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11	SUPERIOR COURT OF CALIFORNIA		
12	COUNTY OF SAN DIEGO		
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14	THE PEOPLE OF THE STATE OF CALIFORNIA, ex rel. BILL LOCKYER, ATTORNEY	Case No	
15	GENERAL OF THE STATE OF CALIFORNIA,	COMPLAINT FOR INJUNCTION, CIVIL	
16	Plaintiff,	PENALTIES, AND OTHER RELIEF (Bus. & Prof. Code, §§	
17	v.	17200, 17500 and Rev. and Tax. Code, § 30101.7(d))	
18	eSMOKES, INC, a Florida Corporation, doing	Code, § 30101.7(d))	
19	business as WWW.ESMOKES.COM and WWW.CIGARETTESBYMAIL.COM, GARY		
20	E. KIRSCHNER, an individual, and DOES 1 through 15, inclusive,		
21	Defendants.		
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23	The People of the State of California, through Bill Lockyer, Attorney General of the		
24	State of California, hereby allege on information and belief as follows:		
25	<u>INTRODUCTION</u>		
26	Youth smoking is a serious pediatric health problem in California and the rest of the		
27	nation. More than 80% of regular smokers began smoking as children. Every day in the United		
28	States more than 2,000 children begin smoking cigarettes, a	and one-third of those children will one	
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day die from tobacco-related disease. It has been shown that the younger a person begins smoking, the more likely it is that he or she will be unable to quit in later life and will suffer a disease attributable to tobacco use. Recent studies indicate that youth demonstrate signs of addiction after smoking only a few cigarettes. Exacerbating these problems, an estimated 690 million packs of cigarettes are sold illegally to children each year nationwide.

Defendants are cigarette sellers who advertise and sell cigarettes over the Internet to California consumers and consumers in other states. Defendants state on their web sites that purchasers must be 21 years of age or older to purchase cigarettes from defendants. However, defendants in fact facilitate and promote the purchase of cigarettes by children because although defendants presently claim on their web sites that they require potential purchasers to provide age verification upon the initial delivery of tobacco products, defendants do not in fact require faceto-face or otherwise adequate verification of age and identity of would-be purchasers upon delivery. The People have documented that defendants have sold cigarettes to children in California from their web sites on nine occasions. The People have informed defendants several times that the People had documented sales to minors from their web sites. Defendants have been similarly informed by New York City on a another occasion. Notwithstanding the fact that they have been so notified, defendants have not taken adequate precautions to ensure that children cannot purchase and receive delivery of cigarettes from their web site. Specifically, defendants fail or refuse to put in place effective safeguards so as to prevent or seriously discourage further sales to minors. By refusing to do so and completing sales of cigarettes to minors, defendants are encouraging and allowing children to purchase cigarettes from their web sites, thus undermining the State's efforts to reduce smoking by minors.

Defendants, in violation of state law, also fail or refuse to either pay taxes owed on cigarettes shipped into California or notify purchasers that they are responsible for taxes owed. In violation of federal law, defendants fail or refuse to report the shipments of cigarettes into the state, including the identity of the purchasers, to the California Board of Equalization ("BOE"), the entity responsible for collecting those taxes. Defendants' also induce consumers to purchase their cigarettes by false and misleading statements on defendants' web sites in which they

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misrepresent both defendants' obligation to report to the BOE shipments of cigarettes into California and California consumers' obligation to pay California taxes on cigarettes purchased over the Internet from defendants and shipped into California.

The People also bring this action pursuant to California's unfair competition statutes, to protect the public from defendants' misleading, unlawful, unfair, and fraudulent business practices. These practices include selling cigarettes to children, failing or refusing to institute adequate procedures and safeguards to ensure that children cannot buy cigarettes from their web sites and that cigarettes cannot be delivered to children, failing or refusing to comply with federal reporting requirements with respect to their Internet cigarette sales to California consumers, and making deceptive or misleading statements concerning defendants' obligation to comply with these federal reporting laws and consumers' obligation to pay California taxes on cigarettes purchased from defendants over the Internet. Defendants' conduct also violates a statute, effective January 1, 2003, enacted for the purpose of ensuring compliance with specific requirements concerning payment of applicable state taxes for cigarettes purchased over the Internet or by mail order.

PARTIES

1. Bill Lockyer is the duly elected Attorney General of the State of California and is the chief law enforcement officer of the state (Cal. Const., art. 5 § 13.) He is authorized by Business and Professions Code sections 17204 and 17206 to bring actions, in his official capacity, to enforce the state's statutes regulating unfair competition. He is also authorized by Revenue and Taxation Code section 30101.7, subdivision (e) to bring actions to facilitate the collection of all applicable state surtaxes and sales or use taxes on cigarettes sold to California residents over the Internet or by mail order. Additionally, he is authorized to assess civil penalties against any entity violating Business and Professions Code section 22963 which, among other things, prohibits both distribution of tobacco products directly or indirectly to persons under the age of 18 through common carriers, and delivery of tobacco products to an address other than the consumer's verified billing address.

Complaint for Injunction, Civil Penalties, and Other Relief

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- 2. Defendants, eSMOKES, Inc., doing business as WWW.eSMOKES.COM and WWW.CIGARETTESBYMAIL.COM (collectively referred to as "eSmokes"), and GARY E. KIRSCHNER, an individual, are cigarette retailers who advertise and sell cigarettes over the Internet to California residents. Defendants receive Internet orders from California residents and ship the orders by common carrier to California.
- 3. eSmokes is, and during the relevant time period was, a Florida corporation with its principal place of business located at 201 South Main, Lowell, North Carolina 28098. eSmokes sells cigarettes over the Internet by operating web sites at www.eSmokes.com and www.cigarettesbymail.com through which cigarettes are advertised and sold to California residents.
- 4. Defendant Gary E. Kirschner ("Kirschner") is and at all relevant times was, President and CEO of eSmokes, Inc. In such capacity, and as an individual, Kirschner controls, manages, supervises, and directs the operations and activities of eSmokes, Inc.
- 5. The true names and capacities of the defendants sued herein under the fictitious names of Does One through Fifteen, inclusive, are unknown to plaintiff who therefore sues defendants by such fictitious names. Plaintiff will amend its complaint to show the true names of such defendants when the same have been ascertained. Plaintiff is informed and believes and upon such information and belief alleges, that each of the defendants designated herein as a DOE is legally responsible in some manner for the events and happenings alleged in this complaint.

JURISDICTION AND VENUE

6. The violations of law alleged in this Complaint occurred in San Diego County and in other counties in California or occurred outside of California but were intended by defendants to influence prospective purchasers in California. Defendants purposefully and voluntarily directed their activities toward California consumers and purposefully availed themselves of the privilege of conducting business in California by both soliciting and transacting business in California. Defendants have intentionally targeted California and have sold cigarettes to consumers in San Diego and in other counties in the State of California.

FACTUAL ALLEGATIONS

Sales of cigarettes to minors

- 7. Pursuant to Penal Code section 308(a), every person, firm or corporation which knowingly or under circumstances in which it has knowledge, or should have grounds for knowledge, sells cigarettes to persons under the age of 18 years is subject either to a misdemeanor criminal action or to a civil action punishable by a fine.
- 8. Defendants have knowledge or grounds for knowledge that they are selling cigarettes to children from their web sites. Defendants were notified in writing by Plaintiff's attorney that since on or before August 2001, eSmokes has sold cigarettes from its web sites to children in California on numerous occasions. eSmokes does not have adequate procedures and safeguards in place to ensure that minors cannot receive cigarettes purchased from its web sites.
- 9. The People, along with 39 other states, sent a letter to defendants on September 16, 2002, informing them that they had information documenting sales to minors from defendants' web sites and asking defendants to immediately review their web sites in light of the legal requirements prohibiting the sales of cigarettes to minors. (A copy of this letter is attached as Exhibit "A" and incorporated herein by reference.) Defendant Kirschner responded to that letter by asking for the specifics. The People sent defendants a second letter dated October 1, 2002, informing them that the People had verified sales to minors from their web sites since at least July 2001. The People also notified defendants, in that letter, that as of January 1, 2003, California prohibits the sale of cigarettes over the Internet unless the seller complies with specified requirements including age verification (Bus. & Prof. Code, § 22963) and payment of applicable taxes (Rev. & Tax. Code, § 30101.7). The People also provided defendants with copies of these newly enacted statutes. (A copy of this letter is attached as Exhibit "B" and incorporated herein by reference.) Defendants did not respond to that letter.
- 10. The People sent another letter to defendants on January 23, 2003, informing them that the California Attorney General had documented sales of cigarettes to minors from their web sites on eight occasions beginning in July 2001, and that the New York City Department of Consumer Affairs had documented and notified eSmokes that a minor placed an order for and

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also requested that Defendants enter into a settlement agreement ("agreement") between defendants and a significant number of concerned states. A copy of the proposed agreement setting forth procedures to ensure that children could not purchase cigarettes from their web sites was included in the January 2003 letter. Although defendants received this letter, defendants did not respond in any way.

11. The People documented yet another sale made to a minor by defendants from one of its web sites in February 2003.

Internet Cigarette Sales-Excise Tax Evasion

- 12. Pursuant to Revenue and Taxation Code section 30101.7(d), if an out-of-state retailer does not collect and remit the tax to the State, the consumer purchasing the cigarettes is ultimately liable for the excise tax. Because eSmokes does not collect and remit any of the applicable California taxes, California consumers who purchase cigarettes from eSmokes are responsible for paying these taxes directly to the State.
- 13. Pursuant to the Jenkins Act, 15 U.S.C. section 375 et seq. ("Jenkins Act"), vendors who sell and ship cigarettes in interstate commerce other than to a licensed distributor must register with the tobacco tax administrator of each state shipped to and, on a monthly basis, report (1) the name and address of the persons to whom cigarette shipments were made, (2) the brands of cigarettes shipped, and (3) the quantities of cigarettes shipped. Reports must be filed no later than the 10th day of each calendar month, reporting each and every cigarette shipment made to the state during the previous calendar month. The seller's registration must list the seller's name, trade name, and the address of all business locations.
- 14. The Board of Equalization ("BOE"), the California taxing entity responsible for collecting cigarette taxes, sends letters to out-of-state distributors, companies, or agencies selling cigarettes to California consumers when it learns that these entities have not reported shipments of cigarettes in compliance with the Jenkins Act. Such a letter is referred to as a "Jenkins Act" ///

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letter. If the BOE does not receive a response, it will routinely send a follow-up letter requesting compliance from the entities.

- 15. The BOE sent a Jenkins Act letter to eSmokes on October 7, 1999, requesting that the company report all its shipments of cigarettes to California consumers as required by the Jenkins Act.
- 16. Although eSmokes filed a Jenkins Act report on August 1, 1999, eSmokes has failed or refused to file any reports with the BOE, since that time, of shipments of cigarettes to California consumers as required by section 376 of the Jenkins Act. In fact, eSmokes states on its web sites that "eSmokes.com currently does not distribute, sell or rent your name, email address, or other personal information to any third party without your consent."

Deceptive Advertising

- 17. At all times relevant to this action, defendants were and are required by the Jenkins Act to report shipments of cigarettes into California to the BOE so that the BOE can collect state taxes on those cigarettes
- 18. Defendants represent or imply through false and misleading statements on their we sites that they do not have to comply with the Jenkins Act's reporting requirements. For example, in the section on "Legal Information" on defendants' web sites, defendants state that it '... is the responsibility of the buyer to ascertain and comply with any laws in regard to the purchase and use of any cigarette products."
- 19. To induce consumers to purchase cigarettes from its web sites, defendants do not inform prospective California purchasers of their obligation to pay California taxes on the cigarettes they purchase from eSmokes. Those taxes amount to \$0.87 per package of twenty cigarettes or \$8.70 per carton. eSmokes, according to its web sites, charges taxes in North Carolina, Virginia and Kentucky. These states impose some of the lowest taxes in the country and amount to \$0.05, \$0.2.5 and \$0.03 per pack, respectively, or \$0.50, \$0.25 and \$0.30 per carton, respectively. A California resident may purchase from eSmokes located in North Carolina, Virginia and Kentucky and pay a price that represents an apparent savings of \$8.20, \$8.45 and \$8.40 per carton, respectively.

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- 20. Further, defendants represent or imply through statements on their web sites that federal law exempts California consumers from paying California taxes on cigarette products purchased for personal consumption from an out-of-state retailer even thought the cigarette products are shipped into California. For example, defendants state on their web sites that "federal legislation permits the purchase of cigarette products for personal consumption from out-of-state."
- 21. Additionally, defendants, through statements on their web sites falsely imply that California consumers' are not required to pay California taxes on the cigarettes they purchase from defendants' web sites. For example, defendants represent on their web sites that transfer of title to the goods being sold in the order takes place in North Carolina and/or Kentucky and eSmokes will charge sales tax if the order is being shipped to North Carolina, Virginia or Kentucky.
 - 22. Defendants' representations are false and misleading for the following reasons:
- (a) Defendants' representation concerning responsibility for tax law compliance implies that defendants are not responsible for ascertaining and complying with the relevant tax laws concerning cigarette products and that the burden of doing so rests with the purchaser. In fact, pursuant to the Jenkins Act, it is the responsibility of the seller to report shipments of tobacco products into California.
- (b) Pursuant to Revenue and Taxation Code sections 30008, 30009 and 30109, California taxes are imposed and collected on the first distribution of untaxed cigarettes in the state. This means that since eSmokes does not pay taxes on cigarettes purchased from its web sites and shipped to consumers in California, the California consumers must pay all taxes owed on the cigarettes;
- (c) Defendants' implication that California taxes need not be paid because the sale takes please in North Carolina, Virginia or Kentucky is erroneous and/or irrelevant because by law consumers are obligated to pay taxes on cigarettes purchased from defendants over the Internet and shipped into the state; and

(d) Federal legislation does not exempt California consumers from paying California taxes on cigarette products purchased for personal consumption from an out-of-state retailer when those products are shipped into California.

Failure to Notify California Purchasers of Tax Obligations

- 23. Effective January 1, 2003, California Revenue and Taxation Code section 30101.7(d) requires that a person may engage in non-face-to-face sales of cigarettes to California consumers provided that either of the following conditions is met:
 - (1) All applicable California taxes on the cigarettes have been paid, or
- (2) The seller includes, on the outside of the shipping container for any cigarettes shipped to a resident in California from any source in the United States, an externally visible and easily legible notice located on the same side of the shipped container as the address to which the package is delivered as follows:

"IF THESE CIGARETTES HAVE BEEN SHIPPED TO YOU FROM A SELLER LOCATED OUTSIDE OF THE STATE IN WHICH YOU RESIDE, THE SELLER HAS REPORTED PURSUANT TO FEDERAL LAW THE SALE OF THESE CIGARETTES TO YOUR STATE TAX COLLECTION AGENCY, INCLUDING YOUR NAME AND ADDRESS. YOU ARE LEGALLY RESPONSIBLE FOR ALL APPLICABLE UNPAID STATE TAXES ON THESE CIGARETTES."

Since January 1, 2003, eSmokes has violated this law by failing to pay applicable taxes or to inform California consumers of their obligation to pay all applicable unpaid taxes on the cigarettes.

24. The failure of out-of-state-retailers like defendants to comply with federal reporting laws, identifying the shipments of cigarettes into California and the identity of the purchasers and notifying purchasers of their California tax obligations, has resulted in significant loss of tax revenue to the state. The Board of Equalization estimates that for fiscal year 2001-2002, California lost approximately \$53.9 million through sales of cigarettes to California consumers over the Internet, by mail order and cross-border sales. This figure represents the taxes owed on 61.9 million packs of cigarettes.

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FIRST CAUSE OF ACTION

Business and Professions Code 17500 False or Misleading Advertising

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28. The People reallege and incorporate by reference, paragraphs 1 through 27, inclusive, as though fully set forth herein.

Complaint for Injunction, Civil Penalties, and Other Relief

25. The People reallege and incorporate herein by reference, paragraphs 1 through 24, inclusive, as though fully set forth herein.

- 26. Within the past three (3) years from the date of the filing of this Complaint, defendants and their agents and representatives, have made or caused to be made, untrue or misleading statements to members of the public, including to potential customers purchasing cigarettes from their web sites, in violation of section 17500 of the Business and Professions Code, in order to induce them to purchase cigarettes from defendants. Said untrue or misleading statements include, but are not limited to the following:
- (a) Representing or implying that eSmokes is not required to comply with the Jenkins Act's reporting requirements:
- (b) Representing or implying that California consumers are not required to pay taxes in California on cigarettes purchased from eSmokes over the Internet;
- (c) Advertising eSmokes' cigarettes at a stated price but failing to inform California consumers that this stated price does not include California taxes; and
- (d) Representing or implying that consumers do not have to pay taxes on cigarettes for personal consumption purchased from defendants over the Internet and shipped into California.
- 27. Defendants knew, or by the exercise of reasonable care should have known, that the statements set forth in paragraph 26 were untrue or misleading at the time such statements were made.

SECOND CAUSE OF ACTION

Revenue and Taxation Code section 30101.7(d) Failure to Notify California Purchasers of Their Tax Obligations

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29. Since January 1, 2003, eSmokes has engaged and continues to engage in non-face-to-face sales of cigarettes to California consumers without satisfying either of the following conditions: (1) paying all applicable California taxes or (2) including on the outside of the shipping container for any cigarettes shipped to a resident in California from any source in the United States an externally visible and easily legible notice located on the same side of the shipped container as the address to which the package is delivered, as required by Revenue and Taxation Code section 30101.7(d).

THIRD CAUSE OF ACTION

Business and Professions Code Section 17200 Unfair or Unlawful Business Acts or Practices

- 30. The People reallege and incorporate by reference paragraphs 1 through 29, inclusive, as though fully set forth herein.
- 31. Within the past four (4) years from the date of the filing of this Complaint, defendants, and each of them, engaged in acts of unfair competition as defined in and prohibited by Business and Professions Code section 17200 by conduct which includes, but is not limited to:
- (a) Making untrue or misleading statements as referenced in paragraph 26 of this Complaint, in violation of Business and Professions Code section 17500;
- (b) Selling cigarettes over the Internet and delivering them by common carrier to California children since at least March 2001, in violation of Penal Code section 308(a);
- (c) Failing to maintain adequate or effective safeguards or procedures to ensure that children cannot purchase cigarettes from defendants' web sites and that cigarettes will not be delivered to children, in violation of Penal Code section 308(a);
- (d) Failing to report to the BOE shipments of cigarettes to California consumers as required by the Jenkins Act;
- (e) Representing that consumers may have an obligation to report the purchase of cigarettes, when in fact it is the defendants' obligation;
- (f) Failing to either pay the California taxes owed on cigarettes purchased by California consumers over the Internet from eSmokes or to clearly notify consumers that Complaint for Injunction, Civil Penalties, and Other Relief

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defendants have reported the sale of cigarettes to the BOE and the purchaser is responsible for the unpaid taxes, in violation of Revenue and Taxation Code section 30101.7(d).

WHEREFORE, the People respectfully pray that this Court grant the following relief:

- Pursuant to Business and Professions Code section 17535, defendants, their successors, employees, agents and representatives, and all other persons who are acting in concert with them, be preliminarily and permanently enjoined from making untrue or misleading statements in violation of Business and Professions Code section 17500 and be specifically enjoined from making the untrue or misleading statements set forth in the First Cause of Action.
- 2. Pursuant to Business and Professions Code section 17203, defendants, their successors, employees, agents, representatives, and all other persons who are acting in concert with them, be preliminarily and permanently enjoined from engaging in unfair competition as defined in Business and Professions Code section 17200 and be specifically enjoined from engaging in the types of acts or practices set forth in the Third Cause of Action.
- Pursuant to Revenue and Taxation Code section 30101.7(e), defendants, their successors, employees, agents, representatives, and all other persons who are acting in concert with them, be preliminarily and permanently enjoined from failing to comply with Revenue and Taxation Code section 30101.7(d)
- That defendants be required to pay to the People civil penalties pursuant to Business and Professions Code section 17536 of \$2,500 for each violation, as determined by proof, in an amount of no less than \$100,000.
- 5. That defendants be required to pay to the People civil penalties pursuant to Business and Professions Code section 17206 of \$2,500 for each violation, as determined by proof, in an amount of no less than \$100,000.
- That defendants be required to pay to the People civil penalties pursuant to the schedule set forth in Revenue and Taxation Code section 30101.7(e), as determined by proof.
- That defendants be required to pay to the People fees and costs, including reasonable attorney's fees pursuant to Code of Civil Procedure section 1021.10.
- That the Court grant such other and further relief as the Court deems just and 12 Complaint for Injunction, Civil Penalties, and Other Relief

1	proper.	
2	Dated: March 28, 2003	
3	Re	espectfully submitted,
4		LL LOCKYER
5	S RI	torney General of the State of California CHARD M. FRANK
6	DI DI	nief Assistant Attorney General ENNIS ECKHART enior Assistant Attorney General
7	De	enior Assistant Attorney General ICHELLE L. FOGLIANI eputy Attorney General
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9	LA	AURA KAPLAN eputy Attorney General
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12	Ge Ge	torneys for The People of the State of alifornia, ex rel. Bill Lockyer, Attorney eneral of the State of California, Plaintiff
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