 43. See, e.g., Co Petro Mktg., 680 F.2d at 573; Skorupskas, 605 F. Supp. at 923. |
| 48. Id. at 10. |
dealers, as there is for issuing companies, broker-dealers, investment companies, investment advisors and others in the securities industry.\footnote{Commodity Investment Fraud II, supra note 4, at 200.}

The Securities Act regulates public offerings of securities and prohibits offers and sales of securities which are not registered with the SEC, subject to exceptions provided by statute and regulations promulgated by the Commission. It further prohibits fraudulent or deceptive practices regarding the offer or sale of securities. In contrast, the Exchange Act applies to those securities which are already issued and outstanding.\footnote{D. Ratner, Securities Regulation § 2 (2d ed. 1984).} The key issue, therefore, is whether the items involved are securities. The Securities Act defines the term “security” to include:

any note, stock, treasury stock, bond, ... certificate of interest or participation in any profit-sharing agreement, ... investment contract ... fractional undivided interest in oil, gas or other mineral rights, or, in general, any interest or instrument commonly known as a “security,” or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing.\footnote{15 U.S.C. § 77b(1) (1982) (emphasis added). This term is also defined by the Exchange Act to include:
any note, stock, treasury stock, bond, debenture, certificate of interest or participation in any profit-sharing agreement or in any oil, gas, or other mineral royalty or lease, any collateral-trust certificate, reorganization certificate or subscription, transferrable share, investment contract, voting-trust certificate, certificate of deposit, for a security, ... or in general, any instrument commonly known as a "security"; or any certificate of interest or participation in, temporary or interim certificate for, receipt for, or warrant or right to subscribe to or purchase, any of the foregoing; but shall not include currency of any note, draft, bill of exchange, or banker's acceptance which has a maturity at the time of issuance of not exceeding nine months, exclusive of days of grace, or any renewal thereof the maturity of which is likewise limited. 15 U.S.C. § 78c(a)(10) (1982) (emphasis added).}

Boiler room operators will usually not promote stocks, bonds, or any other items described as a security in the Securities Act, with the possible exception of investment contracts and/or fractional undivided interests in oil, gas, or other mineral rights. “The mere sale and delivery of a precious metal is not the sale of a security for purposes of the federal securities laws. ... Consequently, unless a metals transaction involves an ‘investment contract’ or some other specified security the Commission has no jurisdiction over the transaction.”\footnote{Commodity Investment Fraud II, supra note 4, at 201.}

In \textit{S.E.C. v. W.J. Howey Co.},\footnote{328 U.S. 293 (1946). Defendants offered tracts of orange trees to investors along with exclusive access service contracts. The practical effect of this was to make purchasers investors in the large groves, not merely owners of small tracts. \textit{Id.}} the Supreme Court defined an investment contract as an investment of money in a common enterprise
with the profits from the investment to be derived solely from the efforts of others.54

There is some authority for the position that promotions of a limited class of boiler room operations might qualify as a security under the Securities Act.

The case law suggests that the sale of metals as part of a package together with particular services provided by the dealer may constitute a security. . . . To constitute an "investment contract," the efforts of the promoter or other person must be essential to the anticipated production of profits. There would be no investment contract if these persons performed merely ministerial functions unrelated to the production of profits. Thus, in the case of sales of precious metals, there probably would be no investment contract where the seller agreed merely to store or insure the metals of the purchaser.

In a precious metals transaction where the dealer represents itself as an expert in metals trading and offers to provide the purchaser with expert investment advice, such as when to buy and sell, the offer of advice arguably is material to the expected profit to be earned by the purchaser. This advice, together with other elements, may constitute sufficient managerial efforts to transform the commodity sale into a securities transaction.55

If it appears that the boiler room operator's sale of an interest in the product qualifies as both the sale of a commodity under the Commodity Exchange Act56 and an investment contract, and thus a security, under the Securities Act,57 the division of jurisdiction between the CFTC and the SEC58 may affect whether a cause of action arises under the commodities or securities laws.59 The grant of exclusive jurisdiction to the CFTC regarding commodity violations may deprive

54. Id. at 298-99. This test has since been modified by the circuit courts to allow them to find a security where some efforts are made by the investors to acquire or increase profits. See United Hous. Found., Inc. v. Forman, 421 U.S. 837, 852, reh'g denied, 423 U.S. 884 (1975) (holding that an investment contract is "an investment in a common venture premised on a reasonable expectation of profits to be derived from the entrepreneurial or managerial efforts of others."); SEC v. Glenn W. Turner Enter., Inc., 474 F.2d 476 (9th Cir.), cert. denied, 414 U.S. 821 (1973). The proper test is not the Howey test (solely from the efforts of others) but "a more realistic test, [which is] whether the efforts made by those other than the investor are the undeniably significant ones, those essential managerial efforts which affect the failure or success of the enterprise." Id. at 482; SEC v. Koscot Interplanetary, Inc., 497 F.2d 473 (5th Cir. 1974) (holding that a pyramid selling scheme constitutes an investment contract notwithstanding some efforts made on the part of investors).

55. Commodity Investment Fraud II, supra note 4, at 201-02 (statement by John Fedders).

56. Commodity Exchange Act § 2(a), 7 U.S.C. § 2 (1982). This section defines "commodity" as "wheat, cotton, rice, corn, oats, barley, rye, flaxseed, grain sorghams, mill feeds, butter, eggs, solanum tuberasum (Irish potatoes), wool, wool tops, fats and oils . . . and all services, rights, and interests in which contracts for future delivery are presently or in future dealt in . . . ." Id.


58. 7 U.S.C. § 2a (1982); see also supra note 24.

59. See, e.g., Mallen v. Merrill Lynch, Pierce, Fenner and Smith, 605 F. Supp. 1105 (N.D. Ga. 1985) (stock index futures are commodities and not securities, thus investor has no claim under federal or state securities laws).
the court of subject matter jurisdiction to entertain a petition for injunctive relief under the Securities Act.60

If the product being promoted by the boiler room operator is a security, the registration and anti-fraud provisions of the Securities Act and the Exchange Act are applicable. No security may be offered or sold to the public unless it is registered with the SEC or meets one of the exceptions to the registration requirement.63

Among the more prominent of those exceptions are transactions by any person other than an issuer, underwriter, or dealer, private

60. Id. at 1114.
62. Id. § 17(a), 15 U.S.C. § 77g (fraud in interstate transactions); id. § 11, 15 U.S.C. § 77k (material misstatement or omission in registration statement); id. § 12(2), 15 U.S.C. § 78 (manipulative or deceptive devices in purchase or sales); Rule 10b-5, 17 C.F.R. § 240.10b-5 (1987) (material misstatement or omission in purchase or sales).
63. Section 5 of the Securities Act prohibits the sale of unregistered securities. It provides:

(a) Unless a registration statement is in effect as to a security, it shall be unlawful for any person, directly or indirectly—

(1) to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to sell such security through the use or medium of any prospectus or otherwise; or

(2) to carry or cause to be carried through the mails or in interstate commerce, by any means or instruments of transportation, any such security for the purpose of sale or for delivery after sale.

(b) It shall be unlawful for any person, directly or indirectly—

(1) to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to carry or transmit any prospectus relating to any security with respect to which a registration statement has been filed under this title, unless such prospectus meets the requirements of section 10; or

(2) to carry or cause to be carried through the mails or in interstate commerce any such security for the purpose of sale or for delivery after sale, unless accompanied or preceded by a prospectus that meets the requirements of subsection (a) of section 10.

(c) It shall be unlawful for any person, directly or indirectly, to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to offer to sell or offer to buy through the use or medium of any prospectus or otherwise any security, unless a registration statement has been filed as to such security, or while the registration statement is the subject of a refusal order or stop order or (prior to the effective date of the registration statement) any public proceeding or examination under section 8.


placements, small offerings, and intrastate offerings. The anti-fraud provision of the Securities Act prohibits the use of the mails or any means of interstate transportation or communication to perpetrate a fraud upon a purchaser. Moreover, any willful violation of the Securities Act or any rule or regulation of the SEC promulgated pursuant to the Securities Act is a felony.

In addition to the registration and anti-fraud provisions of the Securities Act, the anti-fraud provision of the Exchange Act, section 10b, and the regulations thereunder, are particularly relevant to boiler room fraud. Section 10b provides:

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange . . . .

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such

65. Id. § 4(2), 15 U.S.C. § 77d(2). “The provisions of section 5 shall not apply to . . . (2) transactions by an issuer not involving any public offering . . . .” Id.

66. Id. § 3(b), 15 U.S.C. § 77c(b).

The Commission may from time to time by its rules and regulations, and subject to such terms and conditions as may be prescribed therein, add any class of securities to the securities exempted as provided in this section, if it finds that the enforcement of this title with respect to such securities is not necessary in the public interest and for the protection of investors by reason of the small amount involved or the limited character of the public offering; but no issue of securities shall be exempted under this subsection where the aggregate amount at which such issue is offered to the public exceeds $5,000,000.

Id. (emphasis added).


Any security which is a part of an issue offered and sold only to persons resident within a single State or Territory, where the issuer of such security is a person resident and doing business within or, if a corporation, incorporated by and doing business within, such State or Territory.

Id.

68. Id. § 17(a), 15 U.S.C. § 77q(a).

(a) It shall be unlawful for any person in the offer or sale of any securities by the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails, directly or indirectly—

(1) to employ any device, scheme, or artifice to defraud, or

(2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

Id.

69. Id. § 24, 15 U.S.C. § 77x, which provides:

Any person who willfully violates any of the provisions of this title or the rules and regulations promulgated by the Commission under authority thereof, or any person who willfully, in a registration statement filed under this title, makes any untrue statement of a material fact or omits to state any material fact required to be stated therein or necessary to make the statements therein not misleading, shall upon conviction be fined not more than $10,000 or imprisoned not more than five years, or both.

Id.

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rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.\textsuperscript{70}

The Commission has supplemented this by promulgating Rule 10b-5,\textsuperscript{71} which acts as a “catch-all” provision designed to deal with those fraudulent situations which are not specifically prohibited elsewhere. As one commentator stated:

It applies to any purchase or sale by any person of any security. There are no exemptions. It applies to securities which are registered under the 1934 Act, or which are not so registered. It applies to publicly-held companies, to closely-held companies, to any kind of entity which issues something that can be called a “security.” It even applies to “exempted securities,” as defined in SEA § 3(a)(12), (including federal, state and local government securities) which are specifically exempted from certain other provisions of the Act. Because of this broad scope, the rule may be invoked in many situations in which alternative remedies are made available (or are not made available) by applicable provisions of federal securities laws and state securities or corporation laws.\textsuperscript{72}

Rule 10b-5 is similar in concept and scope to the mail fraud and wire fraud provisions of the criminal code.\textsuperscript{73} Among the activities of

\textsuperscript{70} Exchange Act § 10(b), 15 U.S.C. § 78j(b) (1982).

\textsuperscript{71} 17 C.F.R. § 240.10b-5 (1987). This rule provides:

\begin{itemize}
\item It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
\item (a) To employ any device, scheme, or artifice to defraud,
\item (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of circumstances under which they were made, not misleading, or
\item (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.
\end{itemize}

\textit{Id.} \textsuperscript{72} D. RATNER, supra note 50, at 132.

\textsuperscript{73} 18 U.S.C. §§ 1341, 1343 (1982). Section 1341 provides:

Whoever, having devised or intending to devise any scheme or artifice to defraud, or for obtaining money or property by means of false or fraudulent pretenses, representations, or promises, or to sell, dispose of, loan, exchange, alter, give away, distribute, supply, or furnish or procure for unlawful use any counterfeit or spurious coin, obligation, security, or other article, for the purpose of executing such scheme or artifice or attempting so to do, places in any post office or authorized depository for mail matter, any matter or thing whatever to be sent or delivered by the Postal Service, or takes or receives therefrom, any such matter or thing, or knowingly causes to be delivered by mail according to the direction thereon, or at the place at which it is directed to be delivered by the person to whom it is addressed, any such matter or thing, shall be fined not more than $1,000 or imprisoned not more than five years, or both.

\textit{Id.} § 1341. Section 1343 provides:

Whoever, having devised or intending to devise any scheme or artifice to defraud, or for obtaining money or property by means of false or fraudulent pretenses, representations, or promises, transmits or causes to be transmitted by
a boiler room operation which would violate Rule 10b-5 are false statements about the assets of the corporation whose stock was being marketed, false statements regarding the projected selling price of the stock being sold, or a failure to disclose that the seller was engaged as a market-maker for the stock being sold. A willful violation of any provision of the Exchange Act or the regulations promulgated thereunder is also a felony.

The SEC is authorized by Congress to seek an injunction prohibiting conduct which violates any provision of the Securities Act, the Exchange Act, or the rules and regulations promulgated thereunder. Once a violation of the securities laws has been shown, the

means of wire, radio, or television communication in interstate or foreign commerce, any writings, signs, signals, pictures, or sounds for the purpose of executing such scheme or artifice, shall be fined not more than $1,000 or imprisoned not more than five years, or both.

Id. § 1343.

74. R. JENNINGS & H. MARSH, SECURITIES REGULATION 676-81 (4th ed. 1977); see also Chasins v. Smith, Barney & Co., Inc., 438 F.2d 1167 (2d Cir. 1970) (failure of broker to disclose market maker status is omission of material fact); Berko v. Securities and Exch. Comm’n, 316 F.2d 137 (2d Cir. 1963) (broker who knowingly relied upon long distance telephone solicitation to sell stock in company he did not know was operating at a loss and who mailed out brochures that he should have known were misleading was acting in a boiler room operation and caused employer to lose broker dealer license).


Any person who willfully violates any provision of this title (other than section 78dd-1 of this title), or any rule or regulation thereunder the violation of which is made unlawful or the observance of which is required under the terms of this chapter, or any person who willfully and knowingly makes, or causes to be made, any statement in any application, report, or document required to be filed under this title or any rule or regulation thereunder or any undertaking contained in a registration statement as provided in subsection (d) of section 78 of this title or by any self-regulatory organization in connection with an application for membership or participation therein or to become associated with a member thereof, which statement was false or misleading with respect to any material fact, shall upon conviction be fined not more than $100,000, or imprisoned not more than five years, or both, except that when such person is an exchange, a fine not exceeding $500,000 may be imposed; but no person shall be subject to imprisonment under this section for the violation of any rule or regulation if he proves that he had no knowledge of such rule or regulation.

Id.


(b) Whenever it shall appear to the Commission that any person is engaged or about to engage in any acts or practices which constitute or will constitute a violation of the provisions of this title or of any rule or regulation prescribed under authority thereof, it may in its discretion, bring an action in any district court of the United States, United States court of any Territory, or the United States District Court for the District of Columbia to enjoin such acts or practices, and upon a proper showing a permanent or temporary injunction or restraining order shall be granted without bond. The Commission may transmit such evidence as may be available concerning such acts or practices to the Attorney General who may, in his discretion, institute the necessary criminal proceedings under this title. Any such criminal proceeding may be brought
Commission must demonstrate a reasonable likelihood that the defendant will engage in future violations before a court can order permanent injunctive relief. As one commentator stated:

The factors that courts have considered in determining the reasonable likelihood of future violations are:

- The egregiousness of the past violations.
- The isolated or repeated nature of the violations.
- The degree of scienter involved.

either in the district wherein the transmittal of the prospectus or security complained of begins, or in the district wherein such prospectus or security is received.

Id. The Exchange Act § 21(d), 15 U.S.C. § 78u(d) (1982) then provides:

(d) Injunction proceedings. Wherever it shall appear to the Commission that any person is engaged or is about to engage in acts or practices constituting a violation of any provision of this title, the rules or regulations thereunder, the rules of a national securities exchange or registered securities association of which such person is a member or a person associated with a member, the rules of a registered clearing agency in which such person or the rules of the Municipal Securities Rulemaking Board, it may in its discretion bring an action in the proper district court of the United States, the United States District Court for the District of Columbia, or the United States courts of any territory or other place subject to the jurisdiction of the United States, to enjoin such acts or practices, and upon a proper showing a permanent or temporary injunction or restraining order shall be granted without bond. The Commission may transmit such evidence as may be available concerning such acts or practices as may constitute a violation of any provision of this title or the rules or regulations thereunder to the Attorney General, who may, in his discretion, institute the necessary criminal proceedings under this title.

Id.

77. See SEC v. Materia, 745 F.2d 197 (2d Cir. 1984), cert. denied, 471 U.S. 1053 (1985) (court enjoined employee of financial printing company from continuing to steal and trade on information he was privy to in his work); SEC v. Youmens, 729 F.2d 413 (6th Cir.), cert. denied, 105 S. Ct. 507 (1984) (district court abused its discretion by focusing exclusively on fact that defendant had changed occupation to determine likelihood of future violations); SEC v. Washington County Util. Dist., 676 F.2d 218 (6th Cir. 1982) (manager of utility district who failed to disclose "kickback" from underwriter violated federal securities laws and could be enjoined); SEC v. Bonastia, 614 F.2d 908 (3d Cir. 1980) (district court abused its discretion by focusing primarily on fact that defendant was no longer engaged in violations to determine need for injunction); SEC v. Blatt, 583 F.2d 1325 (5th Cir. 1978) (SEC must prove scienter in past violations to obtain an injunction); SEC v. Management Dynamics, Inc., 515 F.2d 801 (2d Cir. 1975) (whether injunction should issue to prevent further violations depends on facts of each case).

78. See SEC v. Murphy, 626 F.2d 633 (9th Cir. 1980) (promise of violator not to repeat acts will not preclude injunction as this would in turn establish a ritualistic dodge and negate usefulness of provision); SEC v. Keracarp Indus., Inc., 575 F.2d 692 (9th Cir.), cert. denied, 439 U.S. 953 (1978) (promise of violator to reform is relevant but not conclusive in determining issue of need for injunction); SEC v. Management Dynamics, Inc., 515 F.2d 801 (2d Cir. 1975) (mere cessation of violation is not ipso facto sufficient to avoid injunction).
d. The sincerity of the defendant's assurances, if any, against future violations.
e. The defendant's recognition of the wrongful nature of his conduct.
f. The likelihood that the defendant's occupation will present opportunities (or lack thereof) for future violations.
g. The defendant's age and health.
h. The lapse of time between the violations and the entering of judgment.
i. The effect of adverse consequences to defendant.79

In actions brought to enforce remedial statutes such as the Securities Act and the Exchange Act, the district court has broad discretion to fashion appropriate relief, including relief ancillary to injunction, to effectuate the statutory purpose and policy of the Act.80

To combat securities violations, the courts have granted several types of ancillary relief, some of which include disgorgement,81 the appointment of a receiver,82 and the impoundment of assets.83

C. Internal Revenue Service

The IRS is not engaged in the investigation of boiler rooms per se. However, there is an overlap between the investment fraud schemes

79. 2 W. McLUCAS, R. MARSHMAN & J. DUBOW, REMEDIES AVAILABLE IN S.E.C. ENFORCEMENT ACTIONS 865, 867-73 (1986) [hereinafter REMEDIES].
80. See SEC v. Materia, 745 F.2d 197 (2d Cir. 1984), cert. denied, 471 U.S. 1053 (1985); Chris-Craft Indus. v. Piper Aircraft Corp., 480 F.2d 341 (2d Cir.), cert. denied, 414 U.S. 910 (1973) (district court has the power to order recission or restitution at request of the SEC where such ancillary equitable relief is necessary to effectuate statutory purposes); SEC v. Manor Nursing Centers, Inc., 458 F.2d 1082, 1103 (2d Cir. 1972) (district court granted ancillary relief where it found violations of anti-fraud and prospectus delivery requirements by stating: "[t]hus, while neither the 1933 nor 1934 Acts specifically authorize the ancillary relief granted in this case, '[i]t is for the federal courts to adjust their remedies so as to grant the necessary relief where federally secured rights are invaded.'"), Id. at 1103 (footnote omitted) (quoting J.I. Case Co. v. Borak, 377 U.S. 426, 433 (1964)); see also J.I. Case Co. v. Borak, 377 U.S. 426 (1964) (federal courts must adjust their remedies to grant the necessary relief where federally secured rights are invaded); Mitchell v. Robert DeMario Jewelry, Inc., 361 U.S. 288 (1960) (district court has power to order employer to make restitution or wages lost to employees unlawfully discharged or discriminated against); SEC v. Texas Gulf Sulphur Co., 446 F.2d 1301 (2d Cir. 1971), cert. denied, 404 U.S. 1005 (1971) (court may require insiders who made use of corporate information to benefit selves to make restitution of profits).
82. For cases which discuss appointment of a receiver as a remedy, see SEC v. Materia, 745 F.2d 197 (2d Cir. 1984), cert. denied, 471 U.S. 1053 (1985); SEC v. Manor Nursing Centers, Inc., 458 F.2d 1082 (2d Cir. 1972).
83. International Controls Corp. v. Vesco, 490 F.2d 1334 (2d Cir.), cert. denied, 417 U.S. 932 (1974) (district court did not abuse power when it froze assets of holding company to prevent compounded fraud from sale of subsidiary stock fraudulently distributed as dividends). See also REMEDIES, supra note 78, at 880-81 (for miscellaneous forms of relief).
promoted by boiler room operators and unlawful tax schemes marketed by tax shelter promoters. Unlawful tax schemes being passed off as tax shelters by promoters are geared to a smaller portion of the general public than a typical boiler room operation. Usually a taxpayer has to be in the highest tax bracket in order for the investment in the tax scheme to be economically attractive. Accordingly, the universe of buyers is smaller and much more selective than that available to boiler room operators. As a result, traditional boiler room tactics are not as common in cases falling under IRS jurisdiction as they are in cases falling under the jurisdiction of the CFTC, SEC, FTC, FBI (Federal Bureau of Investigation) and Postal Inspectors.

Notwithstanding this smaller and more economically cohesive universe of investors, however, the products being sold by abusive “tax shelter” promoters and by boiler room operators may be very similar. Tax shelter promoters sell interests in gold and silver mines, Jojoba bean fields, gas and oil wells, cattle, shipping containers, and real estate. Boiler room operators frequently sell the same things. Both groups are limited only by the extent of their imaginations. The criminality of the tax scheme usually arises because the items which are the subject of the promotion are either sold to more than one person, are substantially overvalued, or simply do not exist. The criminality of boiler room operations is frequently illegal for the same reasons.

Many boiler room promotions are marketed as business investments which frequently appear on the purchasers’ tax return, resulting in a double violation. For example, when a boiler room operator sells an investor an interest in a non-existent gold mine, not only does the operation defraud the investor of the purchase price, but the operator may also be guilty of a felony for aiding and assisting the investor in the filing of a materially false tax return in violation of tax laws.\footnote{26 U.S.C. § 7206(2) (1982).} This violation may also arise when boiler room operators conspire to sell undivided interests in oil and gas wells which do not
exist. They not only sell a security within the meaning of section 2(1) of the Securities Act, they may also be guilty of conspiring to obstruct or impede the lawful operations of the IRS in the assessment and collection of tax. In short, a fraudulent investment scheme may be within the jurisdiction of the IRS as well as the CFTC, SEC and/or FTC.

Two injunction proceedings exist under the Internal Revenue Code which may be available to the government in these cases. One arises in cases where the promoter is promoting abusive tax shelters or engaged in conduct which leads to the aiding and abetting of the investor in the understatement of tax liability and such injunctive relief is appropriate to prevent that conduct.

prisoned not more than 3 years, or both, together with the costs of prosecution.

Id.


If two or more persons conspire either to commit any offense against the United States, or to defraud the United States, or any agency thereof in any manner or for any purpose, and one or more of such persons do any act to effect the object of the conspiracy, each shall be fined not more than $10,000 or imprisoned not more than five years, or both.

If, however, the offense, the commission of which is the object of the conspiracy, is a misdemeanor only, the punishment for such conspiracy shall not exceed the maximum punishment provided for such misdemeanor.

Id. See United States v. Klein, 247 F.2d 908 (2d Cir. 1957), cert. denied, 355 U.S. 924 (1958) (parties found to have organized 17 foreign corporations to hide income and evade taxes under 18 U.S.C. § 321).

86. A promoter who markets abusive tax shelters violates 26 U.S.C. § 6700 (1982), which penalizes any person who makes or furnishes a statement with respect to the allowability of any deduction or credit, the excludability of any income, or the securing of a tax benefit which the person knows or has reason to know is false or fraudulent with regard to a material matter, or who makes or furnishes a valuation with regard to a material matter which exceeds 200% of the amount determined to be correct. Id. § 6700(a)-(b)(1).

A promoter who aids and abets the investor in the underpayment of their tax liability violates 26 U.S.C. § 6701 (1982), which penalizes any person who aids, assists, procures, or advises with respect to the preparation or presentation of a return or other document, knowing that the document will be used with regard to a material matter under the internal revenue laws, and knowing that the document would cause an understatement of tax due from another person. Id. § 6701(a).

The injunction, for violation of these two sections, would be issued pursuant to 26 U.S.C. § 7408, which provides:

(a) Authority to seek injunction.

A civil action in the name of the United States to enjoin any person from further engaging in conduct subject to penalty under section 6700 (relating to penalty for promoting abusive tax shelters, etc.) or section 6701 (relating to penalties for aiding and abetting understatement of tax liability) may be commenced at the request of the Secretary. Any action under this section shall be brought in the district court of the United States for the district in which such person resides, has his principal place of business, or has engaged in conduct subject to penalty under section 6700 or section 6701. The court may exercise its jurisdiction over such action (as provided in section 7402(a)) separate and apart from any other action brought by the United States against such person.

(b) Adjudication and decree.

In any action under subsection (a), if the court finds—
An injunction is also authorized "as may be necessary or appropriate for the enforcement of the internal revenue laws." This language grants the court a broad range of powers necessary to compel compliance with the tax laws.

(1) that the person has engaged in any conduct subject to penalty under section 6700 (relating to penalty for promoting abusive tax shelters, etc.) or section 6701 (relating to penalties for aiding and abetting understatement of tax liability), and
(2) that injunctive relief is appropriate to prevent recurrence of such conduct, the court may enjoin such person from engaging in such conduct or in any other activity subject to penalty under section 6700 or section 6701.
(c) Citizens and residents outside the United States.

If any citizen or resident of the United States does not reside in, and does not have his principal place of business in, any United States judicial district, such citizen or resident shall be treated for purposes of this section as residing in the District of Columbia.

26 U.S.C. § 7408 (1982). See United States v. White, 769 F.2d 511 (8th Cir. 1985) (injunction under section 7408 was proper remedy to prevent defendant from continuing sales of tax avoidance plan that contained false representation about deductibility); United States v. Buttorff, 761 F.2d 1056 (5th Cir. 1985) (injunction under section 7408 was proper to prevent promoter from continuing to sell "pure equity" trust that was actually a sham with no tax benefits); United States v. Philatelic Leasing, Ltd., 801 F. Supp. 1554 (S.D.N.Y. 1995), aff'd, 794 F.2d 781 (2d Cir. 1986) (court could enjoin promoters from continued sales of tax shelter where they grossly overvalued "stamp masters"); United States v. Turner, 601 F. Supp. 757 (E.D. Wis.), aff'd, 787 F.2d 595 (7th Cir. 1985) (injunction under section 7408 was proper to prevent promoter from future sales of overvalued energy management systems given promoter's history of involvement in such schemes); United States v. Savoie, 594 F. Supp. 678 (D. La. 1984) (injunction under section 7408 was proper to prevent defendant and club from preparing taxes and using tax-evasion plan).

87. 26 U.S.C. § 7402(a) (1982). This section provides:
The district courts of the United States at the instance of the United States shall have such jurisdiction to make and issue in civil actions, writs, and orders of injunction, and of ne exeat republica, orders appointing receivers, and such other orders and processes, and to render such judgments and decrees as may be necessary or appropriate for the enforcement of the internal revenue laws. The remedies hereby provided are in addition to and not exclusive of any and all other remedies of the United States in such courts or otherwise to enforce such laws.

Id.

88. See United States v. Ernst and Whinney, 735 F.2d 1296, 1300 (11th Cir. 1984) ("language of § 7402(a) encompasses a broad range of powers necessary to compel compliance with the tax laws."); United States v. Landsberger, 692 F.2d 501 (8th Cir. 1982) (injunction granted to prevent tax haven scheme where taxpayer assigned all future income to organization that gifted back 90% of proceeds); United States v. May, 555 F. Supp. 1008 (E.D. Mich. 1983) (injunction proper to prevent tax protestor from distributing an "alternative tax form" which differed from official form); see also United States v. Ekblad, 732 F.2d 562 (7th Cir. 1984) (section 7402(a) used to enjoin individuals from harassing IRS agents in effort to hinder their effectiveness); United States v. Hart, 701 F.2d 749 (8th Cir. 1983) (declaratory injunctive relief proper to prevent audited defendant from continuing to file and record "common law liens" as real property of IRS employee and from "arresting" agents); United States v. First Nat'l City Bank, 568 F.2d 853 (2d Cir. 1977) (taxpayer not entitled to intervene and prevent IRS
D. State and Local Governments

The Commodity Exchange Act preempts state authority in the area of commodity regulation, thereby forcing a number of states to repeal or ignore their commodity statutes. A number of subsequent amendments to the Act, including the Futures Trading Act of 1982, removed this federal preemption. The states are now free to add legislative provisions to fill gaps which previously prevented their adequate policing of off-exchange commodity fraud. The Futures Trading Act specifically permits the application of other federal and state laws to illegal commodity activities and persons who unlawfully engage in commodity transactions outside the Act's regulatory structure. Also under the Act, the states are authorized to take either administrative or judicial action against persons selling off-exchange commodity investments, including sales of precious and strategic metals.

A number of states have modified their statutes to provide for enforcement in the commodities and boiler room areas. For example, Florida, in 1984, amended its Securities Act, now known as the Florida Securities and Investor Protection Act (Florida Act), extending state regulation to boiler rooms and commodity fraud. Under the Florida Act, it is unlawful to "directly or indirectly manage, supervise, control, or own, either alone or in association with others, any boiler room in this state which sells or offers to sell any security or investment [by means of fraud or misrepresentation]." A "Boiler Room" is defined under the statute to mean "an enterprise in which two or more persons engage in telephone communications with members of the public using two or more telephones at one location, or at more than one location in a common scheme or enterprise." Both security and investment are defined under the statute.

from enforcing levy against nonexempt contents of safe deposit box); United States v. Van Dyke, 568 F. Supp. 820 (D. Or. 1983) (injunction proper to prevent tax protestors from harassing IRS employee by filing "common law liens" against them).

91. Futures Trading Act of 1982, § 12(e), codified in relevant part at 7 U.S.C. § 16(e); see also Commodity Investment Fraud II, supra note 4 at 155.
92. Futures Trading Act of 1982, § 12(e), codified in relevant part at 7 U.S.C. §§ 2, 13a-2(8)(A); see also Commodity Investment Fraud II, supra note 91.
94. Id. § 517.312(1)(b).
95. Id. § 517.021(5).
96. Section 517.021(21) defines "security" to include:
   (a) A note.
   (b) A stock.
   (c) A treasury stock.
   (d) A bond.
   (e) A debenture.
Further, the Florida Act makes it unlawful for any person to engage, either in or from the State of Florida, in any act or practice constituting a violation of any provision of the federal Commodity Exchange Act or the rules and regulations of the Commodity Futures Trading Commission, or to offer, sell, or purchase any security or investment by means of fraud, or to falsely represent that either the investment or person selling the investment is approved by the State of Florida or by the United States.

New York has recently enacted legislation which is in substance a boiler room registration law. The New York statute defines a newly created term, “commodity contract,” and provides that it is unlawful to engage in business as a “commodity broker-dealer, commodity salesperson or commodity investment advisor” unless registered in New York as such or otherwise excluded from the registration requirement. Those excluded from the state registration requirement:

(f) An evidence of indebtedness.
(g) A certificate of deposit.
(h) A certificate of deposit for a security.
(i) A certificate of interest or participation.
(j) A whiskey warehouse receipt or other commodity warehouse receipt.
(k) A certificate of interest in a profit-sharing agreement or the right to participate therein.
(l) A certificate of interest in an oil, gas, petroleum, mineral, or mining title or lease or the right to participate therein.
(m) A collateral trust certificate.
(n) A reorganization certificate.
(o) A reorganization subscription.
(p) Any transferable share.
(q) An investment contract.
(r) A beneficial interest in title to property, profits, or earnings.
(s) An interest in or under a profit-sharing or participation agreement or scheme.
(t) Any option contract which entitles the holder to purchase or sell a given amount of the underlying security at a fixed price within a specified period of time.
(u) Any other instrument commonly known as a security, including an interim or temporary bond, debenture, note, or certificate.
(v) Any receipt for a security, or for subscription to a security, or any right to subscribe to or purchase any security.

Id. § 517.021(21). Section 517.021(10) defines “investment” as any commitment of money or property in expectation of receiving an economic benefit. Id. § 517.021(10).

97. Id. § 517.275.
98. Id. § 517.301(1).
99. Id. § 517.311(3).
100. See 1984 N.Y. Laws 810.
102. Id. § 359-e 14(a)(ii).
103. Id. § 359-e 14(b).
104. Id. §§ 359-e 14(g), (h).
tion requirement are generally those individuals or entities who are either registered with the CFTC or SEC, or are exempt from registration under the regulations of those agencies.\textsuperscript{105}

California has enacted a provision which makes it unlawful to operate a boiler room or other telecommunications solicitation efforts without filing a registration statement with the consumer law section of the Department of Justice.\textsuperscript{106}

VI. SPECIAL PROBLEMS INHERENT IN DEVELOPING AN OPERATIONAL PLAN FOR CRIMINAL ENFORCEMENT

Boiler room operators are a loose-knit organization of criminals who know each other, teach each other, and have previously been involved with each other in other kinds of fraudulent schemes, frequently from the heyday of "hot stock" manipulation in the late 1960's and early 1970's. No single judicial district can begin to manage the problem, which is virulent both in its rapid spread and direct impact on far-flung, large numbers of the public. There are several reasons for this:

First, a boiler room operation is incredibly easy to set up. All the operation needs is a bank of telephones, a list of consumers, a script and a relationship with a financial institution. The financial connection can be arranged through a wholly innocent bank with a cooperating inside officer, or a phony bank.

Second, a boiler room operation does not take the brains, or the planning, or the trigger-fast coordination which are the hallmarks of sophisticated stock manipulations. Any fast-talking swindler can pull it off.

Third, the victims are not concentrated geographically nor by any particular interest, such as an interest in specialized securities markets. In fact, the swindlers, by simple list selection, can put as much distance between their operational centers and the victims as they choose. Similarly, they can reduce the impact of their scheme in any particular locale by scattering their calls and thus minimizing the chances that any particular local law enforcement agency will be motivated to strike back.

Fourth, the operation provides instant gratification—money directly from the victim—in relatively small amounts. The small amounts are another guarantee that no local enforcement agency will mobilize against the operators, particularly if they are operating halfway across the country. The direct payment from victims to promoter avoids hazards of the older types of market manipulation,

\textsuperscript{105} Id.
\textsuperscript{106} See CAL. BUS. \& PROF. CODE § 17511.3(a) (West Supp. 1988).
where a few false steps could bring the walls caving in on the promoters before they took their profit out.

Fifth, these kinds of operations avoid triggering a massive federal response for the simple reason that the scheme does not undermine the integrity of a national institution such as the stock market, but instead merely collects small amounts from isolated individuals.

Sixth, boiler rooms are essentially unregulated and entirely mobile. When the investigations by law enforcement warm up, the operations can be unplugged overnight, moved to the safety of a cooler jurisdiction, and opened under a different corporate name in a matter of days.

Finally, on the surface, the operations appear even more complex than the old stock fraud cases. This gives swindlers a sense of security and encourages the proliferation of the business.

VII. THE INJUNCTION AGAINST FRAUD—18 U.S.C. § 1345

The Comprehensive Crime Control Act\(^\text{\text{107}}\) was passed in 1984, permitting the government to seek injunctions against activities associated with mail fraud,\(^\text{108}\) wire fraud,\(^\text{109}\) and bank fraud.\(^\text{110}\) The statute states that:

Whenever it shall appear that any person is engaged or is about to engage in any act which constitutes or will constitute a violation of this chapter [Chapter 63 of Title 18, comprising sections 1341-1345], the Attorney General may initiate a civil proceeding in a district court of the United States to enjoin such violation. The court shall proceed as soon as practicable to the hearing and the determination of such an action, and may, at any time before final determination, enter such a restraining order or prohibition, or take such other action, as is warranted to prevent a continuing and substantial injury to the United States or to any person or class of persons for whose protection the action is brought. A proceeding under this section is governed by the Federal


[w]hoever, having devised or intending to devise any scheme of artifice to defraud . . . for the purpose of executing such scheme . . . places . . . any matter or thing whatever to be sent or delivered by the Postal Service . . . shall be fined not more than $1,000 or imprisoned not more than five years, or both.

\(^{109}\) Id., § 1343. “Whoever, having devised or intending to devise any scheme or artifice to defraud . . . transmits . . . by means of wire . . . [any communication] . . . for the purpose of executing such scheme . . . shall be fined not more than $1,000 or imprisoned not more than five years, or both.” Id.

\(^{110}\) Id., § 1344. “Whoever knowingly executes . . . a scheme . . . to defraud a federally chartered or insured financial institution; or (2) to obtain . . . assets . . . of [such] financial institution by [fraud] . . . shall be fined not more than $10,000, or imprisoned not more than five years, or both.” Id.
Rules of Civil Procedure, except that, if an indictment has been returned against the respondent, discovery is governed by the Federal Rules of Criminal Procedure.111

A. Scope of the Statute

Upon a showing by the Attorney General that a person is engaged in, or about to engage in, mail, wire, and/or bank fraud, section 1345 permits a federal district court to issue a civil injunction, restraining order, prohibition, or to take any other action which is warranted to prevent a continuing and substantial injury to the government or the public resulting from the violation.112

The purpose of this statute is to provide prosecutors with an effective tool to prevent the continuation of a fraudulent scheme during the pendency of the investigation.113

Another area where there is a great need for injunctive relief is in fraudulent scheme cases. While present law provides limited injunctive relief, this relief is inadequate. First, the relief is restricted to the detention of incoming mail. It does not reach the situation where letters continue to be sent to further a scheme and remittances are collected personally from the customer or to fraudulent schemes which do not entail the use of the mails. Second, the required administrative proceedings entail considerable delay which is compounded by the extra time and energy necessary to bring an injunctive suit in the district court while the administrative proceedings are pending. Since the investigation of fraudulent schemes often takes months, if not years, before the case is ready for criminal prosecution, innocent people continue to be victimized while the investigation is in progress.

Experience has shown that even after indictment or the obtaining of a conviction, the perpetrators of fraudulent schemes continue to victimize the public.114

B. Jurisdiction and Venue

Jurisdiction of the federal courts to enjoin fraudulent boiler room operations has been authorized by Congress.115 This grant of district court jurisdiction over civil actions commenced by the United States is without regard to the subject matter of the litigation.116 The

111. Id. § 1345.
113. Id.
115. 28 U.S.C. § 1345 (1982). "Except as otherwise provided by Act of Congress, the district courts shall have original jurisdiction of all civil actions, suits or proceedings commenced by the United States, or by any agency or officer thereof expressly authorized to sue by Act of Congress." Id.
116. See United States v. Commonwealth of Puerto Rico, 551 F. Supp. 864 (D.P.R. 1982), aff'd, 721 F.2d 832 (1st Cir. 1983) (holding that 28 U.S.C. section 1345 governs the federal government's access to the district courts unless Congress preempts this statute in certain cases by specific statute); see also United States v. Morchetti, 466 F.2d 1309 (4th Cir.), cert. denied, 409 U.S. 1063 (1972) (federal district court has jurisdiction
United States can bring suit "to protect its sovereign interest notwithstanding the lack of any immediate pecuniary interest in the outcome of the litigation."\textsuperscript{117} This congressional authority also provides for jurisdiction over actions in which the United States seeks injunctive relief.\textsuperscript{118}

Venue will lie in the judicial district in which all the defendants reside or in which the cause of action arose.\textsuperscript{119} Typically, a boiler room operation has a business location in one judicial district, but solicits victims from a large number of other judicial districts. If the United States brings the action in either the judicial district in which the defendants live, or the judicial district in which the boiler room is located, the court’s venue requirement would clearly be satisfied.\textsuperscript{120}

Venue is not so clear, however, when the United States seeks to bring the action in other judicial districts. The Northern District of cases in which the United States is a party); Williams v. United States, 42 F.R.D. 609 (S.D.N.Y. 1967) (federal district courts have original jurisdiction, regardless of subject matter of any proceeding commenced by the United States against a state).

\textsuperscript{117} United States v. Lewisburgh Area School Dist., 539 F.2d 301, 305 (3d Cir. 1976) (United States had standing to apply to federal court to determine whether the actions of local taxing bodies violated its sovereign rights); \textit{Cf.} United States v. Allegheny County, 322 U.S. 174 (1944) (Pennsylvania law held unconstitutional because it authorized taxation of property interests of the United States which violated the federal government's sovereignty).


\textsuperscript{119} 28 \textsuperscript{U.S.C.} \textsection{1391} (1976).

\textsuperscript{120} \textit{See} Johnson Creative Arts, Inc. v. Wool Masters, Inc., 573 F. Supp. 1106 (D. Mass. 1983), aff'd, 743 F.2d 947 (1st Cir. 1984). The federal district court in Massachusetts was improper venue for a civil suit brought against a defendant corporation located in New York that merely solicited business and received orders and payments for goods shipped to Massachusetts. \textit{Id.} Venue would be proper, however, in the Southern District of New York where the defendant corporation made decisions and conducted corporate activity. \textit{Id.}
Illinois has successfully engaged in an enforcement program based upon "victim venue."  For criminal venue purposes, venue would lie in the victim's district, that is, the district in which the offense is "begun, continued, or completed." The rationale for this is that the victim receives a wire communication or mail delivery from the defendant and thereafter places money, checks, or other things of value into the mails or other means of transportation in interstate commerce for delivery to the defendants in their home districts.

Therefore, the government should take the position that venue is appropriate for a section 1345 injunction in any district in which venue is appropriate to prosecute for mail or wire fraud. It makes no sense to conclude that the defendant could be prosecuted for mail or wire fraud in one district, but that the petition to enjoin that fraud must be brought in another district.

The cases which have been decided under the civil venue statute, however, suggest a contrary result. "The phrase, 'in which the claim arose' is simpler in its statement than in its operation." Generally, three principal standards have been used by the federal courts to determine where the action arose: "(1) The place of the injury rule; (2) The weight of the contacts rule; and (3) The rule which turns on whether a substantial part of the events or omissions giving rise to the claim occurred in the district."

"The place of the injury test deems that the claim arises in the district in which the plaintiff's injuries were suffered, i.e., where the effect of the defendants' alleged wrongful act occurred." However, in Leroy v. Great Western United Corp., the Supreme Court re-

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122. 18 U.S.C. § 3237(a) (Supp. III 1985). "[A]ny offense against the United States begun in one district and completed in another, or completed in more than one district, may be inquired of and prosecuted in any district in which such offense was begun, continued, or completed." Id.
123. Soper v. Simmons Int'l Ltd., 582 F. Supp. 987, 990 (N.D.N.Y. 1983) (district court held conspiracy cause of action was properly pleaded under the Racketeer Influenced and Corrupt Organizations Act, but transferred the case as venue was improper due to defendant's lack of contacts with the district).
125. Hodson, 528 F. Supp. at 813.
jected the “place of injury” approach, and seems to have adopted the “weight of the contacts” test.

The statute allows venue “in the judicial district . . . in which the claim arose.” Without deciding whether this language adopts the occasionally fictive assumption that a claim may arise in only one district, it is absolutely clear that Congress did not intend to provide for venue at the residence of the plaintiff or to give that party an unfettered choice among a host of different districts. Rather, it restricted venue either to the residence of the defendants or to “a place which may be more convenient to the litigants”—i.e., both of them—or to the witnesses who are to testify in the case.” In our view, therefore, the broadest interpretation of the language of § 1391(b) that is even arguably acceptable is that in the unusual case in which it is not clear that the claim arose in only one specific district, a plaintiff may choose between those two (or conceivably even more) districts that with approximately equal plausibility—in terms of the availability of the witnesses, the accessibility of other relevant evidence, and the convenience to the defendant (but not of the plaintiff)—may be assigned as the locus of the claim.127

The majority of the courts have adopted the “weight of the contacts” test for determining where the action arose.128 “Leroy acknowledged that a claim may arise in more than one district . . . .”129 Leroy requires that each of the districts under consideration be equally plausible, however.130 The resulting test is a combination of the “substantial part of the events” test (allowing venue in a district with a relatively minor amount of activity in preference to a number of other districts with greater activity) and the strict “weight of the contacts” test (limiting the choice of venue to only one district). Accordingly, not only must venue be in a district which had a substantial amount of activity, but there may not be any other district(s) with substantially more activity.

Venue based upon doing business within the district may not rest upon the “minimum contacts” test of International Shoe Co. v. Washington.131 The defendant’s business activities in the forum judicial district must comprise substantially more than minimal contacts.132 For example, venue in Massachusetts was not proper where defendant’s sales in Massachusetts constituted only six percent of its total sales and nothing distinguished Massachusetts from thirty-four other

127. Id. at 184-85 (citations omitted).
129. Id. at 992.
130. 443 U.S. at 185.
states in which the defendant sold its products. Likewise, where a Massachusetts corporation derived only two percent of its total income (amounting to $1,500) from its sales territory in New York, did not maintain a place of business in New York, and made only four visits per year to New York, venue was not appropriate in New York. Conversely, where a California banking corporation had solicited and transacted business in Indiana, including the solicitation and execution of certificates of deposit representing promises to pay Indiana residents, mailed certificates and interest checks to Indiana, issued cashier's checks to Indiana residents, and where Indiana was a more convenient location for most witnesses, venue was appropriate in the Northern District of Indiana. Also, where a publisher of a trade journal, whose principal place of business was in Massachusetts, directly distributed between five and seven percent of its journals to Pennsylvania and regularly solicited Pennsylvania businesses to place advertising in its journal, venue was appropriate in Pennsylvania.

Accordingly, if the government proceeds on a "victim venue" theory in a section 1345 proceeding, it should anticipate a challenge to venue. Even though a statute allows venue where "the claim arose," it is not entirely clear that if a boiler room is located in Los Angeles and has one or two victims in Massachusetts whether venue is appropriate in the District of Massachusetts. The plaintiff has the burden of establishing that venue is appropriate and the government must be prepared to establish that venue in Massachusetts is equally as plausible as venue in the Central District of California.

C. Basis for the Temporary Restraining Order

Injunctive relief applicants may occasionally face irreparable injury before the hearing for a preliminary injunction occurs pursuant to Federal Rule of Civil Procedure 65(a). A temporary restraining order (TRO), however, may be available in such circumstances under Rule 65(b) to "preserve the status quo until there is an opportunity to hold a hearing on the application for a preliminary injunction and may be issued with or without notice to the adverse party." Where

133. Id. at 1112.
138. 11 C. WRIGHT & A. MILLER, FEDERAL PRACTICE AND PROCEDURE § 2951 (1973) [hereinafter C. WRIGHT].
139. Id.
granted, the goal of the TRO "should be restricted to serving their underlying purpose of preserving the status quo and preventing irreparable harm just so long as is necessary to hold a hearing, and no longer."\textsuperscript{140}

A TRO may be granted without notice to the adverse party or his attorney only if (1) it is clear from the verified complaint or the supporting affidavit that "immediate and irreparable injury, loss, or damage will result to the applicant before . . . [he] can be heard in opposition"\textsuperscript{141} and (2) the applicant's attorney certifies in writing what efforts have been made to give notice to the adverse party and why notice should not be required.\textsuperscript{142} The TRO may last no more than ten days;\textsuperscript{143} however, where good cause is shown, it may be extended for a second ten-day period.\textsuperscript{144} Even if notice is given to the adverse party, the applicant must show immediate and irreparable injury before the court will grant the order.\textsuperscript{145}

It thus follows that a showing of immediate and irreparable injury would also be required in cases where notice is not given. In addition, some courts require the applicant to demonstrate not only a reasonable likelihood of prevailing on the merits, but also that the harm in not granting the applicant's restraining order outweighs any possible harm to the defendant or the public by granting the injunction.\textsuperscript{146} The evaluation of these factors and the grant or denial of the TRO rests within the discretion of the trial judge.\textsuperscript{147}

\textsuperscript{141} Id. 65(b)(1).
\textsuperscript{142} Id. 65(b)(2).
\textsuperscript{143} Id. 65(b).
\textsuperscript{144} Id.
\textsuperscript{145} Cf. National Prisoners Reform Ass'n v. Sharkey, 347 F. Supp. 1234, 1236-37 (D.R.I. 1972) (in an ex parte hearing, temporary restraining order (TRO) not granted because of public interest, but the court does not imply that the "immediate and irreparable injury" requirement would be disregarded if the ex parte TRO were granted).
\textsuperscript{146} Garcia v. United States, 680 F.2d 29, 31 (5th Cir. 1982) (must show likelihood of success on the merits, irreparable harm, and that irreparable harm outweighs harm to defendant); Martin v. Attaway, 506 F. Supp. 603, 606 (S.D. Ga. 1981) ("[H]arm to plaintiff outweighs any possible harm to the defendants and to the public . . . ."); Salomon North Am., Inc. v. AMF, Inc., 484 F. Supp. 846, 848 (D. Mass. 1980) (must show both likelihood of success on the merits and that plaintiff's harm outweighs defendant's); National Prisoners Reform Ass'n, 347 F. Supp. at 1236-37 (applicant must show immediate and irreparable harm, probability of success on the merits, and that movant's harm outweighs harm to opposing party and public).
Where notice is given to the adverse party and there is a hearing on the petition, the proceeding is similar to an application for a preliminary injunction.\(^{148}\) "If there is an adversary hearing or the order is entered for an indeterminate length of time, the 'temporary restraining order' may be treated as a preliminary injunction."\(^{149}\)

There is some basis for the position that a TRO should not be treated as a preliminary injunction unless the adverse party consents.

By its terms Rule 65(b) only governs restraining orders issued without notice or a hearing. However... it has been argued that its provisions, at least with regard to the duration of a restraining order, apply even to an order granted when notice has been given to the adverse party but there has been no hearing. This appears to be a sound exercise of judicial discretion, particularly in those situations in which simply giving notice should not justify treating the order as a preliminary injunction since the time constraints do not allow the parties to prepare adequately for a hearing.\(^{150}\)

Therefore, the affidavit supporting the government’s application should establish that the boiler room operator is engaged in mail or wire fraud and that the public will be irreparably harmed unless the boiler room activities are terminated. The restraining order should preserve the status quo, i.e., the public’s enjoyment of money and property without fraud. In other words, it is the pre-boiler room status to be maintained. The restraining order will clearly have an adverse affect upon the operator as “business” activities will be precluded for ten days. Although the restraining order will only temporarily resolve the problem, the order is necessary because the harm to the public if the activity is not enjoined exceeds the harm to the operator during the ten-day period of the restraining order. The operator stands to lose some business for a period of ten to twenty days if he is enjoined. The public, on the other hand, stands to lose 100% of its investment during that same period of time. If the government cannot prove its case at the preliminary injunction stage, the order will automatically dissolve with minimal cost and inconvenience to the boiler room operator. If the government does prevail, then the restraining order was clearly appropriate. The balancing test, therefore, weighs in favor of the public's interest.

\(^{148}\) C. WRIGHT, supra note 138, at 499.

\(^{149}\) Id. at 500; see also Levas & Levas v. Village of Antioch, 684 F.2d 446, 448 (7th Cir. 1982) (TRO treated as one for preliminary injunction); In re Arthur Treacher's Franchisee Litig., 689 F.2d 1150, 1154 (3d Cir. 1982) (temporary restraining order held tantamount to a preliminary injunction); MLZ, Inc., 470 F. Supp. at 275 (application for TRO treated as one for preliminary injunction where opponent was present at hearing); Wisch v. Sanford School, Inc., 420 F. Supp. 1310, 1311 (D. Del. 1976) (plaintiff’s motion for a TRO considered as one for preliminary injunction).

\(^{150}\) C. WRIGHT, supra note 138, at 500 (citation omitted); see Bailey v. Transportation-Communications Employees Union, 45 F.R.D. 444, 445 (N.D. Miss. 1968).
D. Basis for the Preliminary Injunction

To successfully move for a preliminary injunction, the petitioner must show: (1) substantial threat that the plaintiff will suffer irreparable damage in the absence of such relief; (2) that the plaintiff has a substantial likelihood of prevailing on the merits; (3) that the threatened injury to the plaintiff outweighs the possible harm that the injunction might cause any other parties; and (4) that the injunction will not be adverse to the public interest.\(^{151}\)

1. Irreparable Harm

Conditions precedent to the issue of a statutory injunction designed to protect the public interest are less restrictive than the traditional requirement under Rule 65.\(^ {152}\) When “an injunction is expressly authorized by statute and the statutory conditions are satisfied, the usual prerequisite of irreparable injury need not be established.”\(^ {153}\)

Even without this rule, the government can usually meet the irreparable injury test in the case of boiler room operations. In assessing the propriety of extraordinary injunctive relief, it is proper to focus first upon the prevention of injury which cannot later be redressed through other remedies.\(^ {154}\) Boiler room operators typically engage in one or more schemes to defraud and frequently use an alias, operate through nominee corporations, purchase property in other names, move money offshore, and are often out of business and gone from the area before the victims know they have been defrauded. Even if the victims become enlightened and realize who defrauded them, there are usually no funds available to compensate them.

Generally, a monetary loss is not a sufficient irreparable injury to

\(^{151}\) For cases in the Fifth Circuit, see Enterprise Int'l Inc. v. Corporacion Estatal Petrola, 762 F.2d 464, 471 (5th Cir. 1985); Cate v. Oldham, 707 F.2d 1176, 1185 (5th Cir. 1983); Hardin v. Houston Chronicle Pub. Co., 572 F.2d 1106, 1107 (5th Cir. 1978); Canal Auth. of Fla. v. Callaway, 489 F.2d 567, 572 (5th Cir. 1974); see also supra note 120.

\(^{152}\) See infra note 153.

\(^{153}\) Southern Cent. Bell Tel. v. Louisiana Pub. Serv. Comm'n, 744 F.2d 1107, 1120 (5th Cir. 1984); see, e.g., Gresham v. Windrush Partners, 730 F.2d 1417, 1423 (11th Cir.) (“[I]rreparable injury should be presumed from the very fact that the statute was violated.”), cert. denied, 469 U.S. 882 (1984); Trailer Train Co. v. State Bd. of Equalization, 697 F.2d 860, 869 (9th Cir.) (“The standard requirements for equitable relief need not be satisfied when an injunction is sought to prevent the violation of a federal statute which specifically provides for injunctive relief.”), cert. denied, 464 U.S. 846 (1983); Atchison, T. & S.F. Ry. v. Lennen, 640 F.2d 225, 259 (10th Cir. 1981) (not necessary to show irreparable injury where Congress has authorized federal courts to grant injunctive relief).

\(^{154}\) Canal Auth. of Fla., 489 F.2d at 573.
support the issuance of a preliminary injunction. A monetary loss alone, however, will support a preliminary injunction if a legal remedy for monetary damages would be clearly ineffective in making a recovery. "An injury is irreparable if it cannot be undone through monetary remedies." Such is the case with victims of boiler room fraud. Although these victims have the potential to sue for damages, it is clear that such civil suits would be ineffective to recover their losses where funds are not available.

2. Prevail on the Merits

The supporting affidavit should clearly establish that the defendants are engaged in one or more schemes involving mail, wire, and/or bank fraud in violation of the statutory prohibition, and that investors and other parties will continue to be victimized unless defendants are enjoined. The affidavit and the memorandum of points and authorities in support of the petition should focus upon those factors which would lead the judge to conclude that the defendants would continue the unlawful conduct unless enjoined.

3. Harm to Other Parties; Public Interest

In the case of a boiler room operation, the proposed restraining order and preliminary injunction generally will impact only defendants and persons actively participating with them. Thus, it will have the effect of inhibiting criminal conduct by freezing the improperly secured funds in the hands of persons who were not entitled to them in the first place.

Moreover, the injunction will benefit the public interest. The purpose of the government's petition is to terminate criminal fraud and compensate the fraud victims. In section 1345, Congress clearly declared such injunctions to be in the public interest.

E. Basis for the Permanent Injunction

After the preliminary injunction is issued, the parties will normally engage in civil discovery before litigating the permanent injunction on the merits. At trial, the government must demonstrate

155. See Enterprise Int'l, Inc., 762 F.2d at 472 ("[I]njury is 'irreparable' only if it cannot be undone through monetary remedies."); Deerfield Medical Center v. Deerfield Beach, 661 F.2d 328, 338 (5th Cir. 1981) ("[I]njury is 'irreparable' only if it cannot be undone through monetary remedies."); Morgan v. Fletcher, 518 F.2d 236, 240 (5th Cir. 1975) ("Mere injuries... in terms of money... are not enough.").

156. See Placid Oil Co. v. United States Dep't. of the Interior, 491 F. Supp. 895, 906 (N.D. Tex. 1980) (granting preliminary injunction because "[p]laintiffs would not be compensated for economic loss even if they prevailed on the merits.").

157. Deerfield Medical Center, 661 F.2d at 338.

not only that the defendant's conduct includes the perpetration of mail, wire, and/or bank fraud, they must also show a "reasonable likelihood" that the defendants will engage in future violations unless enjoined.\textsuperscript{159} Voluntarily agreeing to refrain from the unlawful conduct in the future will not preclude an injunction.\textsuperscript{160}

F. Scope of Remedies Available

When enforcing remedial statutes such as the Securities Act of 1933, the Securities Exchange Act of 1934, and the Commodity Exchange Act of 1974, district courts have broad discretion to fashion appropriate relief, including relief ancillary to the injunction, to effectuate the statutory purpose and policy.\textsuperscript{161}

\textsuperscript{159} See, e.g., SEC v. Materia, 745 F.2d 197, 200 (2d Cir. 1984) (holding that when a person is engaged or is about to engage in violating the securities laws, "only a reasonable likelihood that the activity . . . will be repeated" must be shown); SEC v. Youmens, 729 F.2d 413, 415 (6th Cir.), \textit{cert. denied}, 469 U.S. 1034 (1984) (must show a reasonable and substantial likelihood of future violations); SEC v. Washington County Util. Dist., 676 F.2d 218, 227 (6th Cir. 1982) ("Proof of past violations . . . serves as a basis . . . that future violations may occur."); SEC v. Bonastia, 614 F.2d 908, 912 (3d Cir. 1980) (to show reasonable likelihood, look to: scienter involved, recurrent nature of violation, defendant's recognition of wrong, sincerity of his promises against future violations, and defendant's professional occupation); SEC v. Blatt, 583 F.2d 1325, 1334 (5th Cir. 1978) (must prove more than past violations when offering positive proof of future violations); SEC v. Management Dynamics, Inc., 515 F.2d 801, 807 (2nd Cir. 1975) ("[P]ast illegal conduct is highly suggestive of the likelihood of future violations."); CFTC v. Skorupskas, 605 F. Supp. 923, 942 (E.D. Mich. 1985) (determination based on totality of circumstances); CFTC v. Morgan, Harris & Scott, Ltd., 484 F. Supp. 669, 676 (S.D.N.Y. 1979) (inference can be drawn from past illegal conduct). \textit{But cf.} CFTC v. Commodities Fluctuations Systems, Inc., 583 F. Supp. 1382, 1385 (S.D.N.Y. 1984) (must look at totality of circumstances and past violations alone are not enough).

\textsuperscript{160} See SEC v. Murphy, 626 F.2d 633, 655-56 (9th Cir. 1980) (defendant's statements of "reformation" were not sufficient to preclude summary judgment); \textit{Management Dynamics, Inc.}, 515 F.2d at 807 ("[I]njunctive relief is not barred by a defendant's disclaimer of an intent to violate the law in the future . . . ."); SEC v. Korscorp Indus., Inc., 575 F.2d 692, 698 (9th Cir.) (promises of reformation are relevant but not conclusive or even necessarily persuasive), \textit{cert. denied}, 439 U.S. 953 (1978).

\textsuperscript{161} Materia, 745 F.2d at 200; CFTC v. Co Petro Mktg. Group, Inc., 680 F.2d 573, 583 (9th Cir. 1983) (remedy ancillary to permanent injunction upheld); Chris-Craft Indus. v. Piper Aircraft Corp., 480 F.2d 341, 390 (2d Cir.) (court has power to grant all equitable relief necessary), \textit{cert. denied}, 414 U.S. 910 (1973); SEC v. Manor Nursing Centers, Inc., 458 F.2d 1082, 1102 (2d Cir. 1972) (injunction alone would not protect the public); \textit{see also} Mitchell v. DeMario Jewelry, 361 U.S. 288, 291-92 (1960) (jurisdiction conferred by Fair Labor Standards Act of 1938 includes remedial powers beyond those expressly granted in the Act); CFTC v. Hunt, 591 F.2d 1211, 1222 (7th Cir.) (disgorgement as an appropriate form of relief), \textit{cert. denied}, 422 U.S. 921 (1979); SEC v. Texas Gulf Sulphur Co., 446 F.2d 1301, 1308 (2nd Cir. 1971) ("SEC may seek other than injunctive relief in order to effectuate the purposes of the Act, so long as such relief is remedial relief and is not a penalty . . . ."); \textit{Morgan, Harris & Scott, Ltd.}, 484 F. Supp. at 677 (ancillary relief necessary); Kelley v. Carr, 567 F. Supp. 831, 940 (W. D. Mich. 1983).
Section 1345 is a remedial statute similar to those involving securities and commodities. Congress intended to authorize the courts to take all actions necessary to terminate fraud and protect the public. Section 1345 is no more narrowly written than the provisions authorizing injunctions to remedy violations of the securities and commodities laws. Although the securities or commodities laws do not specifically authorize ancillary relief, courts have nevertheless historically granted ancillary relief to combat violations. Similar remedies therefore are available under section 1345 in cases where the government shows the boiler room operator to be engaging in mail, wire, and/or bank fraud and a reasonable likelihood of future violations. The following sections discuss the major forms of ancillary relief granted in securities and commodities cases.

G. Appointment of a Receiver

"The decision to appoint an equity receiver in enforcement actions under the commodities and securities laws is a matter within the sound discretion of the trial judge."162 Receivers may recover funds through ancillary actions.163 To the extent possible, attorneys seeking the appointment of an equity receiver should specify in the order the major duties which the receiver is to perform. By doing so, the government can avoid litigation over which procedures the receiver is authorized to perform; the only issue remaining would be whether there was an abuse of discretion when the trial judge assigned the task to the receiver.164

H. Disgorgement and Restitution

Disgorgement or restitution orders attempt to remove the economic incentive of crime and place the victims in their rightful position. The disgorgement order may also deter future violations and "future compliance may be more definitely assured if one is com-

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1983) (disgorgement is an appropriate remedy); CFTC v. United States Metals Depository Co., 468 F. Supp. 1149, 1161 (S.D.N.Y. 1979) (court has broad discretion to enjoin security law violations).

162. CFTC v. American Commodity Group Corp., 753 F.2d 862, 866 n.6 (11th Cir. 1984); see also CFTC v. Chilcott Portfolio Management, Inc., 713 F.2d 1467, 1482 (2nd Cir. 1983) ("The court properly conferred the power on the receiver to sue."); Co Petro Mktg. Group, 680 F.2d at 582-83 (district court properly ordered appointment of a receiver); Manor Nursing Center, Inc., 458 F.2d at 1105 (upholding appointment of trustees or receivers); Carr, 567 F. Supp. at 841 (appointment of an "equity receiver" and an accounting held proper); Morgan, Harris & Scott, Ltd., 484 F. Supp. at 679 (freeze order designed to "preserve status quo until receiver is able to report).

163. American Commodity Group Corp., 753 F.2d at 866 n.6; Chilcott Portfolio Management, Inc., 713 F.2d at 1482; Morgan, Harris & Scott, Ltd., 484 F. Supp. at 679.

164. See American Commodity Group Corp., 753 F.2d at 866.
peled to restore one's illegal gains."¹⁶⁵ In addition, "it would frustrate the regulatory purposes of the Act[s] to allow a violator to retain his ill-gotten gains."¹⁶⁶

Attorneys for the government should choose how they want to accomplish the disgorgement or restitution. The government could seek an order instructing the defendant(s) to pay certain sums of money to certain specified individuals. In the alternative, the disgorgement and restitution could be made through the mechanism of a receiver.¹⁶⁷ If a receiver is needed to provide ancillary relief, attorneys for the government should ensure that the receiver is empowered to initiate whatever judicial or administrative actions are necessary to collect the assets of the promoter and to disburse those funds to the victims in an equitable manner.¹⁶⁸

I. Freezing, Impounding of Assets and Miscellaneous Relief

In addition or in the alternative to receivers and disgorgement, the courts may order that the promoter's assets be frozen or impounded.¹⁶⁹ It is necessary, however, to comply with all the procedural requirements of section 1345. It is not sufficient to cite section 1345 as authority in seeking such orders in the context of a criminal

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¹⁶⁵. Co Petro Mktg. Group, 680 F.2d at 583 (citing Porter v. Warner Holding Co., 328 U.S. 395, 400 (1946)).


¹⁶⁷. See supra text accompanying notes 36-38.


The court may order an accounting for money received and disbursed by the promoter, either separately or as part of a disgorgement/restitution order.

VIII. RULE 6(e) AND SELLS ENGINEERING

May an attorney for the Government presenting a criminal case to a federal grand jury also represent the United States in a civil case seeking an injunction pursuant to section 1345 which involves the same parties and issues as the subject of the grand jury investigation? If so, can the attorney use grand jury information in the civil case? Can the attorney proceed pursuant to Rule 6(e)(3)(A)(i) of the Federal Rules of Criminal Procedure, or must he get an order pursuant to Rule 6(e)(3)(C)(i)?

In United States v. Sells Engineering, Inc., the Supreme Court ruled that attorneys in the Civil Division of the Department of Justice and their assistants and staff may not obtain automatic disclosure of grand jury materials for use in a civil suit pursuant to Rule 6(e)(3)(A)(i) of the Federal Rules of Criminal Procedure, but instead must seek an order pursuant to Rule 6(e)(3)(C)(i), as being preliminary to or in connection with a judicial proceeding, in order to gain access to such materials.

We conclude, then, that Congress did not intend that “attorneys for the government,” should be permitted free civil use of grand jury materials. Congress was strongly concerned with assuring that prosecutors would not be free to turn over grand jury materials to others in the Government for civil uses without court supervision, and that statutory limits on civil discovery not be subverted—concerns that apply to civil use by attorneys within the Justice Department as fully as to similar use by persons in other government agencies.

Having decided that it was necessary to secure an order pursuant to Rule 6(e)(3)(C)(i) prior to disclosing grand jury information to “an attorney for the government” for use in a civil proceeding, the Court then adopted the “particularized need” standard which it had previously outlined in Douglas Oil Co. v. Petrol Stops Northwest, as the standard against which to measure such requests.

Parties seeking grand jury transcripts under Rule 6(e) must show that the material they seek is needed to avoid a possible injustice in another judicial proceeding.

173. Id. at 427-35.
174. Id. at 442.
proceeding, that the need for disclosure is greater than the need for continued secrecy, and that their request is structured to cover only material so needed.

It is clear from Proctor & Gamble and Dennis that disclosure is appropriate only in those cases where the need for it outweighs the public interest in secrecy, and that the burden of demonstrating this balance rests upon the private party seeking disclosure.176

The Court in Sells Engineering specifically refrained from addressing the issue of the continued use of grand jury materials in the civil phase of a dispute by an attorney who also conducted the criminal prosecution.177

Until recently, the Second and Eighth Circuits have differed somewhat in their analysis of this issue.178 In In re Grand Jury Investigation, the same government attorneys in the Antitrust Division who had conducted the grand jury investigation were instructed to pursue a civil investigation and, if appropriate, to prepare a civil complaint.179 The grand jury investigation was already completed at the time these attorneys initially received their civil assignment.180 The grand jury materials which they had accumulated included 250,000 pages of subpoenaed documents and the testimony of dozens of witnesses.181 The Second Circuit held that continued access to these grand jury documents was a “disclosure” of grand jury information that required an order pursuant to Rule 6(e)(3)(c)(i):

The testimony and documents here are voluminous, and we doubt that the two attorneys could independently recall the details of 250,000 pages of subpoenaed documents or the details of testimony by dozens of witnesses. Civil prosecution of the case would therefore invite them to refer repeatedly to the documents and transcripts of which they have prior knowledge and with which they may be partially familiar. Even when a criminal investigation has generated far fewer materials, any resort to these materials by the attorneys pursuing the civil matter to refresh their recollection as to documents or testimony to which they had access in the grand jury proceeding is tantamount to a further disclosure. Viewed in this context, to permit them continued access to the materials is equivalent to “disclosure.”182

The Second Circuit noted that the real issue is whether the prosecutor who conducted the grand jury investigation must be disqualified from litigating the civil case. “[I]t would be almost impossible for any

176. Id. at 222-23; see also Sells Eng'g, Inc., 483 U.S. at 433.
177. 463 U.S. at 431 n.15.
179. In re Grand Jury Investigation, 774 F.2d at 36.
180. Id. at 35.
181. Id.
182. Id. at 40.
attorney in such a position to compartmentalize his thoughts and litigate a civil case without in some way using his recollection of facts learned during the grand jury investigation . . . ." The court, however, did not find it necessary to reach that issue.

In United States v. Archer-Daniels-Midland Co., the Antitrust Division utilized a federal grand jury in the Northern District of California to investigate possible price-fixing by companies engaged in corn milling. Eighteen months after the grand jury concluded its investigation, Nabisco leased its milling facilities to Archer-Daniels-Midland. The Antitrust Division then began a civil investigation to determine whether the lease agreement violated either the Sherman or Clayton Antitrust Acts. Some of the attorneys who were assigned to the civil investigation had previously been assigned to the grand jury investigation. The Eighth Circuit determined that the assignment to a civil case of the same attorneys who participated in a prior grand jury investigation did not constitute a disclosure of things which occurred before the grand jury. The court felt that "[i]f there to be a disclosure, grand jury matters must be disclosed to someone. We do not believe that an attorney's recollection of facts learned from his prior grand jury participation can be considered disclosure so as to invoke the prohibition of Rule 6(e)." The court acknowledged the Second Circuit's decision in In re Grand Jury, but distinguished it because Archer-Daniels did not "contain a clear showing of continued use of grand jury materials by attorneys assigned to the civil litigation to refresh their recollection." The Court also noted that the attorneys in the civil case had not used and would not use any grand jury material except to respond to defendant's discovery efforts. Finally, the Eighth Circuit concluded that "our decision is strengthened by the fact that the civil antitrust suit brought by the Government against ADM and Nabisco alleging an unlawful acquisition or merger is a distinct and separate action from the prior grand jury investigation for price-fixing."

The Supreme Court granted certiorari in United States v. John Doe, Inc., in order to resolve the conflict between the Second and Eighth Circuits, and in the resolution of that conflict addressed the

183. Id. at 43.
184. 785 F.2d 206 (8th Cir. 1986).
185. Id. at 208.
186. Id.
187. Id.
188. Id.
189. Id. at 212.
190. Id. at 213 n.12.
191. Id. at 213 n.13.
192. Id. at 213.
issue which they had avoided in *Sells Engineering*.\textsuperscript{194} The Supreme Court agreed with the Eighth Circuit that the continued use of grand jury information by attorneys who legitimately gained access to the information did not constitute a disclosure within the meaning of Rule 6(e).

[It seems plain to us that Rule 6(e) prohibits those with information about the workings of the grand jury from revealing such information to other persons who are not authorized to have access to it under the Rule. The Rule does not contain a prohibition against the continued use of information by attorneys who legitimately obtained access to the information through the grand jury investigation.\textsuperscript{195}]

The Court went on to hold that such an attorney need “not obtain a court order before refamiliarizing himself or herself with the details of a grand jury investigation.”\textsuperscript{196}

While the Supreme Court’s decision in *John Doe* effectively refuted the Second Circuit’s suggestion that an attorney who conducted or participated in a grand jury investigation must be excused from any subsequent civil proceedings, the Court’s decision leaves unanswered the question of what use that attorney can make of the grand jury information in the civil suit. The Court accepted the Second Circuit’s finding that the filing of the civil complaint in this case did not itself disclose grand jury information.\textsuperscript{197} After noting that the complaint did not quote from or refer to grand jury transcripts, nor to documents subpoenaed by or witnesses called before the grand jury, the Court observed that “[a] Government attorney may have a variety of uses for grand jury material in a planning stage, even though the material will not be used, or even alluded to, in any filing or proceeding.”\textsuperscript{198}

Using the guidance that the Supreme Court has provided in *John Doe*, prosecutors who have conducted or participated in prior grand jury investigations should be able to draft and file a complaint pursuant to section 1345 without violating Rule 6(e) in virtually all instances. The summary nature of the allegations contained in the complaint generally will not require any quote from or reference to a grand jury transcript, nor any reference to persons called as witnesses before or documents subpoenaed by the grand jury. Immediately after the complaint is filed, however, the prosecutor will need

\textsuperscript{194} *Id.* at 1658; see *supra* note 150 and accompanying text.
\textsuperscript{195} *Id.* at 1660.
\textsuperscript{196} *Id.* at 1662.
\textsuperscript{197} *Id.* at 1661.
\textsuperscript{198} *Id.*
to rely on evidence collected during the course of the grand jury investigation to prove the allegations contained in the complaint for injunctive relief. The Supreme Court specifically refrained from addressing this use of grand jury information in its decision in *John Doe.*\(^{199}\)

To the extent that a section 1345 proceeding is construed to be a civil case, the attorney for the government could elect to seek a disclosure order pursuant to Rule 6(e)(3)(C)(i) of the Federal Rules of Criminal Procedure for use prior to or in connection with a judicial proceeding. The scope of the court's order would govern the use of grand jury material in the section 1345 proceeding. Of course, if the proceeding is deemed to be a criminal one, the attorney for the government could still seek a Rule 6(e)(3)(C)(i) order to resolve any issue with regard to disclosure. The question is whether such an order is necessary before the attorney for the government can use grand jury information in the litigation of a section 1345 proceeding. The threshold inquiry would seem to be whether an attorney who litigates an injunction pursuant to this section is involved in the litigation of a criminal or civil case.

When the grand jury conducts its investigation and returns an indictment alleging violations of the mail, wire, and/or bank fraud statutes,\(^ {200}\) the attorney for the government is under no obligation to seek a court order before using grand jury information to prove the allegations contained in the indictment. If the government chooses to litigate the indictment prior to the injunction, no court order will be necessary before litigating the injunction proceeding. Section 1345 provides that if an indictment has been returned against the respondent, discovery will be governed by the Federal Rules of Criminal Procedure.\(^ {201}\) Rule 16(a)(1)(C) of those rules requires the government to allow the defendant to inspect and copy all books, papers, documents, etc., which are in the government's possession and are either material to the preparation of the defendant's case or intended for use by the government as evidence. Congress could not possibly have intended to require the attorney for the government to seek an order pursuant to Rule 6(e)(3)(C)(i) in order to disclose the information which Congress had already mandated in Rule 16(a)(1)(C). The order pursuant to Rule 6(e)(3)(C)(i) is within the sound discretion of the supervising judge. To require such an order in an injunction proceeding where the defendant has already been indicted could subject the attorney for the government to the untenable situation of being

\(^{199}\) The Court decided that case "[w]ithout addressing the very different matter of an attorney's disclosing grand jury information to others inadvertently or purposefully, in the course of a civil proceeding ...." *Id.* at 1662.


required to disclose material pursuant to Rule 16(a)(1)(C), while simultaneously being prohibited from that disclosure because the supervising judge determined that the request for disclosure did not meet the particularized test of *Sells Engineering*202 and *Petrol Stops*.203 Congress did not intend to interject the judiciary into routine discovery proceedings in which there is no dispute between the government and defense with regard to the required disclosures.

Is a contrary result required if the government chooses to litigate the injunction proceeding prior to indicting the respondent? If the government chooses not to indict the respondent, will it be prohibited from litigating a section 1345 injunction without first securing a Rule 6(e)(3)(C)(i) order? If the government seeks such an order, but the government’s application is denied, is the government prohibited from seeking to enjoin fraudulent activity even if it is in possession of proof by a preponderance of the evidence? There is an articulable basis to believe that Congress intended section 1345 to be a criminal proceeding, the litigation of which was not intended to be impeded by the necessity of securing disclosure orders pursuant to Rule 6(e)(3)(C)(i).

First, Congress chose to place the remedy in Title 18 of the Code, rather than in Title 28 or the titles which govern the mails, wires, and banking institutions. The proceedings involved in *Sells Engineering* and *John Doe* were civil in nature. The underlying statute was located in Title 28, and the suits both sought money damages. Therefore, the injunction pursuant to a section 1345 criminal proceeding is clearly distinguishable from the situation presented in those cases.

Second, Congress tied the injunction to proof that the respondents were engaged in specific criminal conduct. In order to establish the basis for an injunction pursuant to section 1345, the government must prove that the defendant’s conduct includes the perpetration of mail, wire, and/or bank fraud. The evidence to prove both the underlying criminal violation and the petition for the injunction are exactly the same. The elements of the underlying criminal violation and the cause of action pursuant to section 1345 are likewise the same, with one exception. In order to establish the elements necessary to issue the injunction, the government must establish not only the criminal violation, but also show a reasonable likelihood that the conduct will continue. This difference in the elements, however, is of no practical

202. See supra note 172 and accompanying text.
203. See supra note 175 and accompanying text.
consequence. There is no danger that the attorney for the government would manipulate the grand jury into investigating issues irrelevant to the criminal charge in order to prove the case for an injunction because if ongoing criminal conduct is involved, that is itself a legitimate area of inquiry for the grand jury.

Third, Congress created the remedy because it viewed the traditional criminal tools to be too slow and ineffective to terminate the criminal conduct and designed the section 1345 injunction to supplement the existing criminal tools. Treating the filing and litigation of section 1345 proceedings as anything other than an exercise of the prosecutor's duties under the criminal law renders the tool ineffective to accomplish the legislative purpose of the Act. Congress must have known that the attorney for the government assisting the grand jury in its investigation and his staff would be the only persons who knew of the illegal conduct and had sufficient information to file the complaint in the section 1345 injunctive proceeding. If Congress did not intend the section 1345 injunction to be part of the government attorney's duties in enforcement of the criminal law, then the effect would be to require a 6(e)(3)(C)(i) order, with resultant disclosure of only a limited scope of documents and testimony. If Congress did not intend the section 1345 proceeding to be criminal in nature, the most likely result would be to effectively deny the person with the most knowledge the opportunity to enjoin the crime. If Congress did not intend the section 1345 injunction to be criminal in nature, the likely result would be extended delays inherent in civil discovery before the government would be prepared to proceed to trial on the merits. Congress acted to protect government investigative files by providing that post-indictment discovery would be pursuant to the more restrictive criminal rules, rather than the civil rules, which are more advantageous to the defense. It is inconceivable that Congress intended an injunction be postponed until after an indictment before seeking a 6(e)(3)(C)(i) order to avoid the “discovery for civil purposes” concern which the Supreme Court had voiced so clearly just one term before in *Sells Engineering*. Yet this is exactly the result of concluding that the section 1345 injunction is not part of the government attorney's duties in enforcing the criminal law.

Fortunately, many section 1345 injunction cases will not require resolution of this issue. In some instances, the government's criminal investigation will be entirely administrative and there will be no grand jury information to be disclosed. In other cases, the criminal investigation might be a mixture of administrative and grand jury proceedings, and the attorney can certify by affidavit that no grand jury information is being used for the civil suit.

In cases where the grand jury conducts an investigation giving rise
to evidence supporting an injunction, the preferred course of action would be for the prosecutor to seek an order pursuant to Rule 6(e)(3)(C)(i) authorizing the use and disclosure of the grand jury material as being preliminary to or in connection with a judicial proceeding. If the prosecution has received the 6(e) order, there is no question but that use of the grand jury information is authorized. The prosecutor who secures a 6(e) order should never have to face the issue of a contempt citation for having willfully disclosed grand jury information while litigating a section 1345 injunction.\textsuperscript{204} Even if the prosecutor has not secured a 6(e) order, however, a strong case can be made that a section 1345 injunctive proceeding is criminal in nature and part of the government attorney’s duties in the enforcement of federal criminal law. In that case, for the purposes of the disclosure requirements of Rule 6(e), the section 1345 proceeding is indistinguishable from trial pursuant to an indictment alleging violations of Title 18, United States Code, sections 1341, 1343 or 1344.

\textbf{IX. CONCLUSION}

The injunction proceeding pursuant to section 1345 is a viable tool to be used by the United States in its efforts to combat boiler room fraud and other investment fraud. The injunction can be used in conjunction with traditional criminal prosecutions, or in lieu of prosecutions in those cases where the government determines that criminal prosecution is not warranted. The injunction can also be used to terminate fraudulent activity much quicker than would be possible if the government limited itself to the traditional, long-term criminal investigation leading to indictment. While the section 1345 injunction has yet to become a frequently used tool, the government is beginning to derive benefits from its use.\textsuperscript{205}

When enacting section 1345, Congress left open several questions with regard to the use of grand jury information which are critical to the implementation of the statute. In reality, most investigations of large and complex mail, wire and bank fraud schemes are conducted by grand juries. The issue regarding the use of grand jury information by the attorney for the government in the litigation of section 1345 proceedings is something that federal prosecutors face every

\textsuperscript{204} \textit{Fed. R. Crim. P.} 6(e)(2).

\textsuperscript{205} \textit{See United States v. Alvin Petroleum Corp.}, No. 87-6626-CIV-Paine, (S.D. Fla. 1987) (enjoining the fraudulent promotion of partnership interests in oil and gas wells and ordering an accounting and disgorgement of profits).
day. Uncertainty with regard to how grand jury information can be utilized in this context has a chilling effect upon the willingness of federal prosecutors to utilize the section 1345 proceeding. Congress can make the injunction against fraud a more potent weapon by clarifying the guidelines regarding the use of grand jury information in these proceedings and by removing all obstacles to the unfettered use of this information in the litigation of section 1345 proceedings.