IN THE CIRCUIT COURT OF COOK COUNTY, ILLINOIS
COUNTY DEPARTMENT, LAW DIVISION
TAX AND MISCELLANEOUS REMEDIES SECTION

MICHAEL LABELL, et al.	)	
	)	
Plaintiffs,	)	Case No. 2015 CH 13399
	)	
v.	)	(Transferred to Law)
	)	
THE CITY OF CHICAGO, et al.	)	
	)	
Defendants.	)	

PLAINTIFFS' MOTION FOR SUMMARY JUDGMENT

Jeffrey M. Schwab (#6290710)
Jacob H. Huebert (#6305339)
Liberty Justice Center (#49098)
190 S. LaSalle Street, Suite 1500
Chicago, Illinois 60603
Telephone (312) 263-7668
Facsimile (312) 263-7702
jschwab@libertyjusticecenter.org
jhuebert@libertyjusticecenter.org

Attorneys for Plaintiffs

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases

Federal Authorities

State and Local Authorities

Other Authorities

Introduction

The City of Chicago applies its amusement tax – a 9% tax on charges paid for the privilege to enter, witness, view, or participate in amusements that take place *within the City of Chicago* – on charges paid for Internet-based streaming video, audio, and gaming services ("streaming services") by customers with Chicago billing address only, regardless of whether those customer use those streaming services within the City of Chicago. The Court should enjoin the application of the amusement tax on streaming services because: (1) imposing the amusement tax on streaming services exceeds the City's authority to tax under Article VII, Section 6(a) of the Illinois Constitution; (2) taxing streaming services differently than equivalent in-person amusements violates the Illinois Constitution's Uniformity Clause; (3) applying the tax to streaming services imposes a discriminatory tax on electronic commerce in violation of the Internet Tax Freedom Act; and (4) taxing activity outside the City's borders violates the U.S. Constitution's Commerce Clause.

Plaintiffs' Statement of Facts

I. The Chicago Municipal Code provides for a tax on amusements.

1. The City of Chicago imposes a 9% tax on charges paid for the privilege to enter, witness, view, or participate in certain activities within the City of Chicago that the Chicago Municipal Code ("Code") defines as amusements (the "amusement tax"). Chi. Mun. Code § 4-156-020, **Exhibit A**.

2. The Code defines an "amusement" subject to the amusement tax to include three categories of activities:

> (1) any exhibition, performance, presentation or show for entertainment purposes, including, but not limited to, any theatrical, dramatic, musical or spectacular performance, promotional show, motion picture show, flower, poultry or animal show, animal act, circus, rodeo, athletic contest, sport, game or similar exhibition

such as boxing, wrestling, skating, dancing, swimming, racing, or riding on animals or vehicles, baseball, basketball, softball, football, tennis, golf, hockey, track and field games, bowling or billiard or pool games;

(2) any entertainment or recreational activity offered for public participation or on a membership or other basis including, but not limited to, carnivals, amusement park rides and games, bowling, billiards and pool games, dancing, tennis, racquetball, swimming, weightlifting, bodybuilding or similar activities; or

(3) any paid television programming, whether transmitted by wire, cable, fiber optics, laser, microwave, radio, satellite or similar means.

Ex. A, § 4-156-010.

3. The Code requires that every owner, manager, or operator of an amusement or a place where an amusement is being held, and every reseller, collect the amusement tax from every customer of an amusement in Chicago, and remit the tax to the Chicago Department of Finance by the 15th of each calendar month. Ex. A, § 4-156-030(A).

4. The Code exempts "automatic amusement machines" from the amusement tax and instead subjects their operators to a $150 tax per year per device. Ex. A, § 4-156-160.

5. The Code defines an "automatic amusement machine" as:

> any machine, which, upon . . . any . . . payment method, may be operated by the public generally for use as a game, entertainment or amusement . . . and includes but is not limited to such devices as jukeboxes, marble machines, pinball machines, movie and video booths or stands and all [similar] games, operations or transactions . . . .

Ex. A, § 4-156-150.

6. The Code exempts from the amusement tax charges for "in person live theatrical, live musical or other live cultural performances that take place in any auditorium, theater or other space in the city whose maximum capacity, including all balconies and other sections, is not more than 750 persons," Ex. A, § 4-156-020(D)(1), and taxes such performances in a space with a capacity of greater than 750 persons at a reduced rate of 5%. Ex. A, § 4-156-020(E).

7. "Live theatrical, live musical or other live cultural performance" means a live performance in any of the disciplines which are commonly regarded as part of the fine arts, such as live theater, music, opera, drama, comedy, ballet, modern or traditional dance, and book or poetry readings. The term does not include such amusements as athletic events, races or performances conducted at adult entertainment cabarets. Ex. A, § 4-156-010.

II. The City applies the amusement tax to streaming services through Amusement Tax Ruling #5.

8. On June 9, 2015, then-Comptroller of the City of Chicago, Dan Widawksy, issued Amusement Tax Ruling #5 (the "Ruling"), declaring that the term "amusement" as defined by the Code includes "charges paid for the privilege to witness, view or participate in amusements that are *delivered electronically*" (emphasis in original). **Exhibit B**.

9. According to the Ruling, amusements delivered electronically include: (1) "charges paid for the privilege of watching electronically delivered television shows, movies or videos . . . delivered to a patron (i.e., customer) in the City"; (2) "charges paid for the privilege of listening to electronically delivered music . . . delivered to a customer in the City"; and (3) "charges paid for the privilege of participating in games, on-line or otherwise . . . delivered to a customer in the City." Ex. B.

10. The Ruling states that providers who receive charges for electronically delivered amusements are considered owners or operators and therefore are required to collect the City's amusement tax from their Chicago customers. Ex. B.

11. Under the Ruling, "[t]he amusement tax does not apply to sales of shows, movies, videos, music or games (normally accomplished by a 'permanent' download). It applies only to rentals (normally accomplished by streaming or a 'temporary' download). The charges paid for such rentals may be subscription fees, per-event fees or otherwise." Ex. B.

12. The Ruling states that the amusement tax applies to any customer of an amusement delivered electronically whose residential street address or primary business street address is in Chicago, as reflected by his or her credit card billing address, zip code, or other reliable information. This "sourcing" determination is based on rules set forth in the Mobile Telecommunications Sourcing Conformity Act, 35 ILCS 638/1 et seq. Ex. B.

13. The Ruling states that "[b]ecause the amusement tax is imposed on the patron, and applies only to activity (i.e., the amusement) that takes place within Chicago, there is no question that the tax applies whenever the amusement takes place in Chicago." Ex. B.

14. The Ruling states that the question of whether a given provider has an obligation to collect the tax from its customer is beyond the Ruling's scope and that a provider may request a private letter ruling from the Chicago Department of Finance, pursuant to Uniform Revenue Procedures Ordinance Ruling #3 (June 1, 2004). Ex. B.

15. The Ruling states that where a charge is "bundled" by including both taxable and non-taxable elements, the Department of Finance applies the rules set forth in Personal Property Lease Transaction Tax Ruling #3 (June 1, 2004). Thus, the amount of amusement tax is based on the amount paid for any amusement, but excludes any separately-stated charges not for amusements. However, if an operator fails to separate the amusement portion of the price from the non-amusement portion, the entire price charged shall be deemed taxable, unless it is clearly proven that at least 50% of the price is not for amusements. Ex. B.

16. The effective date of the Ruling was July 1, 2015, but the Ruling states that the effect of the Ruling would be limited to periods on and after September 1, 2015." Ex. B.

17. In November 2015, the City Council, as part of the City's Revenue Ordinance for 2016, amended the Code as it relates to the amusement tax. That amendment states:

> In the case of amusements that are delivered electronically to mobile devices, as in the case of video streaming, audio streaming and on-line games, the rules set forth in the Illinois Mobile Telecommunications Sourcing Conformity Act, 35 ILCS 638, as amended, may be utilized for the purpose of determining which customers and charges are subject to the tax imposed by this chapter. If those rules indicate that the tax applies, it shall be presumed that the tax does apply unless the contrary is established by books, records or other documentary evidence.

2016 Revenue Ordinance (relevant portions) attached as **Exhibit C**, adding § 4-156-020(G)(1).

18. Prior to the Ruling, the Department of Finance was conducting audits and discovery investigations of providers of streaming services, and some of those providers were collecting the amusement tax from their Chicago customers. Dep. of Mark Pekic, p. 28:15 – 29:11, **Exhibit D**.

19. Mark Pekic is a City of Chicago Auditor Supervisor whose responsibilities include interpreting the amusement tax. Ex. D, p. 24: 3-7.

20. If the City of Chicago were to find that a provider of streaming services was not responsible for collecting and remitting the amusement tax from its Chicago customers because it did not have a substantial nexus to Chicago, the Chicago customers of such streaming services would be liable to pay the City the amount of the amusement tax owed on the charges for those streaming services. Ex. D, p. 53:5-14.

III. Description of various streaming service providers.

21. Netflix is a provider of an on-demand Internet streaming media service, which allows subscribers to watch video content online and offers a flat-rate video-by-mail service, which allows subscribers to borrow DVD and Blu-ray video discs and return them in prepaid mailers. Pls' Resp. Defs' Request for Documents, ¶ 1, **Exhibit E.**

22. Hulu is a provider of an on-demand Internet streaming media service, which allows subscribers to watch video content online. Ex. E, ¶ 1.

23. Spotify is a music streaming service, which allows consumers access to a large library of recorded music without commercial interruptions for a subscription fee. Ex. E, ¶ 1. Similar streaming music services are offered by Pandora (Pandora.com) Apple Music (https://www.apple.com/music), and Google Play (https://play.google.com).

24. Xbox Live Gold is an online multiplayer gaming and digital media delivery service created and operated by Microsoft, which for a fee, allows users to play games with others on an online network. Xbox Live Gold also provides paid members with the following features: matchmaking/smartmatch, private chat, party chat and in-game voice communication, game recording, media sharing, broadcasting one's gameplay via the Twitch live streaming application, access to free-to-play titles, "cloud" storage for gaming files, and early or exclusive access to betas, special offers, Games with Gold, and Video Kinect. Ex. E, ¶ 1.

25. Amazon Prime is a membership service that provides members with certain benefits provided by Amazon.com, including free two-day shipping and discounts on certain items sold on its website, but also provides access to streaming movies, and music, cloud photo storage, and the ability to borrow e-books. Ex. E, ¶ 1.

IV. Plaintiffs use of streaming services and payment of the amusement tax.

26. Starting before June 2015, and continuing through the present, Michael Labell has been a resident of Chicago, Illinois, and has paid for subscriptions to Netflix since January 2016, Spotify since January 2015, and Amazon Prime since February 2016. Decl. Michael Labell, **Exhibit F**, ¶¶ 1-2. Netflix and Spotify have collected the amusement tax in the amount of $59.49 from Michael Labell. *Id*. ¶ 8.

27. Starting before June 2015, and continuing through the present, Jared Labell has been a resident of Chicago, Illinois, and has paid for a subscription to Amazon Prime since

November 2016. Decl. Jared Labell, **Exhibit G**, ¶¶ 1-2. Amazon Prime has not collected the Chicago amusement tax from Jared Labell. *Id*. ¶ 3.

28. Starting before June 2015, and continuing through the present, Forrest Jehlik has been a resident of Chicago, Illinois, and has paid for a subscription to Netflix since January 2016. Decl. Forrest Jehlik, **Exhibit H**, ¶¶ 1-2. Netflix has collected the amusement tax in the amount of $17.10 from Forrest Jehlik. *Id*. ¶ 4.

29. Starting in 2014, and continuing through the present, Zack Urevig has lived in Chicago, Illinois, and has paid for subscriptions to Netflix and Amazon Prime since prior to June 2015, and Spotify since June 2016. Decl. Zack Urevig, **Exhibit I**, ¶¶ 1-2; Dep. Zack Urevig, p. 4:14-20; 12:3-7; 14:2-4; 20:15-16; **Exhibit J**. Netflix and Spotify have collected the amusement tax in the amount of $30.78 from Zack Urevig. Ex. I, ¶ 8.

30. Starting before June 9, 2015, and up until June 2016, and then from June 10, 2017, and continuing through the present, Bryant Jackson-Green was a resident of Chicago, Illinois, and has paid for subscriptions to Netflix from December 2015 through the present, Hulu from February 2016 through July 2016, Spotify since January 2015, and Amazon Prime since October 2016. Decl. Bryant Jackson-Green, **Exhibit K**, ¶¶ 1-2; Dep. Bryant Jackson-Green, **Exhibit L**, 4:11 – 5:15; 8:11-15; 11:8-11; 23:9-14; 27:10-11. Netflix, Hulu, and Spotify have collected the amusement tax in the amount of $41.85 from Bryant Jackson-Green. Ex. K, ¶ 10.

31. Natalie Bezek was a resident of Chicago, Illinois from prior to June 2015 until September 2016, and paid for a subscription to Spotify from April 2015 to August 2016, December 2016, and from March 2017 through September 2017. Decl. Natalie Bezek, **Exhibit M**, ¶¶ 1-2. Spotify collected the Chicago amusement tax from Natlie Bezek in the amount of $9.00, even for the months after she moved out of Chicago. *Id*. ¶¶ 3-4.

32. Emily Rose was a resident of Chicago, Illinois from prior to June 2015 until September 2016, and paid for subscriptions to Netflix from November 2015 to October 2016, Hulu from September 2015 to October 2016, and Amazon Prime since January 2015. Decl. Emily Rose, **Exhibit N**, ¶¶ 1-2. Netflix collected the amusement tax in the amount of $8.64 from Emily Rose, including for the months of October and November 2016 after she moved out of Chicago in September 2016. *Id*. ¶¶ 3-5. Hulu and Amazon Prime never collected the Chicago amusement tax from Ms. Rose. *Id*. ¶¶ 6-7.

Summary Judgment Standard

Summary judgment is appropriate "if the pleadings, depositions, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law." 735 ILCS 5/2-1005(c). Inferences may be drawn from undisputed facts, and summary judgment should be denied only where reasonable persons could draw divergent inferences from the undisputed facts. *Pyne v. Witmer*, 129 Ill. 2d 351, 358 (1989). General assertions unsupported by any evidentiary facts are insufficient to raise a triable issue as against uncontroverted evidentiary matter. *Purdy Co. of Illinois v. Transportation Ins. Co.*, 209 Ill. App. 3d 519, 529 (1st Dist. 1991).

Argument

I. The City's application of the amusement tax to streaming services exceeds its authority to tax under Article VII, Section 6(a) of the Illinois Constitution.

Article VII, Section 6(i) of the Illinois Constitution provides that "home rule units may exercise and perform concurrently with the State any power or function of a home rule unit to the extent that the General Assembly by law does not specifically limit the concurrent exercise or specifically declare the State's exercise to be exclusive." It is axiomatic that home rule units have no jurisdiction beyond their corporate limits except what is expressly granted by the legislature.

Seigles, Inc. v. City of St. Charles, 365 Ill. App. 3d 431, 434 (2006). "Thus, home rule units may not extend their home rule powers, such as the taxing power, beyond their borders unless expressly authorized by the General Assembly." *Hertz Corp. v. City of Chi.*, 2017 IL 119945, ¶ 14. Here, the amusement tax on streaming services applies beyond Chicago corporate limits, and the Illinois General Assembly has not expressly authorized the City to tax streaming services beyond its borders.

The amusement tax on streaming services imposes a 9% tax on customers of streaming services who have Chicago billing addresses regardless of whether those customers ever actually consume those streaming services in or outside of Chicago. As a result, the amusement tax on streaming services inevitably has the extraterritorial effect of taxing customers with Chicago billing addresses who only use a service outside of Chicago and therefore exceeds the grant of the authority set forth by Article VII, Section 6(a).

Apart from the Ruling, the amusement tax applies to certain "amusement" activities in Chicago regardless of whether the patron of such amusement lives in or outside of the city. For example, a person who purchases tickets to see the Chicago Blackhawks play hockey at the United Center in Chicago must pay the 9% amusement tax on the price of those tickets regardless of whether he or she lives in Chicago. But Chicago does not, and cannot, impose the amusement tax on patrons, even those who live in Chicago, of activities that do not take place in Chicago. Thus, a person who purchases tickets to see the Chicago Wolves play hockey at Allstate Arena, in Rosemont, just outside of Chicago, pays no amusement tax to the City – even if the purchaser lives in Chicago.

That only makes sense – but that is not how the Ruling applies the amusement tax to streaming services. Under the Ruling, the 9% amusement tax is applied to charges for streaming

services for any customer who provides a Chicago billing address, regardless of whether that customer uses those services in Chicago or somewhere else. Thus, the amusement tax applies to streaming services without regard to whether the consumption of those services takes place within Chicago: Everyone with a Chicago billing address pays the tax even if they only use a service outside Chicago, and everyone without a Chicago billing address does not pay the tax, even if they only use those services within Chicago.

If the City applied the amusement tax to amusements generally in the same way it applies the tax to streaming services, it would charge persons with a billing address in Chicago when they purchase tickets for any amusement anywhere – such as a hockey game in Rosemont – but would not tax persons who do not have a billing address in Chicago when they purchase tickets for any amusements that physically take place in Chicago – like a hockey game at the United Center. And that would obviously exceed the City's constitutional taxing authority under Article VII, Section 6 of the Illinois Constitution.

Indeed, the Illinois Supreme Court has recently held that Chicago has no authority to tax activities outside its borders except where the Illinois General Assembly has explicitly authorized it to do so. *See Hertz Corp*., 2017 IL 119945, ¶ 14. In *Hertz,* the City of Chicago attempted to impose its lease tax on all Chicago residents who leased vehicles from suburban vehicle rental agencies located within three miles of Chicago's borders – based on the assumption that all Chicago residents would use the rental vehicles primarily in the City – in the absence of written proof that a Chicago resident customer would use the vehicle primarily outside of Chicago. *Id*. at ¶ 5. In contrast, the City did not impose the lease tax on persons who were not Chicago residents who leased vehicles from such suburban vehicle rental agencies. *Id*. The Illinois Supreme Court found that the City had improperly extended its home rule power to

tax beyond its borders because it imposed the lease tax "not on actual use within the City's borders but on the lessee's stated intent to use the property in Chicago or, failing any statement of intent, on presumed use based upon the lessee's residence address." *Id.* at ¶ 29.

The Ruling's application of the amusement tax is analogous to the City's application of the lease tax that the Court struck down in *Hertz*. The Ruling's imposition of the amusement tax on streaming services is not based on actual use within the city's borders but on "the conclusive presumption of taxability based on residency" – or in this case a Chicago billing address. Those with a Chicago billing address are presumed to use streaming services in Chicago, while those without a Chicago billing address are presumed to not use streaming services in Chicago. And unlike the lease tax ruling in *Hertz*, the Ruling does not provide any way for a customer with a Chicago billing address to overcome the presumption that he or she will use streaming services exclusively in Chicago. That means that the City will *always* impose the amusement tax on streaming services used outside of Chicago by customers with a Chicago billing address.

Like the lease tax in *Hertz*, the amusement tax on streaming services is a tax on activities that take place outside of Chicago's borders. And, like the City's extraterritorial application of the lease tax, the Ruling's application of the amusement tax to activities outside its borders has not been expressly authorized by the General Assembly. *See Seigles, Inc.*, 365 Ill. App. 3d at 434. Therefore, the Ruling, like the City's application of the lease tax, exceeds the City's constitutional authority and is therefore invalid.

The Ruling's text attempts to justify its taxation of extraterritorial activities by citing the state's Mobile Telecommunications Sourcing Conformity Act, 35 ILCS 638/1 et seq. ("Mobile Sourcing Act"). SOF 12. But a statutory authorization for a municipality's extraterritorial exercise of power must be express, not implied. *Seigles, Inc.*, 365 Ill. App. 3d at 435. And the

Mobile Sourcing Act does not expressly authorize the City to impose the amusement tax on customers of streaming services with Chicago billing addresses when they use those services outside of Chicago.

The Mobile Sourcing Act allows a municipality to tax charges paid by customers of "mobile telecommunications services" provided by a "home service provider" if the customer's place of primary use is within the territorial limits of that municipality. 35 ILCS 638/20(b). And the Mobile Sourcing Act allows a municipality to tax a cell phone customer if his or her residential street address or primary business street address and the cell phone service provider's licensed service area are in the municipality's boundaries. 35 ILCS 638/10.

But that has nothing to do with streaming services. Streaming services are not "mobile telecommunications services," which the law defines as radio communication services carried on between mobile stations or receivers and land stations, and by mobile stations communicating among themselves, 47 C.F.R. § 20.3; 35 ILCS 638/10, and which are essentially cellular services that provide telephone and Internet access. And the providers of streaming services are not "home service providers," which the law defines as a facilities-based carriers or resellers with a customer contract for the provision of mobile telecommunications services, 35 ILCS 638/10 – in other words, cellular service providers like Verizon and Sprint. Therefore, the Mobile Sourcing Act does not provide the City with any *express* authority to tax streaming services that are used outside of its borders. *See Seigles, Inc.*, 365 Ill. App. 3d at 434.

For these reasons, the Ruling's application of the amusement tax on streaming services exceeds the City's constitutional authority to tax amusements, and this Court should declare the Ruling invalid and enjoin its enforcement.

II. The amusement tax applies to streaming services differently than it applies to in-person amusements in violation of the Uniformity Clause of the Illinois Constitution.

The Uniformity Clause (Article IX, § 2) of the Illinois Constitution provides:

> In any law classifying the subjects or objects of non-property taxes or fees, the classes shall be reasonable and the subjects and objects within each class shall be taxed uniformly. Exemptions, deductions, credits, refunds and other allowances shall be reasonable.

This clause "imposes more stringent limitations than the equal protection clause on the legislature's authority to classify the subjects and objects of taxation." *Allegro Servs. v. Metro. Pier & Exposition Auth.*, 172 Ill. 2d 243, 249 (1996). The test that courts apply in Uniformity Clause cases (the *Searle* test) is "well-established": "a non-property tax must be based on a real and substantial difference between the people taxed and not taxed, and must bear some reasonable relationship to the object of the legislation or to public policy." *Geja's Cafe v. Metro. Pier & Exposition Auth.*, 153 Ill. 2d 239, 247 (1992) (citing *Searle Pharmaceuticals, Inc. v. Dep't of Revenue*, 117 Ill. 2d 454, 468 (1987)).

A plaintiff is not required to come forward with any and all conceivable explanations for the tax and then prove each one unreasonable; upon a good-faith uniformity challenge, a taxing body must produce a justification for its classifications. *Geja's Cafe*, 153 Ill. 2d at 248. It then becomes the plaintiff's burden to persuade the court that the purported justification is insufficient, either as a matter of law or as unsupported by the facts. *Id*. at 248-49; *see also Empress Casino Joliet Corp. v. Giannoulias*, 231 Ill. 2d 62, 72 (2008).

A. The amusement tax violates the Uniformity Clause because it applies to streaming services differently than it applies it other amusements.

The amusement tax, by its terms, applies to amusements *within the City of Chicago*. Chi. Mun. Code 4-156-020. But the way that the City imposes the amusement tax on streaming

services treats customers of streaming services differently based on the billing addresses of those customers, not based on whether such customers use streaming services in Chicago.

While the purported purpose of the amusement tax is to tax customers for the privilege of using streaming services and other amusements that take place in Chicago, the Ruling *only* applies the tax to customers of streaming services with Chicago billing addresses regardless of whether they use those services in Chicago, and *never* applies to customers of streaming services that do not have Chicago billing addresses, even if those customers use those streaming services in Chicago. In contrast, the amusement tax otherwise applies *only* to customers of all other amusements who incur charges for amusements that take place in Chicago, and *never* applies to customers of amusements who incur charges for amusements that take place outside of Chicago, even if those customers are Chicago residents, or have Chicago billing addresses.

In *Searle,* the Illinois Supreme Court found that there is no real and substantial difference between a corporation that is a member of an affiliated corporate group and elects to file a federal consolidated income tax return and a corporation that is a member of an affiliated corporate group and does not elect to file a consolidated corporate Federal income tax return, where the state permitted the latter to "carry back" an operating loss over the three previous years, but prohibited the former from doing so. 117 Ill. 2d at 469. The Illinois Supreme Court has also found that where two alcoholic products were virtually identical save for the method of production of their alcoholic content, there was no real and substantial difference between them, and the state could not tax one at a rate nearly eight times higher. *Federated Distribs., Inc. v. Johnson,* 125 Ill. 2d 1, 21 (1988). The Court found that taxing these virtually identical low-alcohol products at different rates bore no reasonable relationship to the object of the legislation

– to promote temperance in the consumption of alcohol – and in fact, it would actually frustrate that purpose. *Id.*

The City's inconsistent application of the amusement tax is similarly irrational. There is no "real and substantial difference" between customers of streaming services who are taxed under the Ruling and those who are not that is rationally related to the City's objective in taxing amusements that take place within Chicago. There is no "real and substantial difference" between customers of streaming services who do not live in Chicago but use those services in Chicago – who are not taxed – and customers of other amusements that take place in Chicago and do not live in Chicago – who are taxed. Similarly, there is no "real and substantial difference" between customers of streaming services who live in Chicago but use streaming services outside of Chicago – who are taxed – and customers of other amusements that take place outside of Chicago and live in Chicago – who are not taxed. The only difference is the type of amusement that the customer is paying for – either in or outside of Chicago.

Further, there is no rational relationship between the different applications of the amusement tax to streaming services and other amusements and the object of the amusement tax. The purpose of the amusement tax is to tax charges paid on amusements that take place in Chicago, and the amusement tax does, in general, only tax amusements that tax place within Chicago – but not with respect to streaming services, which the City taxes not based on whether they are used in Chicago but based on a customer's billing address, which has no necessary relationship to where the customer uses the service. Thus, the Ruling's application of the amusement tax to streaming services violates the Uniformity Clause.

B. The Ruling violates the Uniformity Clause because it subjects streaming services to greater taxation than automatic amusement machines that deliver the same types of entertainment.

The amusement tax also violates the Uniformity Clause for a second reason: because it does not apply to "automatic amusement machines," that provide video, music, and gaming entertainment, such as video machines, jukeboxes, and pinball machines, SOF 5, but, under the Ruling, does apply to streaming services, similar services transmitted over the Internet that provide video, music, and gaming. The Code exempts use of automatic amusement machines from the amusement tax and instead subjects their operators to a $150 tax per year per device. SOF 4.

There is no "real and substantial difference" between customers of automatic amusement machines and customers of streaming services that justifies exempting the former from taxation and taxing the latter. Both services provide on-demand video, music, or gaming entertainment. For example, Spotify, an Internet music service, allows consumers to access recorded music from a library of music for a fee, SOF 23, – just as a jukebox does.[1] Xbox Live Gold allows one to play videogames, SOF 24, just as a coin-operated video game machine does, and Netflix allows one to watch videos, SOF 21, just as a video booth does. Yet customers of streaming services are taxed at 9%, while customers of automatic amusement machines are not taxed at all. The only difference between customers of automatic amusement machines and customers of streaming services is how the customer accesses the video, audio, or gaming entertainment.

When Chicago imposed its transaction tax on coin-operated self-serve car washes, while exempting automatic car washes, the First District Court of Appeals found no real and

[1] Modern jukeboxes, incidentally, can operates by allowing one to choose a song from a library on the Internet. *See, e.g,* Internet jukeboxes offer countless tunes, GMA News Online, http://www.gmanetwork.com/news/scitech/content/7070/internet-jukeboxes-offer-countless-tunes/story.

substantial difference between self-serve car washes and automatic car washes, calling it an "artificial distinction . . . based solely on the customer's hands-on participation in [the self-serve] wash process." *Nat'l Pride of Chicago, Inc. v. Chicago*, 206 Ill. App. 3d 1090, 1104-05 (1st Dist. 1990). The distinction between streaming services and automatic amusement machines is similarly arbitrary.

In addition, the tax on customers of streaming services, but not customers of automatic amusement machines does not bear a reasonable relationship to the object of the legislation or to public policy. The purported purpose of the amusement tax is to tax customers of amusements that take place in Chicago. But exempting customers of automatic amusement machines in Chicago does not serve that purpose.

C. The Ruling violates the Uniformity Clause because it taxes certain performances delivered through streaming services at a higher rate than it taxes in-person live performances.

The Ruling also violates the Uniformity Clause for a third reason: because it taxes certain performances at a higher rate than the Code taxes those same performances when they are consumed in person. The Code exempts from the amusement tax "admission fees to witness in person live theatrical, live musical or other live cultural performances that take place in any auditorium, theater or other space in the city whose maximum capacity, including all balconies and other sections, is not more than 750 persons," and taxes such performances in a space with a capacity of greater than 750 persons at a reduced rate of 5%. SOF 6. The City asserts that the purpose of the exemption is to "foster the production of live performances that offer theatrical, musical or cultural enrichment to the city's residents and visitors." Chicago Amend Coun. J. 11-12-98, p. 81835, **Exhibit O**.

There is no real and substantial difference between live theatrical, musical, or cultural performances and streaming services providing similar or identical performances. The only difference is that live performances take place at a specific venue in Chicago, whereas such customers of streaming services can view similar performances from anywhere. This is not a difference in substance; it is a difference in form. The substance – the performances – are the same; it is only the form – whether one is watching at a specific venue or on the Internet – that is different.

In addition, exempting (or applying a reduced rate to) live theatrical, musical, or cultural performances from the amusement tax while applying the tax to streaming services that provide similar or identical performances bears no reasonable relationship to the object of the legislation or to public policy. The City's purpose is to foster the production of live performances that offer theatrical, musical, or cultural enrichment to the City's residents and visitors, and viewing such performances over the Internet furthers that purpose. City residents who view such performances on the Internet can be just as enriched as persons who view them in person, and those who produce such performances can profit from having them sold through streaming services. The reality is that the City is simply using the amusement tax to benefit certain amusements that it likes at the expense of other amusements. That's exactly what the Uniformity Clause prohibits.

For these reasons, the City's favorable treatment of live theater, musical, or cultural performances by eliminating or reducing the amusement tax on those performance, while imposing the amusement tax on similar streaming services violates the Uniformity Clause.

III. The amusement tax discriminates against electronic commerce in violation of the Internet Tax Freedom Act.

The Internet Tax Freedom Act ("ITFA"), which is set forth in a note to 47 U.S.C. § 151, provides that no state or political subdivision of a state may impose multiple or discriminatory

taxes on electronic commerce. ITFA § 1101(a). Congress enacted ITFA to "foster the growth of electronic commerce and the Internet by facilitating the development of a fair and consistent Internet tax policy." S. Report No. 105-184, at 1 (1998). One of ITFA's primary purposes is to prevent state and local taxing authorities from imposing discriminatory taxes on electronic commerce that would stifle its development. *See, e.g.*, H.R. Rep. No. 105-808, pt. 1, at 8–9 (1998) (explaining that discriminatory state taxation could prevent electronic commerce from becoming ubiquitous); S. Rep. No. 105-184, at 2, 11 (1998) (stating that ITFA was intended to encourage "policies on taxation that eliminate any disproportionate burden on interstate commerce conducted electronically and establish a level playing field between electronic commerce using the new media of the Internet and traditional means of commerce").

ITFA accordingly imposes a moratorium on "discriminatory taxes on electronic commerce." ITFA § 1101(a)(2). Further, Congress recently enacted a permanent moratorium on discriminatory taxes on electronic commerce with the Trade Facilitation and Trade Enforcement Act of 2015, 114 Pub. L. No. 125, § 922, 130 Stat. 122 (2016). "Electronic commerce" is "any transaction conducted over the Internet or through Internet access, comprising the sale, lease, license, offer, or delivery of property, goods, services, or information, whether or not for consideration, and includes the provision of Internet access." ITFA § 1105(3). The term "tax" under the ITFA includes those that a seller is required to collect and remit. ITFA § 1105(8). A tax on electronic commerce tax is deemed to be a "discriminatory tax" if it:

> (i) is not generally imposed and legally collectible by such State or such political subdivision on transactions involving similar property, goods, services, or information accomplished through other means; [or]
>
> (ii) is not generally imposed and legally collectible at the same rate by such State or such political subdivision on transactions involving similar property, goods, services, or information accomplished through other means . . .; [or]

> (iii) imposes an obligation to collect or pay the tax on a different person or entity than in the case of transactions involving similar property, goods, services, or information accomplished through other means . . . .

Id. § 1105(2)(A)(i)-(iii). ITFA does not prohibit the taxation of electronic commerce transactions per se but does prohibit jurisdictions from imposing greater tax burdens on electronic transactions when such burdens are not imposed on traditional commerce. Moreover, in determining the existence of discrimination, ITFA compares transactions that are "similar"; they need not be identical.

ITFA prohibits the City from imposing a tax at a different rate on services provided over the Internet, such as streaming services, than on transactions involving similar services provided through other means, ITFA, § 1105(2)(A)(ii), and from imposing an obligation to pay the tax on a different person or entity on services provided by the Internet, than on transactions involving similar services provided through other means, ITFA § 1105(2)(A)(iii).

The Illinois Supreme Court recently addressed whether a state statute violated ITFA by requiring out-of-state retailers to collect use taxes on performance marking sales exceeding $10,000. *Performance Mktg. Ass'n v. Hamer*, 2013 IL 114496, ¶ 23. "Performance marketing" refers to marketing or advertising programs in which a person or organization that publishes or displays an advertisement is paid by a retailer when a specific action, such as a sale, is completed. *Id*. at ¶ 8. The statute imposed the use tax obligation on out-of-state retailers that made sales through performance marketing over the Internet, but did not impose the obligation on out-of-state retailers conducting performance marketing activities through print media or on over-the-air broadcasting in Illinois. *Id.* at ¶ 23. The Court held that the statute violated ITFA because it only applied to online performance marketing and therefore imposed a discriminatory tax on electronic commerce.

Similarly, under the Ruling, the amusement tax imposes an unlawful discriminatory tax on electronic commerce by taxing streaming services but not on similar amusements that take place in person in Chicago.

The Ruling's imposition of the amusement tax on streaming services violates ITFA because, as explained in Section II.B, it requires customers of streaming services to pay the amusement tax, even as the Code entirely exempts users of "automatic amusement machines," – which also allow users to watch videos, listen to music, and play games – from taxation. Rather, the City imposes a $150 tax per year per device on the operator of the automatic amusement machine. Thus, the City taxes entertainment that is delivered through the Internet at a higher rate than it taxes identical entertainment that is not delivered through the Internet – precisely what ITFA prohibits.

In addition, the application of the amusement tax on streaming services violates ITFA because, as explained in Section II.C, live theatrical, musical, and cultural performances at theaters and other venues are either exempt from the amusement tax or are taxed at a lower rate, depending on the size of the venue. Streaming services that provide access to similar or identical theatrical, musical, or cultural performance over the Internet are subject to the 9% amusement tax, and thus are tax at a higher rate than similar live in-person theatrical, musical, and cultural performances.

Defendants cannot distinguish between live performances in a theater or other venue and those delivered through the Internet by asserting, as they do, that the two are different because the experience of watching an in-person performance is different from the experience of watching a performance on the Internet. That is the exact distinction that ITFA prohibits: treating a product delivered online as though it is different simply because it is delivered online. No

doubt the "experience" of participating in performance marketing delivered over the Internet is much different from the experience of participating in performance marketing delivered in print or on an over-the-air broadcast – but the Illinois Supreme Court nonetheless held that the state could not impose a use-tax obligation on one but not the other. *Performance Mktg.*, 2013 IL at ¶ 23. Likewise, in this case, streaming services provide theatrical, musical, and cultural performances as those performed live and in person. The fact that the latter provide a different experience that are similar (and sometimes identical) in content to those performed live and in person. The fact that the latter may provide a different experience because they are in person and not on the Internet, is not an appropriate distinction to make under ITFA; it is the very distinction that ITFA prohibits. Therefore, the Ruling's application of the amusement tax to streaming services violates ITFA.

IV. The amusement tax applies to streaming services that are used outside Chicago in violation of the Commerce Clause of the United States Constitution.

The Commerce Clause (Article I, Section 8, Clause 3) of the United States Constitution prohibits state interference with interstate commerce. A local tax satisfies the Commerce Clause only if it "(1) is applied to an activity with a substantial nexus with the taxing state, (2) is fairly apportioned, (3) does not discriminate against interstate commerce, and (4) is fairly related to the services provided by the State." *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977); *Quill Corp. v. North Dakota*, 504 U.S. 298, 311 (1992). The Ruling's application of the Amusement Tax to Internet services violates requirements (1), (2) and (4).

A. There is no substantial nexus between Chicago and streaming services.

The Ruling's application of the amusement tax to streaming services does not satisfy the substantial-nexus requirement. For an activity to have a substantial nexus with a particular

jurisdiction, there must be a connection between the jurisdiction and the activity itself – not just a connection between the jurisdiction and the actor the government seeks to tax. *Allied-Signal, Inc. v. Dir., Div. of Taxation*, 504 U.S. 768, 778 (1992).

In *National Bellas Hess v. Department of Revenue*, 386 U.S. 753 (1967), the Supreme Court struck down an attempt by Illinois to require an out-of-state mail-order house to collect the state's use tax when its only connection with Illinois customers was by delivery of goods by common carrier or mail. *Id*. at 754. The company owned no tangible property in Illinois, had no sales outlets, representatives, telephone listings, or solicitors in Illinois, and did not advertise in Illinois by radio, television, billboards, or newspapers. *Id*. The Court concluded that the company's contacts were insufficient to satisfy the substantial-nexus requirement. *Id*. at 759. As the Supreme Court later explained, *Bellas Hess* stands for the proposition that a vendor whose only contacts with the taxing State are by mail or common carrier lacks the "substantial nexus" required by the Commerce Clause. *Quill Corp.*, 504 U.S. at 311.

Under the Ruling, there is no substantial nexus between streaming services that are taxed and Chicago. The Ruling's use of billing addresses as a proxy for use of streaming services within the city does not ensure a substantial nexus between the City and activities it is taxing. Again, the substantial-nexus rule requires that the City have a connection with the *activity* is taxing – not just the *actor* who pays the tax. *Allied-Signal, Inc.*, 504 U.S. at 778. But the Ruling's taxation based on billing addresses ensures only (at most) that the City has a connection with the actor who pays the tax – it does not ensure that the City has any connection with the activity being taxed because, as discussed above, a customer with a Chicago billing address might consume streaming services entirely outside Chicago. The Ruling therefore fails the substantial-nexus requirement and violates the Commerce Clause.

B. There is no fair apportionment between the tax and the customer's use of streaming services.

In addition, the Ruling's tax on streaming services does not satisfy the fair-apportionment requirement of the Commerce Clause test because the tax is imposed when the customer is witnessing, viewing, or participating in amusements outside of Chicago. "The primary purpose of the fair apportionment prong . . . is to prevent multiple taxation by 'ensur[ing] that each State taxes only its fair share of an interstate transaction.'" *Irwin Indus. Tool Co. v. Ill. Dep't of Revenue*, 238 Ill. 2d 332, 345 (2010) (citation omitted). To be fairly apportioned, a tax must be internally and externally consistent. *Id*. at 345-46. To be internally consistent, a tax must be structured so that, if every state were to impose the same tax, no multiple taxation would result. *Id*. at 346. To be externally consistent, a tax must apply only to that portion of the revenues from the interstate activity that reasonably reflects the in-state component of the activity being taxed. The Court thus examines "the in-state business activity which triggers the taxable event and the practical or economic effect of the tax on that interstate activity." *Id*. (quoting *Goldberg v. Sweet*, 488 U.S. 252, 260-61 (1989)).

Here, the Ruling's tax on streaming services is not externally consistent – it does not apply only to that portion of the revenues from the interstate activity that reasonably reflects the in-state component of the activity being taxed. The City taxes streaming services based on the customer's billing address, not where the customer uses those services. The Ruling's tax on streaming services is all or nothing: If you have a billing address in Chicago, you pay the tax; if you don't have a billing address in Chicago, you don't pay the tax, regardless of how much you use those streaming services in Chicago.

C. The tax on streaming services is not fairly related to the extent of the contact with Chicago.

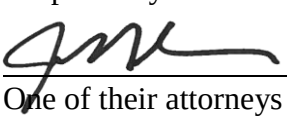
Finally, the Ruling's tax on streaming services does not satisfy the fairly related requirement. The "fairly related" prong of the Commerce Clause test requires that "the measure of the tax must be reasonably related to the extent of the contact." *Commonwealth Edison Co. v. Montana*, 453 U.S. 609, 626 (1981). Here, the tax on streaming services is not reasonably related to the extent of the contact with Chicago. As stated through this brief, the City imposes the tax on streaming services only on those who have a Chicago billing address, but does not impose the tax on those without a Chicago billing address. Allowing the City to tax amusements simply because a customer has a billing address in the City, would allow the City to tax all Chicago residents who pay for amusements outside of the city. This is not enough to satisfy the fourth prong – that the tax is fairly related to contact of the activity with Chicago.

Conclusion

Plaintiffs ask the Court to enter summary judgment (1) declaring that the Ruling's application of the amusement tax to streaming services violates Article VII, Section 6 and the Uniformity Clause of the Illinois Constitution, the Internet Tax Freedom Act, and the Commerce Clause of the U.S. Constitution; (2) enjoining the City from collecting the Ruling's tax on streaming services; and (2) awarding the Plaintiffs $166.86 in damages for the amount in amusement taxes collected from each of them for their use of streaming services.

Dated: September 27, 2017

Respectfully submitted,



One of their attorneys

Jeffrey M. Schwab (#6290710)
Jacob H. Huebert (#6305339)
Liberty Justice Center (#49098)
190 S. LaSalle Street, Suite 1500
Chicago, Illinois 60603
Telephone (312) 263-7668
Facsimile (312) 263-7702
jschwab@libertyjusticecenter.org
jhuebert@libertyjusticecenter.org

CERTIFICATE OF SERVICE

I, Jeffrey Schwab, an attorney, hereby certify that on September 27, 2017, I served the foregoing Plaintiffs' Motion For Summary Judgment on Defendants' counsel of record by the Court's Electronic Filing System and electronic mail to Steve Tomiello (Steven.Tomiello@cityofchicago.org).

Jeffrey M. Schwab