

**UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK**

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STATE FARM MUTUAL AUTOMOBILE :
INSURANCE CO. and STATE FARM FIRE & :
CASUALTY CO., :
:

Plaintiffs, :

-against- :

EASTERN MEDICAL, P.C., MEDICAL :
ACUPUNCTURE SERVICES, P.C., ROBERT :
HARD, M.D., ELVIN RUIZ, M.D., JOSEPH :
MORRIS A/K/A JOSEPH CAROLLO, BAYSIDE :
MANAGEMENT, INC., MANAGEMENT :
SERVICE ORGANIZATION, INC., LAI FAN XUE, :
CHENG HE SU, LI LI ZHANG, QUN LIU, RUN :
SHENG XIE, and YAN YAN YU, :

Defendants. :

MEMORANDUM & ORDER

05-CV-3804 (ENV) (RML)

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VITALIANO, D.J.

Plaintiffs State Farm Mutual Automobile Insurance Company and State Farm Fire & Casualty Company (collectively "State Farm") bring this action against defendants Eastern Medical, P.C. ("Eastern"), Medical Acupuncture Services, P.C. ("MAS"), and Joseph Morris a/k/a Joseph Carollo ("Carollo") (collectively, the "management defendants"), as well as Robert Hard, M.D., Elvin Ruiz, M.D., Bayside Management, Inc. ("Bayside"), Management Service Organization, Inc. ("MSO"), Lai Fan Xue, Cheng He Su, Li Li Zhang, Qun Liu, Run Sheng Xie, and Yan Yan Yu (collectively, the "acupuncture defendants"). State Farm's first amended complaint ("the complaint") alleges that, under New York's no-fault auto insurance regime, defendants filed over 600 fraudulent claims for medically unnecessary acupuncture treatments, totaling over \$1.9 million, in violation of the Racketeering Influenced and Corrupt Organizations Act, 18 U.S.C. § 1961 et seq. ("RICO"), and constituting fraud under New York common law.

State Farm seeks to recoup payments already made to Eastern and MAS, and it also seeks a declaratory judgment denying Eastern and MAS any right to payment on claims still pending with State Farm. Defendants have filed two motions to dismiss¹ pursuant to Fed. R. Civ. P. 12(b)(6); they have also moved under Fed. R. Civ. P. 21 for severance of the state law claims. For the reasons stated below, State Farm's common law fraud claims are dismissed to the extent they are based solely on fraudulent licensure and arise from payments made before April 4, 2002; the balance of the motions are denied.

DISCUSSION

To survive dismissal, a complaint must allege "enough facts to state a claim to relief that is plausible on its face." Bell Atlantic Corp. v. Twombly, 550 U.S. 544, 570, 127 S. Ct. 1955, 1974 (2007). A mere "formulaic recitation of the elements of a cause of action" is insufficient; a complaint must also allege facts that "raise a right of relief above the speculative level . . . on the assumption that all allegations in the complaint are true." Id., 550 U.S. at 555, 127 S. Ct. at 1965 (citation omitted).

State Farm contends that various defendants committed substantive RICO violations as well as RICO conspiracy. Substantive RICO claims must allege: "(1) that the defendant (2) through the commission of two or more acts (3) constituting a 'pattern' (4) of 'racketeering activity' (5) directly or indirectly invests in, or maintains an interest in, or participates in (6) an 'enterprise' (7) the activities of which affect interstate or foreign commerce." Moss v. Morgan Stanley, Inc., 719 F.2d 5, 17 (2d Cir. 1983) (quoting 18 U.S.C. § 1962(a)-(c)). The racketeering

¹ One motion was filed by the acupuncture defendants, in which the management defendants joined; a second motion was filed separately by the management defendants. The Court addresses both motions in this Order.

activities, such as the acts of mail fraud alleged in the complaint, constitute the predicate acts on which the RICO violations are based.

State Farm's RICO allegations, the Court finds, are sufficient to survive dismissal at the pleading stage. First, defendants' arguments regarding reasonable reliance are misplaced: reasonable reliance is not an element of a RICO claim predicated on mail fraud, Bridge v. Phoenix Bond & Indem. Co., 553 U.S. 639, 661, 128 S. Ct. 2131, 2145 (2008), and even if it were, "[t]he issue of reasonable reliance [is] more appropriately decided on a motion for summary judgment rather than a motion to dismiss," Allstate Ins. Co. v. Valley Phys. Med. & Rehab., P.C., No. 05-CV-5934, 2009 WL 3245388, at *9 (E.D.N.Y. Sep. 30, 2009); see also Republic of Colombia v. Diageo N. Am. Inc., 531 F. Supp. 2d 365, 446 n.28 (E.D.N.Y. 2007); AIU Ins. Co. v. Olmecs Medical Supply, Inc., 2005 WL 3710370, at *14 (E.D.N.Y. Feb. 22, 2005).²

Defendants next argue the lack of a continuous pattern of racketeering activity, claiming that State Farm is artificially separating its fraud allegations in order to satisfy the RICO pleading standard. But the cases cited by the management defendants (Mgmt. Defs.' Reply Br. 11-12) each involve a single transaction, act, or attempt at extortion, whereas State Farm alleges at least 600 separate and temporally distinct acts of mail fraud in the form of fraudulent no-fault benefit claims assigned by hundreds of individual assigners. This pattern of activity, spanning a period from 2000 to 2007, easily satisfies the continuity requirement of RICO.³

² The cases on which defendants rely, Blue Cross and Blue Shield of New Jersey v. Philip Morris, Inc., 113 F. Supp. 2d 345 (E.D.N.Y. 2000), and Grumman Allied Indus. v. Rohr Indus., Inc., 748 F.2d 729 (2d Cir. 1984), are both inapposite because they involved grants of summary judgment rather than Rule 12 dismissal. See also Republic of Colombia, 531 F. Supp. 2d at 446 n.28 (considering same two cases and reaching same result).

³ The management defendants also allege a lack of continuity as to them, contending (1) that

As for whether the predicate acts of racketeering activity were properly pled, defendants' argument that they are not is fundamentally flawed. The claimed RICO violations, first of all, are predicated not on New York common law fraud as defendants argue (Acupuncture Defs.' Memo. 16), but on federal mail fraud. See Bridge, 553 U.S. at 653, 128 S. Ct. at 2141 ("Congress chose to make mail fraud, not common-law fraud, the predicate act for a RICO violation."). As a result, their attack on the pleading grounded in supposed inadequacies under New York law misses the mark.⁴ Moreover, numerous decisions in this district have held that similarly alleged schemes to defraud New York no-fault insurers satisfy the standards for pleading RICO claims predicated on the federal mail fraud statute. See, e.g., Allstate Ins. Co. v. Etienne, No. 09-CV-3582, 2010 WL 4338333 (E.D.N.Y. Oct. 26, 2010); Allstate Ins. Co. v. Halima, No. 06-CV-1316, 2009 WL 750199 (E.D.N.Y. Mar. 19, 2009); State Farm Mut. Auto. Ins. Co. v. Liguori, 589 F. Supp. 2d 221 (E.D.N.Y. 2008); State Farm Mut. Auto. Ins. Co. v. CPT Med. Servs., P.C., No. 04-CV-5045, 2008 WL 4146190 (E.D.N.Y. Sep. 5, 2008).

Notwithstanding, the management defendants independently argue that they did not participate in the "operation or management" of the alleged enterprises (Eastern and MAS) as RICO requires, see, e.g., Reves v. Ernst & Young, 507 U.S. 170, 185, 113 S. Ct. 1163, 1173 (1993), and so dismissal as to them is still appropriate. State Farm, however, has pled sufficiently detailed allegations of how the management defendants established, controlled, and

their only alleged malfeasance was fraudulent incorporation, and (2) that MAS's alleged involvement was too short. To the contrary, the complaint contains allegations of numerous actions by Morris, Bayside, and MSO throughout the relevant time period, all part of the overall mail fraud scheme pled in the complaint.

⁴ However, even if the Court were to examine the RICO allegations under New York law rather than federal law, the result would be the same, as State Farm's claims of fraud under New York law are also adequately pled. See infra at 6-7.

directed Eastern and MAS, surviving Rule 12. Cf. Allstate Ins. Co. v. Rozenberg, 590 F. Supp. 2d 384, 391-92 (E.D.N.Y. 2008); CPT Med. Servs., 2008 WL 4146190, at *11.

Defendants then make a frivolous argument that Eastern and MAS are alleged to be both enterprises and participants in the racketeering scheme, failing to satisfy RICO's distinctiveness requirement. "[U]nder Section 1962(c), it is well-established that the alleged 'enterprise' through which a pattern of racketeering activity is conducted must be distinct from those persons or entities who stand accused of conducting that racketeering activity." Rozenberg, 590 F. Supp. 2d at 390 (citing Riverwoods Chappaqua Corp. v. Marine Midland Bank, N.A., 30 F.3d 339, 344 (2d Cir. 1994)). In fact, State Farm did not name Eastern or MAS as defendants in any of the RICO claims, and so, as to them, there are no such claims to dismiss.

Finally, defendants assert that, even if the RICO claims were properly pled, they are partially, if not fully, barred by the statute of limitations. Such an assertion, however, is premature. Determining when State Farm knew or should have known of its alleged injuries and the peccancies of defendants would require the Court to look beyond the complaint. If anything, this argument is more appropriately addressed in a motion for summary judgment. See State Farm Mut. Auto. Ins. Co. v. Grafman, 655 F. Supp. 2d 212, 226 (E.D.N.Y. 2009) ("[T]here is insufficient information to determine whether, as a matter of law, plaintiff 'knew or should have known' of the injury from defendants' alleged scheme within the limitations period."); see also Allstate Ins. Co. v. Halima, 2009 WL 750199, at *6; CPT Med. Servs., 2008 WL 4146190, at *7.

On a different slant, State Farm also properly pleads the existence of a RICO conspiracy. In order to survive dismissal on a § 1962(d) claim, a "plaintiff must allege only that defendants agreed to commit at least two predicate RICO acts, not that defendants themselves committed the two predicate acts, or even that these acts were carried out." State Farm Mut. Auto. Ins. Co. v.

CPT Med. Servs., P.C., 375 F. Supp. 2d 141, 150-51 (E.D.N.Y. 2005) (citing Salinas v. United States, 522 U.S. 52, 64, 118 S. Ct. 469, 476-77 (1997)). The complaint theorizes and avers that each submission of a fraudulent insurance claim to State Farm was a predicate act of mail fraud under RICO, and the complaint adequately alleges that each relevant defendant agreed to the commission of multiple acts of mail fraud.

Shifting gears again, the complaint contains adequate allegations to state claims of New York common law fraud too. Defendants' arguments fall short one more time. First, defendants assert that, under New York licensing law, acupuncture falls within the ambit of medicine and thus licensed physicians may legally practice acupuncture. This view is completely unsupported. Since 1991, acupuncture and medicine have been governed by different sections of New York Education Law, and each has its own separate licensing regime. See 1990 N.Y. Sess. Laws 772 (McKinney); N.Y. Educ. Law § 8210 et seq. (acupuncture); N.Y. Educ. Law § 6520 et seq. (medicine). Medical licenses do not automatically permit physicians to practice acupuncture; if they wish to do so, they must satisfy separate state certification requirements. See 8 N.Y. Comp. Codes R. & Regs. § 60.9; see also, e.g., Quality Medical Care, P.C. v. New York Cent. Mut. Fire Ins. Co., 26 Misc. 3d 139(A), 907 N.Y.S.2d 440 (N.Y. App. Term 2010) (“Physicians are not authorized to practice acupuncture by virtue of their medical licenses; rather, they must satisfy [state] certification requirements if they are to practice acupuncture.”) (citing 8 N.Y. Comp. Codes R. & Regs. § 60.9; N.Y. Educ. Law §§ 8212, 8216(3)). Indeed, in cases similar to the one presented here, professional corporations relying solely on physicians to provide acupuncture have been ruled ineligible to receive New York no-fault benefits. See, e.g., Quality Medical Care, 26 Misc. 3d 139(A), 907 N.Y.S.2d 440; 563 Grand Medical, P.C. v. Allstate Ins. Co., 6 Misc. 3d 1019(A), 800 N.Y.S.2d 346 (N.Y. Civ. Ct. 2005).

Second, defendants argue that New York's "30-day rule," requiring that insurers process no-fault claims within 30 days, see N.Y. Ins. Law § 5106(a); 11 N.Y. Comp. Codes R. & Regs. § 65-3.8, precludes State Farm's claims for fraud. They contend that, as a no-fault insurer in New York, State Farm is required to process claims within 30 days and, once payments were made, is precluded from recovering the payments on the basis of fraud, including fraudulent billing based on lack of medical necessity, or, pursuant to 11 N.Y. Comp. Codes R. & Regs. § 65-3.16(a)(12), fraudulent licensure.

The law suggests, however, that the 30-day rule does not have such preclusive effect on an insurer's affirmative fraud claims. Many courts in this district have reached a diametrically different conclusion. See Grafman, 655 F. Supp. 2d 212; Liguori, 589 F. Supp. 2d 221; CPT Med. Servs., 2008 WL 4146190; Allstate Ins. Co. v. Valley Phys. Med. & Rehabilitation, P.C., 555 F. Supp. 2d 335 (E.D.N.Y. 2008) (granting motion for reconsideration and vacating prior decision dismissing fraud claims); State Farm Mut. Auto. Ins. Co. v. Kalika, 04-CV-4631, 2006 WL 6176152 (E.D.N.Y. Mar. 31, 2006). This law, in turn, is premised upon the New York Court of Appeals' ruling in State Farm Mut. Auto Ins. Co. v. Mallela, 4 N.Y.3d 313, 794 N.Y.S.2d 700, 827 N.E.2d 758 (2005). Succinctly, defendants' sweeping argument is undermined by New York's high court interpretation of the relevant state law, agency regulations, and then by post-Mallela federal case law.

Of course, what is left, in any event, is whether State Farm can recoup payments made before April 4, 2002, when the fraudulent licensure provision went into effect. Mallela cuts against State Farm this time, as it does indeed bar recovery for payments made before that date, where the payments were induced by fraudulent licensure. Id. Yet, significantly, the fraud claims in Mallela were premised *only* on fraudulent licensure; there were no allegations of

fraudulent billing as there are here. Id. at 320. As to this variety of fraud, the April 4, 2002 date in Mallela is inapposite. See CPT Med. Servs., 2008 WL 4146190, at *9. Therefore, State Farm's New York common law fraud claims are dismissed to the extent that they rely solely on fraudulent licensure and stem from payments made before April 4, 2002.

Next defendants argue that the declaratory judgment claims should be dismissed for want of jurisdiction. To determine whether declaratory judgment jurisdiction exists, courts must consider "(1) whether the judgment will serve a useful purpose in clarifying or settling the legal issues involved; and (2) whether a judgment would finalize the controversy and offer relief from uncertainty." Duane Reade, Inc. v. St. Paul Fire & Marine Ins. Co., 411 F.3d 384, 389 (2d Cir. 2005). Defendants argue that State Farm is litigating a hypothetical theory rather than resolving a current controversy. But, quite the opposite, there is an obvious dispute between the parties, as State Farm demands a judgment that it need not pay claims it has already received from defendants, that is, one party has demanded payment, and the other denies obligation to pay. It is difficult to imagine a clearer example of a ripe dispute. Moreover, adjudication of the declaratory judgment claims would certainly "serve a useful purpose in clarifying or settling the legal issues involved" in whether defendants' alleged scheme constituted violations of RICO and/or were acts of fraud under New York law. Clearly, a judgment one way or the other would finalize the controversy regarding real and pending unpaid claims. The Court thus has jurisdiction over State Farm's declaratory judgment claims for they are ripe for resolution.⁵

Lastly, defendants argue that, "assuming the Court dismisses the Federal claims while ruling that the Plaintiffs have properly pleaded a cause of action for common law fraud, it should

⁵ Defendants initially argued that the Court should abstain from considering the declaratory judgment claims. Their argument was later withdrawn. (Acupuncture Defs.' Reply Br. 19.)

sever and dismiss the State Law claims” pursuant to Fed. R. Civ. P. 21. (Acupuncture Defs.’ Memo. 33.) The argument is academic, and the motion it underlies is denied on that ground.

CONCLUSION

For the foregoing reasons, State Farm’s New York common law fraud claims (Counts IV and VIII) are dismissed to the extent that they rely solely on fraudulent licensure and stem from claim payments made before April 4, 2002. Defendants’ motions are otherwise denied.

SO ORDERED.

Dated: Brooklyn, New York
December 16, 2010

ERIC N. VITALIANO
United States District Judge