

IN THE UNITED STATES DISTRICT COURT FOR THE
NORTHERN DISTRICT OF ALABAMA
SOUTHERN DIVISION

UNITED STATES OF AMERICA)	
)	
Plaintiff,)	
)	
v.)	Civil No.
)	
LAKEISHA PEARSON)	
)	
Defendant.)	

COMPLAINT FOR PERMANENT INJUNCTION AND OTHER RELIEF

The United States of America, by undersigned counsel, alleges as follows:

1. The United States brings this complaint to enjoin Lakeisha Pearson and any other person working in concert or participation with her from directly or indirectly:

(a) preparing federal income tax returns, amended returns, or other tax-related documents and forms, including any electronically-submitted tax returns or tax-related documents, for any entity or person other than herself;

(b) assisting in the preparation of federal tax returns and amended returns;

(c) understating taxpayers' liability as prohibited by 26 U.S.C. § 6694;

(d) engaging in other activity subject to penalty under 26 U.S.C. §§ 6694, 6695(g), 6700, and 6701;

(e) engaging in any activity subject to penalty under 26 U.S.C. § 6695, including failing to supply a list of clients or provide copies of clients' tax returns to the Service on request; and

(f) engaging in conduct that substantially interferes with the proper administration and enforcement of the tax laws.

2. This action has been requested by the Chief Counsel of the Internal Revenue Service, a delegate of the Secretary of the Treasury, and commenced at the direction of a delegate of the Attorney General of the United States pursuant to 26 U.S.C. §§ 7401, 7402, 7407, and 7408.

Jurisdiction and Venue

3. Jurisdiction is conferred on this Court by 28 U.S.C. §§ 1340 and 1345 and 26 U.S.C. §§ 7402(a), 7407, and 7408.

4. Venue is proper in this Court pursuant to 28 U.S.C. §§ 1391 and 1396 because Pearson resides and does business in Birmingham, Alabama, within this judicial district; the events giving rise to this claim occurred within this judicial district; and a substantial number of Pearson's customers who filed false and fraudulent returns reside within this judicial district.

Defendant

5. Pearson is a paid tax return preparer who resides in Birmingham, Alabama.

6. Pearson received tax return preparation training from taking classes at H&R Block and Jackson Hewitt.

7. Pearson also receives income tax return preparation training from the Drake software that she uses to prepare tax returns, which is where she learns about yearly changes to the federal income tax laws.

Summary of Pearson's Activities

8. Since 2008, Pearson has operated a sole proprietorship whose principal business is preparing federal income tax returns.

9. Pearson has utilized three names for this business, each assigned a different Employer Identification Number: LGS Tax Service, Positive Endeavors LLC, and AGA Tax Service.

10. Pearson is currently operating her business under the name AGA Tax Service.

11. Pearson employs three individuals in her business and has represented to the Internal Revenue Service ("IRS") that none of those individuals prepares tax returns.

12. IRS records show that Pearson prepared approximately 168 returns for the 2008 tax year, 441 returns for the 2009 tax year, 556 returns for the 2010 tax year and 764 returns for the 2011 tax year, or a total of almost 2,000 returns for the 2008 through 2011 tax years.

Description of Fraudulent Return Preparation Schemes

13. Since 2008, Pearson has repeatedly and continually improperly claimed a credit under 26 U.S.C. § 32, *i.e.*, the Earned Income Tax Credit (“EITC”), on her clients’ returns to generate large and erroneous refunds for her clients. The EITC is a refundable credit, which means that it can generate a refund exceeding the amount of income tax paid by an individual taxpayer. The false or overstated EITC claims reported by Pearson on her clients’ returns generate corresponding decreases in tax liability or increases in refunds, regardless of whether the individual client paid any taxes during the year.

14. The amount of the EITC that a taxpayer may claim increases in proportion to a taxpayer’s wages or other earned income up to a certain dollar amount. As such, there is a “plateau” of earned income amounts that will result in the maximum possible EITC a taxpayer may claim. Because that “plateau” amount may be more than the income the taxpayer actually earned, a return falsely overstating income will, in certain circumstances, generate a larger refund.

15. The amount of the EITC that a taxpayer may claim increases for each “qualifying child” claimed by the taxpayer, up to three children.

16. A taxpayer may claim an individual as a “qualifying child” if that individual meets the following requirements:

(a) is related to the taxpayer as one of the following: son, daughter, stepchild, foster child, brother, sister, stepbrother, stepsister, or a descendent of any of them; and

(b) is under the age of 19 at the end of the tax year, or under the age of 24 and a student at the end of the year, or is permanently and totally disabled; and

(c) shares the principal place of abode with the taxpayer for more than one half of the year; and

(d) has not filed a joint federal income return for that tax year. *See* 26 U.S.C. §§ 32(c)(3), 152(c).

17. Pearson inflates her clients’ EITC claims by reporting fraudulent income and/or by improperly claiming individuals as a “qualifying child” on her clients’ returns.

18. Pearson has employed several schemes to fraudulently increase her clients’ EITC claims. Ten client files provided by Pearson to the IRS in May 2011 show that Pearson has inflated her clients’ income or improperly claimed a

“qualifying child” on her clients’ returns to increase her clients’ EITC claims by using the following schemes:

(a) One client file contained a false W-2 statement, which listed an EIN that did not match the employer named on the W-2.

(b) Three of the client files contained Forms W-3, Transmittal of Wage and Tax Statements, reporting wages as “household help” in amounts appearing on the return. In each case, the W-3 reported that the taxpayer was the employer issuing the W-3 to himself or herself. All three clients’ EITC claims were increased as a result of including the income on the false W-3.

(c) Five client files contained returns with questionable Schedules C, which lists a taxpayer’s profit and loss from a business, that listed gross receipts but no expenses.

(d) Three files contained “Information Sheet” or “Additional Questions” worksheets, apparently signed by the taxpayer, that identified the taxpayer’s mother as a dependent. The returns prepared by Pearson for those clients and filed with the IRS listed the mother as a disabled “sister” and claimed the mother as a “qualifying child” to inflate the EITC claims on those returns.

19. Further evidence of Pearson’s continual and repeated preparation of returns that claim fraudulent or overstated EITCs includes the following:

(a) For the 2008 tax year, 97 % of the returns prepared by Pearson claimed a refund, and 92% of those returns claimed the Earned Income Tax Credit.

(b) For the tax years 2009 through 2011, 99% of the returns prepared by Pearson claimed a refund, and over 92% of those returns claimed the Earned Income Tax Credit.

(c) Of the returns prepared by Pearson for the 2011 tax year, 53 % of her clients claimed that they were related to, and provided a home for, disabled qualifying children. Research received from the IRS' Wage and Investment Research Group indicates that the average percentage of disabled qualifying children in paid-preparer client returns is a mathematical mean of 7.3% and a median of 3.6%.

20. Pearson knew or should have known that the positions taken on the returns, including positions with respect to disabled qualifying children and unsubstantiated claims of income, were not reasonable.

Pearson's Failure to Comply with Due Diligence Requirements

21. Pearson has also repeatedly and continually failed to comply with the due diligence requirements set forth in 26 U.S.C. § 6695(g) for determining eligibility and amount of these EITCs.

22. Section 6695(g) of the Internal Revenue Code provides for the imposition of a penalty against a return preparer who fails to exercise due diligence in determining a taxpayer's eligibility for the EITC.

23. The due diligence a preparer must undertake, as set forth in 26 C.F.R. §1.6695-2(b), includes, *inter alia*, the duty to make reasonable inquiries if the information provided by the taxpayer appears to be incorrect, incomplete, or inconsistent, as well as a duty to contemporaneously document the inquiries made and the responses to these inquiries.

24. In 2010, the IRS conducted an investigation of Pearson for returns she prepared for the 2008 tax year to determine whether the due diligence requirements were being met with respect to (1) the eligibility of taxpayers to claim the EITC on the returns she prepared and (2) whether the amount of EITC claimed on the returns she prepared was correct.

25. During that investigation the IRS reviewed 144 returns prepared by Pearson and determined that 64 of those returns failed to meet the due diligence requirements of 26 U.S.C. § 6695(g), resulting in a penalty of \$6,400.00. The IRS also asserted penalties for the 108 requested returns that were not available, resulting in additional penalties of \$10,800.

26. At a subsequent managerial conference, held on May 26, 2010, Pearson produced 82 additional files. As a result, 53 of the penalties were

eliminated, and \$5,300 of the assessment was reversed. There remained, however, an assessed balance of \$11,900.

27. Pearson paid \$7,421 in penalties on March 21, 2011, leaving an unpaid balance of \$4,479.

28. On March 4, 2011, the IRS again contacted Pearson to determine if she was in compliance with the due diligence requirements set forth in 26 U.S.C. § 6695(g). At that time, the IRS requested 10 client files at random.

29. The files produced by Pearson to the IRS in May 2011 show that, despite being penalized for failing to comply with due diligence requirements in 2010, Pearson is continuing to fail to comply with the due diligence requirements under 26 U.S.C. § 6695(g). Pearson's failure to comply with the due diligence requirements is evidenced by the following:

(a) Of the ten files reviewed by the IRS, nine files included EITC claims relating to qualifying children who did not bear the relationship of son or daughter to the taxpayer. There was no documentation in the file to prove the listed relationship or any evidence that Pearson made any attempt to verify that these alleged dependents were qualifying children.

(b) Eight of files reviewed by the IRS included EITC claims relating to a qualifying child that was either a student or disabled. Seven of the eight files contained no evidence indicating that the alleged qualifying child was

disabled or a full-time student during the tax year. Also, there was no evidence that Pearson made any attempt to verify that the alleged qualifying child was a full time student or disabled other than an “Additional Questions” worksheet that was completed with “yes” or “no” answers to questions.

(c) Four of the files reviewed contained “Additional Question” or “Information Sheet” worksheets in which the responses conflicted with the filed returns.

(d) Five of the files reviewed included a return with a Schedule C that reported gross receipts but no expenses. There was no evidence in those files indicating how the figures on the Schedule C were calculated. Had expenses been reported, the amount of the claimed EITC would have been lower.

(e) Three of the files reviewed contained Forms W-3, Transmittal of Wage and Tax Statements, reporting wages as “household help” in amounts appearing on the return. In each case, the W-3 reported that the taxpayer was the employer issuing the W-3 to himself or herself.

30. Some of the returns in the client files produced by Pearson in May 2011 had white-out over certain information printed in the original return with apparently different information hand-written on the white-out. Information on the returns covered by white-out includes the date the return was prepared and the relationship of certain dependents. It appears that Pearson was attempting to alter

the client returns in her files *post facto* so that the information in those returns would match the information in the files that were being provided to the IRS.

Harm to the United States

31. Pearson has caused substantial revenue losses to the United States.

32. As of May 25, 2011, audits conducted of Pearson's returns reporting an EITC claim resulted in adjustments in 99% of the examined returns. These adjustments total \$1,373,814, or approximately \$4,689 per return.

33. Spread over the 1,781 returns with EITC claims that Pearson prepared during the 2008-2011 filing seasons, the IRS estimates the harm to the United States from Pearson's misconduct to be as high as \$8.3 million.

COUNT I:
INJUNCTION UNDER 26 U.S.C. §7407
FOR CONDUCT SUBJECT TO PENALTY UNDER 26 U.S.C. §§ 6694 AND
6695

34. The United States incorporates by reference the allegations in paragraphs 1 through 33.

35. Section 7407 of the Internal Revenue Code authorizes a district court to enjoin a person who is a tax return preparer from engaging in certain prohibited conduct or from further acting as a tax return preparer. The prohibited conduct justifying an injunction includes, *inter alia*, the following:

(a) engaging in conduct subject to penalty under 26 U.S.C. § 6694, which penalizes a tax return preparer who prepares a return that contains an understatement of tax liability or an overstatement of a refund due to an unreasonable position that the return preparer knew or should have known was unreasonable;

(b) engaging in conduct subject to penalty under 26 U.S.C. § 6695(g), which penalizes a tax return preparer for failing to exercise due diligence in determining eligibility for the EITC; and

(c) engaging in any other fraudulent or deceptive conduct which substantially interferes with the proper administrations of the Internal Revenue laws.

36. In order for a court to issue such an injunction, the court must find that:

(a) the tax return preparer engaged in the prohibited conduct, and
(b) injunctive relief is appropriate to prevent the recurrence of such conduct.

37. If a tax return preparer's conduct is continual or repeated and the court finds that a narrower injunction would not be sufficient to prevent the preparer's interference with the proper administration of the internal revenue laws, the court

may enjoin the person from acting as a tax return preparer. *See* 26 U.S.C. § 7407(b).

38. Pearson has continually and repeatedly engaged in conduct subject to penalty under 26 U.S.C. § 6694 by preparing returns that understate her clients' tax liabilities and overstate their refunds based on unreasonable and reckless positions.

39. Pearson has continually and repeatedly engaged in conduct subject to penalty under 26 U.S.C. § 6695 by failing to exercise due diligence in determining her clients' eligibility for the EITC. Even after the IRS imposed over \$11,000 in penalties against Pearson for this conduct, she continues to claim the EITC on the returns she prepares for her clients without exercising due diligence.

40. Pearson has continually and repeatedly engaged in conduct that violates 26 U.S.C. §§ 6694 and 6695 and which substantially interferes with the administration of the internal revenue laws.

41. Injunctive relief is necessary to prevent this misconduct because, absent an injunction, Pearson is likely to continue preparing false federal income tax returns.

42. A narrower injunction would be insufficient to prevent Pearson's interference with the administration of the federal tax laws. Pearson's continued preparation of returns claiming false EITCs through the use of multiple schemes, and continued failure to comply with the due diligence requirements even after the

imposition of penalties and the knowledge that the IRS would be monitoring her compliance, demonstrate the necessity of enjoining her from preparing returns.

43. Only a permanent injunction is sufficient to prevent future harm. If Pearson is not permanently enjoined from preparing tax returns, the IRS will be required to spend additional scarce and unrecoverable resources to investigate and analyze returns she prepares in the future. In addition the IRS will be harmed through the loss of revenues resulting from bogus and fraudulent refunds being claimed on returns prepared by Pearson.

COUNT II:
INJUNCTION UNDER 26 U.S.C. §7408
FOR CONDUCT SUBJECT TO PENALTY UNDER 26 U.S.C. § 6701

44. The United States incorporates by reference the allegations contained in paragraphs 1 through 43.

45. Section 7408 of the Internal Revenue Code authorizes a district court to enjoin any person from engaging in conduct subject to penalty under 26 U.S.C. § 6701, which penalizes a person who aids or assists in the preparation of tax returns that the person knows will result in an understatement of tax liability.

46. Pearson has engaged in conduct subject to penalty under 26 U.S.C. § 6701 by preparing or directing the preparation of income tax returns that claim an EITC when she knows or should reasonably know that her clients are not eligible for the credit, or the credit in the full amount claimed.

47. Pearson's actions described in paragraphs 8-20, above, fall within 26 U.S.C. § 7408(c)(1), and injunctive relief is appropriate to prevent recurrence of this conduct.

48. Accordingly, Pearson should be permanently enjoined from preparing any returns that improperly claim or inflate a claim to the EITC.

COUNT III:
INJUNCTION UNDER 26 U.S.C. §7402 FOR UNLAWFUL
INTERFERENCE WITH THE ENFORCEMENT OF INTERNAL REVENUE
LAWS

49. The United States incorporates by reference the allegations contained in paragraphs 1 through 48.

50. Section 7402(a) of the Internal Revenue Code authorizes a court to issue orders of injunction as may be necessary or appropriate for the enforcement of internal revenue laws.

51. Pearson has repeatedly and continually engaged in conduct that interferes substantially with the administration and enforcement of internal revenue laws.

52. If Pearson continues to act as a tax return preparer, her conduct will result in irreparable harm to the United States, and the United States has no adequate remedy at law.

53. Pearson's conduct has caused and will continue to cause substantial tax losses to the United States Treasury, much of which may be undiscovered and unrecoverable. Moreover unless Pearson is enjoined from preparing returns, the IRS will have to devote substantial and unrecoverable time and resources auditing her clients individually to detect false, fraudulent, or overstated refund claims in future returns.

54. The detection and audit of erroneous EITC refund claimed filed by Pearson's clients will be a significant burden on IRS resources.

WHEREFORE, the plaintiff, United States of America, respectfully prays for the following:

A. That the Court find that Lakeisha Pearson has repeatedly and continually engaged in conduct subject to penalty under 26 U.S.C. §§ 6694 and 6695 and that injunctive relief is appropriate under 26 U.S.C. § 7407 to prevent recurrence of that conduct.

B. That the Court find that Lakeisha Pearson has repeatedly and continually engaged in conduct subject to penalty under 26 U.S.C. § 6701 and that injunctive relief is appropriate under 26 U.S.C. § 7408 to prevent recurrence of that conduct.

C. That the Court find that Lakeisha Pearson has repeatedly and continually engaged in conduct that substantially interferes with the proper

enforcement and administration of the internal revenue laws, and that injunctive relief against Pearson is appropriate to prevent the recurrence of that conduct pursuant to 26 U.S.C. § 7402(A).

D. That the Court enter a permanent injunction prohibiting Lakeisha Pearson or any other person working in concert or participation with her from directly or indirectly:

1. preparing federal income tax returns, amended returns, or other tax-related documents and forms, including any electronically-submitted tax returns or tax related documents, for any entity or person other than herself;
2. assisting in the preparation of federal tax returns and amended returns;
3. understating taxpayers' liability as prohibited by 26 U.S.C. § 6694;
4. engaging in other activity subject to penalty under 26 U.S.C. §§ 6694, 6695(g), 6700, and 6701;
5. engaging in any activity subject to penalty under 26 U.S.C. § 6695, including failing to supply a list of clients or provide copies of clients' tax returns to the Service on request; and
6. engaging in conduct that substantially interferes with the proper administration and enforcement of the tax laws.

E. That the Court enter an injunction requiring Pearson:

1. At her own expense, to send by certified mail, return receipt requested, a copy of the final injunction entered against her in this action, as well as a copy of the Complaint setting forth the allegations as to how Pearson fraudulently prepared federal income tax returns, to each person for whom she prepared federal income tax returns or any other federal tax forms after January 1, 2008;

2. to turn over to the United States copies of all returns or claims for refund that she prepared for clients after January 1, 2008;

3. to turn over to the United States a list with the name, address, telephone number, email address, and social security number or other taxpayer identification number of all customers for whom she prepared returns after January 1, 2008;

4. within forty-five (45) days of entry of the final injunction in this action, to file a sworn statement with the Court evidencing her compliance with the foregoing directives; and

5. to keep records of her compliance with the foregoing directives, which may be produced to the Court, if requested, or the United States pursuant to paragraph F, below.

F. That the Court enter an order allowing the United States to monitor Pearson's compliance with the injunction, and to engage in post-judgment discovery in accordance with the Federal Rules of Civil Procedure; and

G. That the Court grant the United States such other and further relief as the Court deems appropriate

Dated: August 3, 2011

Respectfully submitted,

JOHN A. DICICCO
Principal Deputy Assistant Attorney
General

/s/ Michelle Abrams Levin
MICHELLE ABROMS LEVIN
D.C. Bar No. 494961
Attorney for Plaintiff
Trial Attorney, Tax Division
U.S. Department of Justice
Post Office Box 14198
Ben Franklin Station
Washington, D.C. 20044
Telephone: (202) 353-1758
Facsimile: (202) 514-9868
michelle.a.levin@usdoj.gov

Of counsel:

Joyce White Vance
United States Attorney