



Wine Institute Fights to End Illinois False Claims/Use Tax Prosecutions

The Venue

- The action was filed in Chicago in the State courts, in the Circuit Court of Cook County.

The Plaintiffs

- The following entities, Chimney Rock Winery, LLC, the Miner Family Winery, LLC, Staglin Family Vineyards, LLC and the Wine Institute (the "Wineries") are filing suit.
- The Plaintiffs are represented by Michael Wynne and Adam Beckerink, attorneys in the Chicago office of Reed Smith LLP.

The Defendants

- The Illinois Department of Revenue (the "Department"), and the Illinois Attorney General (the "Attorney General").

The Controversy

- The action was filed as one reaction to hundreds of Illinois False Claims Act (the "IFCA") prosecutions that the Attorney General has allowed a private attorney/firm, Stephen B. Diamond, P.C. ("Diamond"), to bring on his own and on the State's behalf against Wineries that made internet sales to Mr. Diamond.
- Diamond claims that the Wineries should have charged tax on the shipping fees for his online purchases delivered to Illinois. The Illinois Supreme Court held in *Kean v. Wal-Mart Stores, Inc.*, 235 Ill. 2d 351 (2009) that in an online sale the shipping charges were part of the selling price, and therefore taxable, where the customer did not have another option for obtaining the product purchased and thus an inseparable link was created between the delivery of the item and the sale of merchandise. Diamond claims delivery is inseparably linked in his purchases.
- The Department's regulation, unaltered after the *Kean* decision, provides that delivery charges are *deemed* to be agreed upon separately from the selling price of the purchased item, and are therefore not taxable, so long as the seller requires a separate charge for delivery and so long as the charges designated as transportation or delivery or shipping and handling are actually reflective of the costs of such shipping, transportation or delivery. 86 Ill. Admin. Code §130.415(d). Diamond exploits the Wineries reliance on the Department's regulation.
- Many Wineries would not, under the Department's regulations, owe any tax when they have documentation which demonstrates that the purchaser had the option of taking delivery of the wine at the seller's location. Declining that option renders the shipping charges not taxable because they are separately agreed upon, and Illinois does not tax transportation services.

- The Attorney General has authorized Diamond to proceed, and has participated in, approved, and received a statutory share of settlements, in cases claiming that the seller's pick-up location must be within Illinois for the regulation to result in no tax on the shipping charge.

Was Litigation Avoidable?

- The Wine Institute, on behalf of its members, explored administrative and legislative options for solutions to stop the actions against its members, with direct and indirect discussions with the Attorney General, the Department of Revenue, members of the legislature and other interested parties. Illinois' massive budget problems have foreclosed progress on many important issues, including ours.
- The Wine Institute arranged Illinois counsel for members to consult if they received purchase orders or summonses from Diamond.
- Counsel for many of our members advised us that the Attorney General had authorized cases to go forward even when counsel had advised the Attorney General that:
 - there were prior sales and use tax audits of the Wineries, in which the auditor found no liability on the issue;
 - some of the Wineries were already under audit on the issue, so Diamond was not bringing new information to the State;
 - there were Wineries that paid the tax on the issue, despite the Department's regulation stating that the charges were not taxable, and the Department ordered no penalties to be imposed, and
 - certain Wineries' websites allowed customers the option to pick up their wine at the seller's location and, that based on such facts, some Wineries received Private Letter Rulings from the Department that their shipping charges were not taxable.

What Will the Lawsuit Do?

- The Plaintiffs are asking for three things:
 - For the court to enjoin the Attorney General from authorizing any IFCA prosecution without first establishing that the Department: (i) agrees with the interpretation of the tax law; (ii) would not, based on the facts alleged, abate any penalty; and (iii) would, if it encountered the facts alleged, impose a negligence or fraud penalty under the tax laws.
 - For the Department to implement procedures by which targets of IFCA prosecutions can obtain an abatement of taxes paid as a result of a position authorized by the Attorney General that is contrary to the Department's regulations.
 - For the Attorney General to review all pending IFCA prosecutions and take steps to conform the positions authorized there with the declarations the court may make in the litigation initiated by the Wine Institute.

What are the Claims Made in the Lawsuit?

- The Plaintiffs claim that:

- The Attorney General, by reserving the non-taxable treatment of the Department's regulations only for sellers that offer an Illinois location for purchasers to exercise the option of picking up their purchases at the seller's location, but not allowing it for sellers whose location is outside Illinois, is discriminating against interstate commerce in a manner prohibited by the Dormant Commerce Clause of the United States Constitution.
- The Attorney General has targeted Internet Vendors and electronic commerce in violation of the anti-discrimination provisions of the Internet Tax Freedom Act.
- The Attorney General has exercised legislative authority by superseding the Department's regulations with its own positions on Illinois tax law and broadly applying them to Internet Vendors without adopting those positions as a regulation in conformity with State law, and has therefore violated the Separation of Powers provisions of the Illinois Constitution of 1970.
- The Department has failed to implement the provisions of the Taxpayers' Bill of Rights, that require the abatement of tax, penalty and interest that is assessed based on reliance on erroneous written information of the Department, for taxpayers that are made to pay tax by the Attorney General on positions contrary to the Department's regulations.

Are There More Cases? What Do I Do if I Have Been Sued?

- IFCA cases are filed "under seal," meaning they remain secret until the Attorney General authorizes them to proceed by unsealing. Therefore, it is possible there are more cases on file than we know about because they have yet to be unsealed.
- Unsealed IFCA prosecutions will proceed, regardless of what occurs in the Wine Institute case, unless and until the Attorney General agrees or is ordered in the Wine Institute case to take some action to end the prosecution or modify the State's position in such cases.
- If you receive a summons in an IFCA case, you should seek legal representation in Illinois to prevent a default judgment establishing liability against you.
- If you receive an order from an Illinois purchaser that seems unusual, *e.g.*, the shipping charge will be in excess of the purchase price, or more than one order to the same location by different purchasers, or to a business address in Chicago, feel free to contact the Wine Institute and we will put you in touch with someone who can advise you of appropriate options to avoid an IFCA prosecution or to establish a defense to the IFCA prosecution.