

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

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THE CITY OF NEW YORK,

Plaintiff,

COMPLAINT

03 CV 0383 (DAB (GWG))

- against -

CYCO.NET, INC., RICHARD A. URREA,
BRENT WOLFORD, DANIEL R. URREA,
HEMI GROUP, LLC, BRIAN PEREYRA, D.C.,
INC., FRED TEUTENBERG, MICHAEL E.
SMITH, doing business as PaylessCigs,
DOMAINS FOR SALE, HOORAY'S INC.,
STEPHEN F. KNOPP, BURT NEWMAN, d/b/a
Newman Enterprises, DMITRIY ZILBERMAN,
S4L DISTRIBUTING, INC., WILLIAM C.
BAKER III, and DOUBLE B DISTRIBUTING,
d/b/a Discount Tobacco Store,

Defendants.

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Plaintiff the City of New York (the "City"), by its counsel Michael A. Cardozo, Corporation Counsel of the City of New York, as and for its complaint against the defendants, respectfully alleges, with knowledge of its own actions and on information and belief as to the actions of others, as follows:

INTRODUCTION

1. This is a civil action under the Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. § 1961 *et seq.*, New York General Business Law § 349 and state common law for redress from defendants' scheme to defraud New York City of tax revenues by concealing from New York tax administrators Internet sales of cigarettes to New York City residents.

2. The defendants are cigarette sellers that advertise and sell cigarettes over the Internet to New York City residents. Each defendant receives Internet orders from City residents and ships the orders by common carrier or United States Postal Service into New York. None of the defendants notifies New York's tobacco tax administrator of the shipments, in violation of the Jenkins Act, 15 U.S.C. § 375 *et seq.*

3. Defendants' scheme relies on the fact that the City and State of New York impose excise and sales taxes of \$33.30 on every carton of cigarettes sold within the City, an amount that exceeds cigarette taxes in most other states. Cigarette sellers in other states, particularly those with negligible tax rates, accordingly are able to offer cigarettes at prices well below prices offered by New York City stores.

4. A carton of premium brand cigarettes sold in such low-tax states as Virginia or Kentucky may be purchased for approximately \$30.00, while the same carton purchased in New York City costs approximately \$70.00. The difference in price is almost entirely attributable to the fact that the out-of-state seller is not required to collect New York taxes in a sale to a New York purchaser.

5. While geography previously limited the ability of cigarette sellers to avail themselves of this cross-border tax differential, the advent of the Internet eliminated most obstacles to out-of-state cigarette sellers that wish to sell to residents of differently-taxed states, including New York. Internet sellers thus offer New York City residents cigarettes at approximately half of the New York store price.

6. However, Internet offers of cheap cigarettes exemplify the adage that a deal that sounds too good to be true probably isn't. Although Internet sellers are not required to collect taxes from New York purchasers, the taxes are still owed and the cigarette purchaser is

responsible for payment. By law, the fact that a New Yorker purchased the cigarettes out of state is immaterial. If used in New York, the cigarettes are taxed. The “discount” offered by the Internet seller consists almost entirely of the unpaid taxes assessed by the purchaser’s state, and the “savings” realized by the purchaser is largely, if not entirely, illusory.

7. Cigarette tax evasion over the Internet is merely the latest variant of what is referred to as the “cross-border” excise tax problem that has threatened cigarette tax revenues for as long as significant interstate differences among cigarette tax rates have existed. To protect state tax revenues from the effect of cross-border tax differences, Congress passed the Jenkins Act nearly fifty years ago.

8. The Jenkins Act requires cigarette sellers to notify state tax administrators of every interstate cigarette shipment made by the seller into the administrator’s state. Cigarette sellers that ship in interstate commerce must file with the tobacco tax administrator of each state a monthly report containing the name and address of each person to whom the seller has shipped.

9. Because the purchaser typically remains liable for the tax in his or her home state, regardless of the out-of-state locus of the purchase, the notice required under the Jenkins Act serves to alert state tax administrators to out-of-state purchases on which tax is due. The state tax administrator is therefore able to collect the tax from the in-state purchaser. In the absence of a Jenkins Act report, state tax administrators have little means to detect the out-of-state purchase.

10. Defendants’ “business plan” thus depends upon concealing their customers’ purchases from state tax authorities. If Internet purchasers were identified and required to pay taxes, virtually all of the economic incentive for the Internet purchase disappears.

11. To be still more effective, defendants must also inform their customers of defendants' policy of concealing their customers' purchases from state tax authorities. By doing so, defendants assure their customers that an unexpected tax liability will not arise in the future, i.e., that their customers will not be caught.

12. Defendants' "business plan" is further strengthened by concealing the purchasers' tax liability from the purchasers themselves. Law-abiding purchasers made aware of their liability for cigarette taxes would understand that they realize little or no legal savings on Internet purchases, and the economic incentive for the purchases would disappear.

13. Thus, to encourage purchases by City residents, defendants actively thwart the Jenkins Act. First, defendants simply refuse to file Jenkins Act reports of their shipments into New York.

14. Second, defendants advertise their policy of concealment, assuring customers that defendants will not report cigarette purchases to state tax authorities or will not file Jenkins Act reports. Some of the defendants even offer prospective customers bogus "legal opinions" that the defendants are not legally required under the Jenkins Act or otherwise to notify state tax authorities of out-of-state purchases. The advertising serves to assure defendants' customers' that their purchases will remain secret, and untaxed.

15. Third, defendants falsely inform their New York customers that cigarettes purchased over the Internet are "tax-free," notwithstanding that New York residents must pay taxes on cigarettes purchased out-of-state. To preserve the economic incentive for the purchase, defendants mislead their customers into believing that no tax payment is required for Internet purchases.

16. By selling cigarettes without complying with the Jenkins Act and/or by informing prospective customers that defendants do not comply with the Jenkins Act and/or by advertising Internet cigarette sales as “tax-free,” defendants have devised a scheme or artifice to defraud within the meaning of the mail and wire fraud statutes, 18 U.S.C. §§ 1341 and 1343. Defendants’ actions are intended to and do have the effect of concealing cigarette purchases by New York residents, so that the taxes owing on the purchases cannot be collected by New York’s taxing authorities. The City of New York is thereby defrauded of tax revenues owed by City residents who purchase cigarettes at defendants’ Internet sites.

17. In using an “enterprise” as defined by 18 U.S.C. § 1961 *et seq.* to implement their Internet and mail-based scheme to defraud the City of cigarette tax revenues, defendants’ conduct violates the federal racketeering laws.

18. In this action, the City of New York seeks: i) to recover from defendants three times the amount of the tax revenues lost as a result of the defendants’ scheme; ii) to require defendants to comply with the Jenkins Act; iii) to enjoin defendants from informing their customers that defendants do not file Jenkins Act reports; iv) to require defendants to inform their customers that taxes are owed on purchases from defendants’ sites and that defendants do file Jenkins Act reports; v) to enjoin defendants from falsely claiming that cigarettes sold to New York City residents are “tax-free”; and vi) to recover the attorney’s fees incurred in bringing this action.

PARTIES

19. Plaintiff the City of New York (the “City”) is a municipal corporation organized under the laws of the State of New York.

20. Defendant Cyco.net, Inc. (“Cyco.net”), is a publicly traded corporation formed under the laws of the State of New Mexico with a principal place of business at 4201 Yale Blvd NE, Suite G, Albuquerque, NM 87107 and/or 400 Gold SW # 980, Albuquerque, NM 87102. Cyco.net owns or controls a retail cigarette outlet known as “Aabakismokes” (a/k/a “Cycocigs”) (collectively referred to as the “Aabakismokes Enterprise”) that sells cigarettes over the Internet by operating web-sites accessible to residents of the City of New York. The web-site addresses of the Aabakismokes Enterprise are www.aabakismokes.com and www.cycocigs.com. Approximately forty percent (40%) of the Aabakismokes Enterprise’s Internet sales are to New York residents.

21. Defendant Richard A. Urrea is a citizen of the State of New Mexico and is the President of defendant Cyco.net.

22. Defendant Daniel R. Urrea is a citizen of the State of New Mexico and is the Chief Financial Officer of defendant Cyco.net.

23. Defendant Brent Wolford is a citizen of the State of New Mexico and is the Chief Technical Officer of defendant Cyco.net.

24. Defendant Hemi Group, LLC (“Hemi Group”), is a limited liability corporation formed under the laws of the State of New Mexico with a principal place of business at 250 Sheep Springs Circle, Jemez Pueblo, NM 87024. Hemi Group owns or controls a retail cigarette outlet known as “Cigarettespecials” (a/k/a “BuyDiscountCigarettes,” “FreeCigs4u,” “CyberCigarettes” and “AdobeCigarettes”) (collectively referred to as the “Cigarettespecials Enterprise”), that sells cigarettes over the Internet through web-sites accessible to residents of the City of New York. The web-site addresses of the Cigarettespecials Enterprise are

www.cigarettespecials.com, www.BuyDiscountCigarettes.com, www.FreeCigs4u.com,
www.cybercigarettes.com and www.AdobeCigarettes.com.

25. Defendant Brian Pereyra is a resident of the State of New Mexico and is the “Administrative Contact” for the Hemi Group web-sites.

26. Defendant D.C. Inc., is a corporation formed under the laws of the State of Missouri, with a principal place of business at 895 Bolger Ct., Fenton, Mo 63026. D.C. Inc. owns or controls a retail cigarette outlet known as “Dirtcheapcig,” 900 McGuire Ave. Suite C, Paducah, KY 42001 (the “DirtCheapCig Enterprise”). The DirtCheapCig Enterprise sells cigarettes over the Internet by operating a web-site accessible to residents of the City of New York. The web-site address of the DirtCheapCig Enterprise is www.dirtcheapcig.com.

27. Defendant Fred Teutenberg is a resident of the State of Missouri and is the President of defendant D.C., Inc.

28. Defendant Michael E. Smith, is a resident of the State of Virginia residing at 717 West 33rd St., Richmond, VA 23225. Michael Smith owns or controls a retail cigarette outlet known as “Paylesscigs,” that sells cigarettes over the Internet by operating a web-site accessible to residents of the City of New York (the “Paylesscigs Enterprise”). The web-site address of the Paylesscigs Enterprise is www.paylesscigs.com.

29. Defendant Domains For Sale, is a Virginia business with a principal place of business at 2711 Buford Road #194, Bon Air, VA 23235. Domains For Sale is the site registrant for the web-site maintained by the Paylesscigs Enterprise.

30. Defendant Hooray’s, Inc. (“Hooray’s”) is a corporation organized under the laws of the State of Kentucky with its principal place of business at 12619 Shelbyville Rd., Louisville, KY 40243. Hooray’s owns or controls a retail cigarette outlet known as “Smokes-

Direct” (a/k/a “Cigsonline”), that sells cigarettes over web-sites accessible to residents of the City of New York (the “Smokes-Direct Enterprise”). The web-site addresses of the Smokes-Direct Enterprise are www.smokes-direct.com and www.cigsonline.com.

31. Defendant Stephen F. Knopp is a resident of the State of Kentucky and is the President of Defendant Hooray’s Inc.

32. Defendant Burt Newman, d/b/a Newman Enterprises, is a resident of the State of California residing at or with a principal place of business at 1645 Currycomb Dr., San Marcos, CA 92069 and is the Site Registrant for the Hooray’s Inc. web-sites.

33. Dmitriy Zilberman is a resident of the State of Kentucky and is an employee or officer of defendant Hooray’s Inc. and the “Administrative Contact” for the Smokes-Direct Enterprise web-site.

34. Defendant S4L Distributing, Inc. (“S4L Inc.”), is a corporation formed under the laws of the State of Virginia with a principal place of business located at 1514 E. 3rd Avenue, Big Stone Gap, VA 24219. Defendant S4L Inc. owns or controls a retail cigarette outlet known as “Bulkcigs” (a/k/a “S4L.com” or “DiscountTobaccostore”) that sells cigarettes over the Internet through web-sites accessible to residents of the City of New York (the “Bulkcigs Enterprise”). The web-site addresses of the Bulkcigs Enterprise are www.bulkcigs.com, www.discounttobaccostore.com and www.S4L.com.

35. Defendant William C. Baker III is a resident of the State of Virginia and is an employee or officer of defendant S4L, Inc.

36. Defendant Double B Distributing d/b/a Discount Tobacco Store (“Double B”) is a Virginia business with a principal place of business at 113 E. Jackson St., Gate City, VA 24251. Double B owns or controls a retail cigarette outlet known as “Discounttobaccostore”

(a/k/a “S4L.com” or “Discounttobaccostore”) that sells cigarettes over the Internet through a web-site accessible to residents of the City of New York, located at www.dicounttobaccostore.com. Double B is associated with the Bulkcigs Enterprise.

JURISDICTION AND VENUE

37. The City’s federal claims allege violations of 18 U.S.C. § 1961 *et seq.*

38. The court has jurisdiction over the subject matter of this action pursuant to 18 U.S.C. § 1964 and 28 U.S.C. §§ 1331, 1332, 1337 and 1367.

39. Venue is proper in this district under 18 U.S.C. § 1965(a) and (b) and 28 U.S.C. § 1391(b) because a substantial part of the events and omissions giving rise to the claims occurred in this district.

40. Personal jurisdiction is proper under 18.U.S.C. § 1965 and also proper because each defendant, in person or through an agent, transacts or has transacted business within New York and this district, or contracts or has contracted to supply goods or services within New York or this district, or has committed a tortious act within New York or this district. All defendants did and continue to do business within New York and this district, made contracts to be performed in whole or in part in New York and this district, and/or performed tortious acts reasonably expected to have consequences in New York and this district while deriving substantial revenue from interstate or international commerce.

FACTS

Cigarette Taxation in New York

41. The City and State of New York each impose an excise tax on all cigarettes possessed for sale or use in their respective jurisdictions. *See* Administrative Code of the City of New York (“Admin. Code”) § 11-1302(a) (1) and (2) and New York State Tax Law

(“N.Y. Tax Law”) §§ 471 and 471-a. The New York State excise tax on cigarettes is presently \$1.50 per pack. The New York City excise tax is \$1.50 per pack. The combined State and City sales tax is \$0.33 per pack. The total tax on a pack of cigarettes is therefore \$3.33, or \$33.30 per carton.

42. The cigarette taxes of other states are generally lower than New York’s. For example, the States of Virginia and Kentucky have cigarette taxes of, respectively, \$.025 and \$.03 per pack. Cigarette sellers located in those states, among others, are therefore able to offer cigarettes for sale at lower prices than the same cigarettes sold by “brick and mortar” stores in New York.

43. Because out-of-state sellers are now easily available to New York City residents over the Internet, a City resident may purchase from an Internet seller located, for example, in Virginia or Kentucky, and pay a price that represents an *apparent* savings of approximately \$30 per carton over the New York City price.

44. The “savings” to City residents who purchase over the Internet is in fact illusory. Pursuant to N.Y. Tax Law § 471-a and Admin. Code § 11-1302 (a)(2), out-of-state purchases of cigarettes possessed for use in New York City are subject to New York State and City cigarette tax, which must be paid by the purchaser. Of course, if the purchaser does pay the tax, most of the “discount” gained through the Internet purchase evaporates.

45. It follows that the underlying assumption of the Internet cigarette business, and the principal basis of its profitability, is that purchasers will evade the tax imposed by their home states. It is therefore crucial to the success of their businesses for defendants to conceal their sales to New York residents from New York’s tax authorities. A recent report, *Buying Cigarettes Over the Internet*, Prudential Financial Research (September 24, 2002) (hereafter

“*Prudential Report*”) concludes that the primary reason for the growth of Internet cigarette sales is tax avoidance, and that consumers elect to purchase cigarettes over the Internet in order to avoid state and local taxes. *Prudential Report* at 3, 18.

The Jenkins Act

46. Although enacted long before the Internet or overnight delivery, the Jenkins Act, 15 U.S.C. § 375 -378 (1949), was passed as a Congressional remedy to the identical problem of cross-border tax evasion now posed by Internet sales, but as accomplished through the earlier technology of the telephone and the U.S. Postal Service. The legislative history of the Jenkins Act, dating from 1949 and 1955, comments on the “large and increasing loss of revenue to the States caused by the evasion of sales and use taxes on cigarettes shipped in interstate commerce to consumers.” Congress was troubled by the “discrimination caused by this evasion against sellers of cigarettes in States having a higher tax than the tax of the seller States” and “the fact that this evasion was accomplished through the use of the United States mail.” *S.Rep.No.1147, 84th Cong., 1st Sess., U.S. Code Cong. and Admin. News p. 2883 (1955).*

47. Congress took note that “certain individuals and organizations are using the United States mails to circumvent State laws,” and that “[a]dvertisements of organizations specializing in this business cite the availability and use of the United States mails as proof of legality of their operations.” Congress believed that “respect for the laws of the sovereign States will be furthered ... and ... the public interest will be served by [a] bill eliminating any inference that the Federal Government approves of the circumventing of State laws.” *S.Rep.No.644, 81st Cong., 1st Sess., U.S. Code Cong. and Admin. News pp. 2158, 2159-60 (1949).*

48. The Jenkins Act thus sought to “level the playing field” among the States with respect to interstate differences in cigarette tax rates. The Act provides a procedure by which state tobacco tax administrators are to be informed of cigarette imports into their states, so

that the taxes owed by resident purchasers can be collected. Under the Act, cigarette 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.

Internet Cigarette Tax Evasion

49. The typical Internet cigarette purchase is accomplished by the buyer accessing an Internet web-site that sells cigarettes. The sites are easily located by the use of Internet search engines. A recent (November 2002) survey located approximately 400 Internet sites that sell cigarettes.

50. Having accessed an Internet cigarette seller, the prospective purchaser typically must register with the site, providing name, address, e-mail address, and telephone number. The purchaser then selects the cigarettes desired from a menu and proceeds to the "check-out" area. Billing and shipping information are displayed, based on the purchaser's registration entries. The purchaser selects payment methods, including credit cards, and shipment methods, including the United States Postal Service or a common carrier such as UPS or Federal Express.

51. The United States General Accounting Office, in a report entitled *Internet Cigarette Sales: Giving ATF Investigative Authority May Improve Reporting and Enforcement*, GAO Report 02-742 (August 2002) ("*GAO Report*"), examined 147 Internet web-sites offering cigarettes for sale. None of the sites stated that they complied with the Jenkins Act. *GAO*

Report at 16. To the contrary, 78% of the sites expressly stated that they do not report cigarette sales to state tax administrators, or that they maintain customer information as “private,” or that they are not required to comply with the Jenkins Act. The remaining 22% of the sites gave no indication one way or the other whether or not they complied with the Jenkins Act. *GAO Report* at 16.

52. Many Internet cigarette sellers cited in the *GAO Report* claim on their web-sites that the cigarettes they sell are “tax-free.”

53. The *Prudential Report* contains anecdotal observations that confirm those in the *GAO Report*. In telephone contacts, virtually all of Internet cigarette sellers stated that they were not legally obligated to report sales to state tax authorities and/or that the buyer did not have to pay any taxes on the cigarettes purchased. *Prudential Report* 11-14.

Allegations Against Defendants

54. All of the retail cigarette enterprises named in this complaint flout the Jenkins Act, as indicated by statements on the web-sites of their respective enterprises:

a. The Aabakismokes Enterprise states on its web-sites:

All information obtained from our customers is for the sole use of this site to serve our customers. At **no time** will we sell, copy or transfer our e-mail list or customer names and addresses to any person or entity *including governments*. As tempting as it may become to profit from this information or be intimidated by outside forces we will stand committed to shield this information. We feel that our customers are our greatest asset and our future, to compromise them would destroy our business.

www.cycocigs.com and www.aabakismokes.com (original emphasis).

b. The Cigarettespecials Enterprise makes a variety of statements related to the Jenkins Act in its web-sites:

[W]e do not ever share your personal information with any other company or government agency!

www.cigarettespecials.com, “Home Page”

CigaretteSpecials.com does not share your personal information with *any* third party, including State taxing authorities

www.cigarettespecials.com, “Privacy Policy” (original emphasis).

CigaretteSpecials.com does not report any sales activity to any State taxing authority and is not required to do so.

www.cigarettespecials.com, “Legal Notices”

The Cigarettespecials Enterprise also states:

No tobacco tax (flashing banner)

All sales are tax free!! (original emphasis)

www.cigarettespecials.com, “Home Page”

The Cigarettespecials Enterprise states on its other web-sites that:

Buydiscountcigarettes does not share your personal information with any third party, including State taxing authorities.

www.buydiscountcigarettes.com, “Privacy Policy”

“No tobacco tax” (flashing banner)

www.buydiscountcigarettes.com, “Home Page” (original emphasis)

FreeCigs4u.com does not report any sales activity to any State taxing authority and is not required to do so.

www.FreeCigs4u.com, Legal Notices

AdobeCigarettes.com does not share your personal information with any third party, including State taxing authorities.

www.Adobecigarettes.com, Privacy Policy (original emphasis, text in red).

c. The Dirtcheapcig Enterprise states in the “Frequently Asked Questions” section of its web-site:

Do you furnish customer names and addresses to governmental authorities?

It is our researched legal opinion that we are not required to furnish such information. To date we have never furnished such information. We are the last refuge of the persecuted smoker.

www.dirtcheapcig.com

d. The Payless Cigs Enterprise states on its web-site:

We do not provide your information to anyone! Most other cigarette sites don't either, but a few do report sales to state tax offices, so find out before you buy, if not you could receive an unexpected tax bill from your state tax office. The only way we will provide any information to anyone is by Court Order from a court with local jurisdiction.

www.paylesscigs.com

e. The Smokes-Direct Enterprise states on its web-site that:

Smokes-Direct.com does not report any sales activity to any State taxing authority and is not required to do so.

www.smokes-direct.com and www.cigsonline.com, “Legal Notices”

The Smokes-Direct Enterprise states on another of its web-sites:

Privacy Policy and Tax Reporting: You are probably aware that a federal regulation known as the Jenkins Act requires cigarette vendors to report their sales to the appropriate state tax authorities. You may not know, however, that the Jenkins Act was passed more than 50 years ago. Long before the advent of electronic communications and e-commerce. Since that time the federal government and several states have passed legislation specifically relating to electronic communications. The Privacy Act of 1974 and the Electronics Communications act of 1986 are examples of this type of legislation. At this very moment Congress is debating additional legislation to protect privacy in electronic commerce. To this end we believe there is ample

justification to state the following policy: We will not divulge your information to any third party with out either your express consent or as directed by the lawful order of a court of proper jurisdiction.

www.S4L.com, “Privacy Policy”

55. The *Prudential Report* documents that telephone salespersons at Internet cigarette sites routinely inform purchasers that Jenkins Act reports are not filed, and/or not required and/or that the sales are tax-free. For example, operators at the Aabakismokes Enterprise are reported as informing callers that the enterprise was under no legal obligation to report the sales to any tax collection agency. *Prudential Report* at 11.

56. The statements on the enterprise web-sites, that i) the sales are “tax-free,” ii) that the seller is not required to file Jenkins Act reports and, iii) that purchasers of cigarettes over the Internet are not required to pay taxes, are all false.

57. Inquiries to officials at the New York State Department of Taxation and Finance reveal that none of the enterprises have filed any Jenkins Act reports.

Extent of the City’s Injury

58. While the extent of the City’s damages is to be determined at trial, defendants’ systematic concealment of their sales is clearly having the desired effect of increasing defendants’ business. The *Prudential Report* documents statements by salespersons at the Aabakismokes Enterprise that a large volume of its sales are to residents of New York City, with the number increasing following the recent tax rise. *Id.* at 11.

59. Defendant Daniel Urrea, an associate of the Aabakismokes Enterprise, is quoted in the July 2, 2001 *Albuquerque Tribune* as stating that approximately forty percent of the customers of the Aabakismokes Enterprise are New Yorkers. See www.abqtrib.com/archives/business01/070201_business_smokes.shtml.

60. An operator at the Dirtcheapcig Enterprise is also reported in the *Prudential Report* to have observed an increase in orders from New York residents following the recent cigarette tax increase. *Prudential Report* at 12.

61. A recent survey has shown that between 1 and 3 percent of adult smokers with Internet access purchased their cigarettes through the Internet, with the number trending upward. The *Prudential Report* estimates that Internet sales accounted for 2% of industry volume in 2002, growing to nearly 6% by 2005.

62. The *GAO Report* cites an estimate by the State of California that the state lost approximately \$13 million in tax revenue from May 1999 through September 2001 because of Internet cigarette vendors' noncompliance with the Jenkins Act. The *Prudential Report* estimates that the losses to the states from Internet sales in 2002 was \$254 million, and will grow to \$889.6 million by 2005.

ALLEGATIONS RELATED TO THE RICO CLAIMS

The Enterprises

63. At all times relevant to this complaint, each of the Internet enterprises named above, *i.e.*, Aabakismokes Enterprise, the Cigarettespecials Enterprise, the Dirtcheapcig Enterprise, the Paylesscigs Enterprise, the Smokes-Direct Enterprise and the Bulkcigs Enterprise (referred to generically as "Internet Cigarette Enterprises") constituted an "enterprise" within the meaning of 18 U.S.C. § 1961 (4). Each Internet Cigarette Enterprise is an entity that engages in activities affecting interstate commerce.

64. Each Internet Cigarette Enterprise is an on-going association-in-fact enterprise composed of individuals with a common purpose, a continuity of structure and

personnel, and a consensual decision-making structure that is used to engage in a common course of conduct, both legal and illegal.

65. The affairs of each Internet Cigarette Enterprise are conducted through a pattern of racketeering activity within the meaning of 18 U.S.C. § 1961 (1) (B), consisting principally of multiple and continuing instances of mail and wire fraud in violation of 18 U.S.C. § 1341 and 18 U.S.C. § 1343.

66. Each Internet Cigarette Enterprise exists separate and apart from the pattern of unlawful activity within the meaning of 18 U.S.C. § 1961 (1) (B), because each enterprise engages in other lawful activity beyond the commission of the predicate offenses. The structure of each enterprise is beyond that required for the commission of the pattern of unlawful activity, each enterprise would continue to exist even in the absence of the predicate offenses and the common activities of each enterprise extend beyond the minimal association necessary to sustain the pattern of racketeering. The associates of each enterprise have common links other than the racketeering activity.

67. The personnel and structure of each Internet Cigarette Enterprise has remained constant over time. Those associated with each enterprise contemplate its indefinite existence. Each enterprise has operated in the past, continues to operate and can be expected to continue operating in the future.

68. Defendants Cyco.net, Richard A. Urrea, Brent Wolford, and Daniel R. Urrea are associates of the Aabakismokes Enterprises.

69. Defendant Hemi Group is an associate of the Cigarettespecials Enterprise.

70. Defendant Brian Pereyra is an associate of the Cigarettespecials Enterprise.

71. Defendant D.C. Inc. is an associate of the Dirtcheapcig Enterprise.
72. Defendant Fred Teutenberg is an associate of the Dirtcheapcig Enterprise.
73. Defendant Michael E. Smith is an associate of the Paylesscigs Enterprise.
74. Defendant Hooray's is an associate of the Smokes-Direct Enterprise.
75. Stephen F. Knopp is an associate of the Smokes-Direct Enterprise.
76. Defendant Burt Newman, d/b/a Newman Enterprises, is an associate of the Smokes-Direct Enterprise.
77. Defendant Dmitriy Zilberman is an associate of the Smokes-Direct Enterprise.
78. Defendant S4L, Inc. is an associate of the Bulkcigs Enterprise.
79. Defendant William C. Baker III is an associate of the Bulkcigs Enterprise.
80. Defendant Double B Distributing, d/b/a Discount Tobacco Store, is an associate of the Bulkcigs Enterprise.

Defendants' Racketeering Activity

81. At all times relevant to this complaint, each defendant identified above as associated with an Internet Cigarette Enterprise conducted the management and operation of the affairs of the enterprise directly or indirectly through a pattern of racketeering activity within the meaning of 18 U.S.C. §§ 1961 (1) (B), 1961 (5) and 1962 (c), in violation of 18 U.S.C. § 1962 (c), namely, by committing multiple and continuing acts of mail and wire fraud in violation of 18 U.S.C. § 1341 and 18 U.S.C. § 1343.

82. At all times relevant to this complaint, each defendant identified above as associated with an Internet Cigarette Enterprise used that enterprise to defraud New York City of tax revenues by selling cigarettes to New York City residents while refusing to provide New

York tax authorities with Jenkins Act reports, and/or by informing New York City residents that the enterprise does not comply with the Jenkins Act, and/or by falsely representing that cigarettes purchased over the Internet are tax-free.

83. At all times relevant to this complaint, each defendant identified above as associated with an Internet Cigarette Enterprise conspired to violate the provisions of 18 U.S.C. § 1962(d) by agreeing to conduct the affairs of their respective Internet Cigarette Enterprise through a pattern of racketeering activity. Each defendant agreed to further an endeavor of the enterprise that, when completed, amounted to the criminal offense of mail and wire fraud, in violation of 18 U.S.C. § 1341 and 18 U.S.C. § 1343.

84. At all times relevant to this complaint, each defendant identified above as associated with an Internet Cigarette Enterprise intentionally furthered the acts of the enterprise by receiving Internet orders for cigarettes from New York residents, by shipping cigarettes to New York City residents, by refusing to file Jenkins Act reports for the enterprise, by advertising the enterprise's non-compliance with the Jenkins Act and by falsely advertising that the enterprise's cigarette sales are "tax free."

85. At all times relevant to this complaint, each defendant identified above as associated with an Internet Cigarette Enterprise agreed to a plan whereby cigarettes will be sold to New York residents without informing the New York tax authorities of the sales, and /or by falsely advertising the cigarettes as "tax-free," and/or by advertising that sales will not be reported to the New York tax authorities. Each defendant has recognized that an essential element of the plan consists of multiple violations of 18 U.S.C. § 1341 and § 1345, in that the mails and the wires would be used in furtherance of a scheme or artifice to defraud New York City of tax revenue. Each defendant has agreed that certain associates of their respective Internet

Cigarette Enterprise would commit such violations while other associates of the enterprise would provide services intended to support and facilitate the violations.

86. At all times relevant to this complaint, the purpose of the each Internet Cigarette Enterprise was (1) to maintain and advertise Internet sites where New York City residents could purchase cigarettes; (2) to receive orders for cigarettes from New York City residents over the Internet; (3) to sell cigarettes to New York City residents at prices made possible by the fact that the enterprises need not collect New York State and City cigarette taxes; (4) to encourage sales to New York City residents by assuring them that the sales will not be reported to any New York tax authorities; (5) to sell cigarettes to New York City residents without providing the New York State Department of Taxation and Finance with Jenkins Act reports; (6) to defraud New York City of tax revenues by intentionally withholding Jenkins Act reports from the New York tax authorities; (6) in some instances, to mislead New York City residents into believing that their purchases from the enterprise are “tax-free.”

Predicate Acts

87. At all times relevant to this complaint, each defendant devised, intended to devise, carried out and intended to carry out a scheme or artifice to defraud New York City of property in the form of cigarette tax revenues owed by New York City residents who had purchased cigarettes from each Internet Cigarette Enterprise. To execute this scheme, and to receive the financial benefits of this scheme, each defendants has repeatedly used the mails and wires to ship, transport, sell, distribute, or transfer cigarettes to New York City purchasers while intentionally concealing the sales from the New York tax authorities.

88. Evidence that defendants intentionally seek to defraud New York of taxes is provided by statements transmitted over the Internet to customers that each defendant’s respective Internet Cigarette Enterprise does not inform New York tax authorities of the

purchases and/or that the enterprise is not required to file Jenkins Act reports and/or that the cigarettes sold by the enterprise are “tax-free.”

89. The statements that the Internet Cigarette Enterprises are not required to provide Jenkins Act reports to the New York tax authorities are false, as are the statements that the cigarette purchases are “tax-free.”

90. Each defendant identified above as associated with an Internet Cigarette Enterprise intentionally conceals the names of New York City residents who owe taxes on their cigarette purchases. Defendants do so to permit the enterprise to continue to sell cigarettes at an apparently lower price than the cigarettes could be sold for if the purchasers knew that taxes were due.

91. The defendants thus engage in unlawful activity within the meaning of 18 U.S.C. § 1961 (1) (B), consisting of predicate acts of mail and wire fraud in violation of 18 U.S.C. §§ 1341 and 1343.

92. A separate instance of mail or wire fraud occurs each time that an enterprise uses the mails or wires to effect a sale of cigarettes to a New York resident and does not subsequently file a Jenkins Act report with New York’s tax authorities.

FIRST CLAIM FOR RELIEF
(Violation of § 1962(c))

93. The City realleges paragraphs 1-92 above as if fully set forth herein.

94. New York City is a “person” under 18 U.S.C. §§ 1961 (3) and 1962 (c).

95. Each defendant identified above as associated with an Internet Cigarette Enterprise is a “person” as defined in 18 U.S.C. §§ 1961 (3) and 1962 (c).

96. Each Internet Cigarette Enterprise identified above is an “enterprise” within the meaning of 1961 (4) and 1962 (c). Each Internet Cigarette Enterprise engages in activities affecting interstate commerce at all times relevant to the complaint.

97. Each of the defendants is associated with one of the Internet Cigarette Enterprises and has conducted or participated, directly or indirectly, in the management and operation of the affairs of the enterprise through a pattern of racketeering activity within the meaning of 18 U.S.C. §§ 1961 (1) (B) and 1961 (5) and 1962 (c), to wit, multiple and repeated acts of mail and wire fraud in violation of 18 U.S.C. §§ 1341 and 1343.

98. The predicate acts of mail and wire fraud constitute a pattern of unlawful activity within the meaning of 18 U.S.C. § 1961 (1) (B). The predicate acts are both related and continuous. The acts are connected to one another as part of a scheme to accomplish a uniform purpose, the making of a profit from the sale of cigarettes by concealing taxes owed on the sales. The repeated nature of the conduct during the period of the scheme and the threat of similar conduct occurring in the future makes the acts continuous.

99. New York City suffered injury to its business or property within the meaning of 18 U.S.C. § 1964 (c) by reason of defendants’ violation of 18 U.S.C. § 1962 (c) because each carton of cigarettes sold to a New York City resident without the filing of a Jenkins Act report deprives the City of cigarette excise and sales taxes, in an amount to be determined at trial.

SECOND CLAIM FOR RELIEF
(Violation of § 1962(d))

100. The City realleges paragraphs 1-99 above as if fully set forth herein.

101. New York City is a “person” under 18 U.S.C. §§ 1961 (3) and 1962 (c).

102. Each defendant identified above as associated with an Internet Cigarette Enterprise is a “person” as defined in 18 U.S.C. §§ 1961 (3) and 1962 (c).

103. Each Internet Cigarette Enterprise identified above is an “enterprise” within the meaning of 18 U.S.C. § 1961 (4) and 18 U.S.C. § 1962 (c). Each enterprise engaged in activities affecting interstate commerce at all times relevant to this complaint.

104. Each defendant is associated with one or more of the Internet Cigarette Enterprises identified above and conspired within the meaning of 18 U.S.C. § 1962 (d) to violate 18 U.S.C. § 1962 (c). Each defendant agreed and intended to participate in the affairs of the enterprise through a pattern of racketeering by furthering or facilitating an endeavor of the enterprise that, when completed, would satisfy all of the elements of a criminal offense, to wit, multiple and repeated acts of wire and mail fraud, in violation of 18 U.S.C. §§ 1341 and 1343.

105. With knowledge that a Internet Cigarette Enterprise engaged in multiple and repeated acts of mail and wire fraud in violation of 18 U.S.C. §§ 1341 and 1343, each defendant associated with that enterprise agreed to facilitate acts of other defendants associated with the enterprise that were necessary to fulfill the scheme to conceal sales of cigarettes to New York City residents.

106. New York City suffered injury to its business or property within the meaning of 18 U.S.C. § 1964 (c) by reason of defendants’ violation of 18 U.S.C. § 1962 (d) because each carton of cigarettes sold to a New York City resident without the filing of a Jenkins Act report deprives the City of cigarette excise and sales taxes, in an amount to be determined at trial.

**THIRD CLAIM FOR RELIEF
(VIOLATION OF GBL § 349)**

107. The City re-alleges paragraphs 1-106 above as if fully set forth herein.

108. Defendants failure to file Jenkins Act reports is materially deceptive and misleading to New York City consumers.

109. Defendants statements that their cigarettes are “tax-free” and/or that defendants are not required to file Jenkins Act reports are materially deceptive and misleading to New York City consumers.

110. By reason of defendants’ deceptive and misleading conduct, the City has been injured in that it has been unable to collect taxes owed to it, in an amount to be determined at trial.

FOURTH CLAIM FOR RELIEF
(Common Law Fraud)

111. The City re-alleges paragraphs 1-110 above as if fully set forth herein.

112. Defendants have a statutory duty under the Jenkins Act to provide New York taxing authorities with reports of out-of-state purchases of cigarettes by New York City residents.

113. Defendants intentionally fail to provide Jenkins Act reports to New York tax authorities in order to conceal cigarette sales on which taxes are owed to the City and State of New York

114. As a result of defendants’ intentional omissions to state material facts, the City has been injured in that it has been unable to collect taxes owed to it, the amount to be determined at trial.

WHEREFORE, New York City respectfully prays that the Court grant judgment against the defendants as follows:

- a. On the First Claim For Relief, pursuant to 18 U.S.C. 1964 (c), as against each defendant named herein and each of them jointly and severally, award the City three times its excise and sales taxes lost as a result of each defendant's violation of 18 U.S.C. § 1962(c).
- b. On the Second Claim For Relief, pursuant to 18 U.S.C. 1964 (d), as against each defendant named herein and each of them jointly and severally, award the City three times its excise and sales taxes lost as a result of each defendant's violation of 18 U.S.C. § 1962(d);
- c. On the First and Second Claims For Relief, enjoin defendants' further violation of 18 U.S.C. § 1962 (c) and (d) by: i) requiring defendants to file Jenkins Act reports with New York's taxing authorities, ii) requiring defendants to inform their customers that defendants do file Jenkins Act reports, and iii) requiring defendants to inform their New York customers that taxes are due on all cigarette purchases;
- d. On the Third Claim For Relief, award the City its actual damages caused by defendants' violation of GBL § 349 and enjoin further violations thereof;
- e. On the Fourth Claim For Relief, as against each defendant named therein and each of them jointly and severally, award the City its damages caused by defendants' fraud.

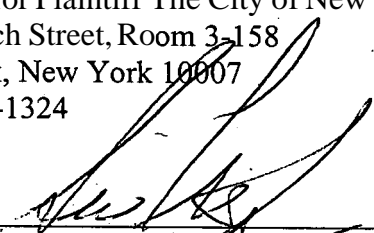
- f. **Award** the City its attorney's fees, pursuant to 18 U.S.C. § 1964 (c) and GBL § 349 (h).
- g. Award such other and further relief as the Court may deem appropriate.

JURY DEMAND

Plaintiff hereby demands a **jury** trial as to all issues of this suit.

Dated: New York, New York
January 17, 2003

MICHAEL A. CARDOZO
Corporation Counsel of the
City of New York
Attorney for Plaintiff The City of New York
100 Church Street, Room 3-158
New York, New York 10007
(212) 788-1324

By: 
Eric Proshansky (EP 1777)
Assistant Corporation Counsel

Of Counsel:

Gail Rubin