

The Counselor

The newsletter of the Illinois State Bar Association's Business Advice & Financial Planning Section

Requirements contract or not? No courts agree

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BY STEPHEN M. PROCTOR

A contract for the sale of goods should state a quantity to be enforceable. (Uniform Commercial Code Article 2201). Article 2 of the UCC permits a quantity to be measured by the "requirements of the buyer." (UC Article 2306) Of course, "requirements of the buyer" is not a fixed quantity, but it is sufficient to be

enforceable.

As interpreted by the 7th Circuit Court of Appeals, a requirements contract has the following elements: 1) it must obligate the buyer to buy goods, 2) it must obligate the buyer to buy goods exclusively from the seller, and 3) it must obligate the

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Tax scams hit home

BY KATHRYN GARLOW, CPA, JD, CSEP

My sister called and asked me for my advice, "Kathy, someone from the IRS called and left a message. They want me to call them back. I'm worried." I replied with the same answer I have given clients who receive a similar call, "This is a fake phone call. The IRS doesn't contact you by telephone, only through written correspondence." The false calls are becoming more frequent. I even received a voice mail message on my cell phone from a Washington DC number claiming that he was an IRS officer and I was guilty of tax evasion. He told me not to disregard this message and I needed to call back right away before I was arrested. At least the gentleman concluded his message with a

friendly wish to have a nice day.

The IRS warns that these con-artists sound very convincing. The callers want consumers to share their personal information, enabling the scammers to use the stolen identities to file fraudulent tax returns or compel taxpayers to wire money they do not owe. The callers claim to be employees of the IRS and use fake names and identification badge numbers. Victims are told to pay their balance due through a pre-loaded debit card or wire transfer. The callers can become hostile and insulting as they threaten to arrest or deport the victim.

On the IRS website there is a list of five tell-tale signs of a scam where scammers

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buyer to by all of its requirements from the seller. Note the emphasis on the buyer's obligations.

BRC Rubber & Plastics, Incorporated (BRC) entered into an agreement on January 1, 2010 to purchase carbon black from Continental Carbon Company. But Continental had trouble filling all of its orders for carbon black and refused to ship some of BRC's orders. BRC sued, claiming it had a requirements contract and that Continental breached it by refusing to ship BRC's orders. The district court agreed and awarded damages to BRC for nearly \$1 million. But Judge Williams of the 7th Circuit Court of Appeals had a much different view of the contract. (*BRC Rubber & Plastics, Incorporated v. Continental Carbon Company*, 7th Circuit Court of Appeals, Nos. 14-1416 & 14-1555, Nov. 5, 2015).

The terms of the agreement between BRC and Continental included the following:

"Quantity of Material

It is the intent of this Agreement that Continental Carbon Company agrees to sell to BRC Rubber and Plastics approximately 1.8 million pounds of [carbon] black annually. These volumes are to be taken in approximately equal monthly quantities. BRC Rubber and Plastics, to the best of their ability, will provide accurate forecasts of the future usage at their manufacturing sites which will assist Continental Carbon Company in meeting these and additional requirements."

"Meet or Release

If during the term of this agreement BRC receives an offer that they believe is better than the terms offered in this agreement, Continental Carbon will have the right to meet this

agreement or release BRC from any further obligation . . ."

There was also a "Rebate/Penalty" provision under which BRC would pay a little less per pound if it bought much more than 1.8 million pounds annually, and a little more per pound if it bought much less.

In 2010, Continental shipped 2.6 million pounds to BRC. However, in 2011, Continental could not keep up with demand. BRC placed an order on April 26, 2011 which Continental neither confirmed nor shipped. The parties continued communicating and it soon became apparent that there was a fundamental difference in their view of the agreement. In Continental's view, as long as it shipped approximately 1.8 million pounds annually, it did not have to accept and fill every BRC order. In BRC's view, it's agreement with Continental was a requirements contract and Continental had to fill all of BRC's orders. As noted, BRC filed suit, persuaded the district court that the agreement was, indeed, a requirements contract, and was awarded nearly \$1 million.

Judge Williams, writing for the 7th Circuit, vacated the judgment and sent the case back. To analyze the reasons, we go back to the elements of a requirements contract as defined by 7th Circuit cases. Basically, BRC was not obligated to purchase.

First was the provision regarding the quantity of material that BRC was "required" to purchase. To Judge Williams, this provision was an estimate and did not contain the critical element of actually requiring BRC to purchase anything.

Second, Judge Williams viewed the "Meet or Release" provision as a right of first refusal. If BRC wanted to buy carbon black from another seller at a lower price, Continental would be given the chance to meet the price. Added Judge Williams, "But nothing in the "Meet or Release" provision prevented BRC from manufacturing its own carbon black or abandoning its use of carbon black altogether. In other words,

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OFFICE

ILLINOIS BAR CENTER
424 S. SECOND STREET
SPRINGFIELD, IL 62701
PHONES: 217-525-1760 OR 800-252-8908
WWW.ISBA.ORG

EDITORS

Dennis J. Jacknewitz
David A. Johnson, Jr.

MANAGING EDITOR / PRODUCTION

Katie Underwood

✉ kunderwood@isba.org

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the provision did not obligate BRC to buy carbon black from Continental.”

Third, the agreement lacked the critical element of exclusivity. BRC again cited the “Meet or Release” provision to demonstrate that BRC had to buy exclusively from Continental. But, to Judge Williams, that was a misreading of the provision. As noted, Judge Williams saw it as a right of first refusal. Judge Williams further noted that price is not the only factor when a buyer decides from whom to buy and BRC conceded as much. So, again, the provision lacked the exclusivity element required by the 7th Circuit.

Interestingly, the court never indicated whether BRC actually purchased exclusively from Continental. Presumably, it did (at least until Continental refused to ship). But the court did emphasize

a point that was more important than whether BRC purchased exclusively from Continental, that is whether BRC *had to purchase exclusively* from Continental. One way to analyze the case is to view it from the opposite perspective. Suppose it had been BRC that purchased carbon black from someone other than Continental? What remedies would Continental have had? Based on the decision by Judge Williams, the answer is probably none. No provision in the agreement quoted by the court would have provided Continental with specific remedies or clear damages if Continental had been the aggrieved party.

So the conclusion goes back to the elements of a requirements contract. No doubt BRC intended to buy carbon black from Continental. BRC could have made explicit its intention to buy exclusively

from Continental all of its requirements of carbon black. But BRC may have intended to “hedge its bets” by leaving these critical elements open and ambiguous. In doing so, it also gave an “out” for Continental. The lesson is that any buyer that expects to have an assured supply of products by purchasing its requirements from a specific seller should make clear in the agreement that the buyer is also committing to purchase its requirements from the seller exclusively, exposing the buyer to damages if the buyer goes elsewhere for its products. ■

For more information about this article, contact Stephen M. Proctor, Vice Chair of the Business Group, at 847.734.8811 or via e-mail at sproctor@masudafunai.com.

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Tax scams hit home

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request information. Note that the IRS works differently from these scams, as follows:

1. The IRS will only ask for payment with a written, mailed bill. They will not ask for payment over the telephone.
2. In the written correspondence, the IRS will give you the opportunity to question or appeal the amount due.
3. The IRS does not require taxpayers to pay only by a prepaid debit card.
4. The IRS will not ask for credit or debit card numbers over the phone.
5. The IRS will not threaten to bring in law-enforcement groups to have you arrested for not paying the amount due.

In addition to not making phone calls, the IRS also does not use unsolicited emails, text messages or any social media to discuss the taxpayer’s personal tax issue.

If a taxpayer wants to contact the IRS to find out about their tax return, they should call the IRS at 1-800-829-1040. If a taxpayer has been contacted in one of these scams, they can report the incident to the Treasury

Inspector General for Tax administration at 1-800-366-4484 or at the website, <www.tigta.gov>.

In addition to the telephone scams, there is also a rise in identity theft. Thieves file false tax returns under stolen social security numbers to claim and collect false refunds. They also use stolen Federal Employer Identification Numbers of businesses to create false Forms W-2 to further the fraud of stolen refunds. The IRS is aware of these issues and according to their website they are “working hard to prevent and detect identity theft as well as reduce the time to resolve these issues.”

The IRS has been sending out notices to notify taxpayers that there are issues with processing their tax return or that more information is needed to accurately process the return. The IRS is finding that multiple returns are filed under the same social security number and returns are filed with false W-2 withholding information to claim refunds. The IRS is holding the returns from further processing until the taxpayer contacts them.

Once it is determined that the social security number has been compromised, that taxpayer needs to do the following:

- Respond immediately to the IRS tax notice
- Complete IRS Form 14039, Identity Theft Affidavit
- File a report with law enforcement
- Report identity theft at www.ftc.gov
- Contact one of the three major credit bureaus (Equifax, Experian, TransUnion) to place a fraud alert on their credit records.
- Contact their financial institutions to see if any accounts have been breached.

The IRS will respond to the taxpayer by assigning an identification number (ITIN) that the taxpayer will then use to file his next tax return. This number will only be good for one tax year. The IRS will automatically reassign a new ITIN each year. This system is meant to prevent taxpayers from being victimized by identity thieves a second time after the IRS has closed their case.

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The IRS is allocating more resources to the issues of the fraudulent calling schemes and identity theft. They understand that they need to revamp their fraud detection system to catch new schemes as they emerge. Meanwhile, the IRS suggests protecting yourself, as follows:

- Don't carry your Social Security Card or any documents that contain your Social Security number (SSN) or Individual Taxpayer Identification Number (ITIN)
- Don't freely give out your SSN or ITIN; only give it out when required
- Protect your financial information
- Check your credit report every 12 months
- Review your Social Security Administration earning statement annually
- Secure personal information in your home
- Protect your personal computer by using firewalls and anti-spam/virus software.
- Change your passwords on Internet accounts
- Don't give out personal information over the phone, through the mail or Internet unless you have initiated the contact or you are sure you know who you are dealing with

Taxpayers need to be alert and take precautions. ■



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