

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW JERSEY
NEWARK DIVISION

UNITED STATES OF AMERICA,)	
)	
Plaintiff,)	
)	
v.)	Civil No.
)	
CARMEN GONZALEZ, d/b/a CARMEN)	
TAX SERVICES,)	
)	
Defendant.)	

COMPLAINT FOR PERMANENT INJUNCTION AND OTHER RELIEF

Plaintiff, the United States of America, alleges against Defendant, Carmen Gonzalez, individually and doing business as Carmen Tax Services, as follows:

1. This is a civil action brought by the United States under §§ 7402(a), 7407, and 7408 of the Internal Revenue Code (26 U.S.C.) (“I.R.C.”) (“Code”) to enjoin Defendant, Carmen Gonzalez, and anyone in active concert or participation with her, from directly or indirectly:

- (a) acting as a federal tax return preparer or requesting, assisting in, or directing the preparation or filing of federal tax returns, amended returns, or other related documents or forms for any person or entity other than herself;
- (b) engaging in any activity subject to penalty under 26 U.S.C. § 6695, including § 6695(g), which penalizes preparers who claim the Earned Income Tax Credit (EITC) for their customers without first complying with the due diligence requirements imposed by Treasury regulations;
- (c) engaging in any other activity subject to penalty under I.R.C. §§ 6694, 6701, or

any other penalty provision in the I.R.C.; and

- (d) engaging in any conduct that substantially interferes with the proper administration and enforcement of the internal revenue laws.

Jurisdiction and Venue

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, pursuant to the provisions of I.R.C. §§ 7402, 7407, and 7408.

3. This Court has jurisdiction under 28 U.S.C. §§ 1340 and 1345 and I.R.C. §§ 7402(a), 7407, and 7408.

4. Venue is proper in this Court under 28 U.S.C. § 1391(b) because a substantial part of the events giving rise to this suit occurred in this judicial district.

Defendant's Activities

5. Gonzalez is a commercial tax return preparer doing business under the name "Carmen Tax Services" (CTS). Gonzalez is not a CPA, nor does she hold any other professional licenses.

6. Gonzalez resides in Allentown, Pennsylvania, and operates her business out of an office located at 253 Livingston Avenue, New Brunswick, New Jersey 08901.

7. Since 1990, Gonzalez has operated CTS for the purpose of preparing federal and state income tax returns. Gonzalez advertises CTS as a limited liability company (LLC), but there are no corporate filings on record with the New Jersey Secretary of State to support that claim.

8. According to Gonzalez, she is the only person at CTS who prepares tax returns. However, she employs two individuals to assist her with clerical work during filing season.

9. Gonzalez charges return preparation fees ranging from \$125 to \$190, and the returns

prepared by Gonzalez list “Carmen Gonzalez Income Tax” as the paid preparer.

10. The table below shows the number of returns prepared by Gonzalez between 2006 and 2009 and the number of those returns claiming a refund and/or the EITC:

Tax Year	Return Type	# of Returns	# of Refund Returns	# of EITC Returns	% of Refund Returns	% of EITC Returns
2006	1040	589	517	263	88%	45%
2007	1040	625	535	255	86%	41%
2008	1040	650	555	256	85%	39%
2009	1040	717	631	343	88%	48%

11. As the table shows, Gonzalez prepared at least 589 returns in 2007, 625 in 2008, 650 in 2009, and 717 in 2010, with a high refund rate ranging between 85 and 88 percent each year. In addition, between 39 and 48 percent of those returns included a claim for the EITC.

12. The IRS has audited 30 returns claiming the EITC that Gonzalez prepared for tax years 2006, 2007, 2008 and 2009. Of those 30 returns, 27 resulted in the IRS reducing or disallowing the amount claimed, a more than 90% disallowance rate, resulting in adjustments totaling \$110,784, or \$3,693 per return on average.

13. The EITC is a refundable tax credit available to certain low-income individuals. The amount of the credit is based on the taxpayer’s income, filing status, and claimed number of dependents. The requirements for claiming the EITC are located in 26 U.S.C. § 32.

14. Because the EITC is a refundable credit, claiming an EITC can reduce a taxpayer’s federal tax liability below zero, entitling the taxpayer to a refund from the U.S. Treasury.

15. Due to the method used to calculate the EITC, an individual can claim a larger EITC

by claiming multiple dependants and, for certain income ranges, individuals with higher annual incomes are entitled to a larger credit than those with lower annual incomes.

16. Unscrupulous tax return preparers like Gonzalez exploit the rules by claiming on their customers' returns bogus dependants and/or by minting phony Schedule C businesses.

17. Because of the potential for abuse in claiming the EITC, Congress has authorized the Secretary of the Treasury to impose "due diligence" requirements on federal income tax return preparers claiming the EITC for their customers. These "due diligence" requirements obligate the tax return preparer to make "reasonable inquiries" to ensure the customer is legitimately entitled to the EITC. The tax return preparer may not "ignore the implications of information furnished to, or known by, the tax return preparer, and must make reasonable inquiries if the information furnished to the tax return preparer appears to be incorrect, inconsistent, or incomplete." *See* 26 C.F.R. § 1.6695-2 (2010). Tax return preparers must also document their compliance with these requirements and keep that documentation for three years. *Id.*

18. To document compliance with the due diligence requirements, tax return preparers must complete either the "Paid Preparer's Earned Income Credit Checklist" (Form 8867) or record and maintain other documentation verifying customer eligibility for the EITC.

19. In 2006, the IRS audited 100 federal tax returns prepared by Gonzalez which claimed the EITC. Gonzalez failed to satisfy the due diligence requirements on all 100 of those tax returns by neglecting to complete any Forms 8867 and/or by failing to maintain other documentation to verify the customers' eligibility for the EITC (i.e. proof of dependants, Schedule C income, and head of household status).

20. Examples of Gonzalez's failure to comply with the due diligence requirements included: files containing claims of foster children with no supporting documentation; numerous questionable head of household claims; and a large number of suspicious Schedule C businesses listing no expenses, but conveniently claiming the exact amount of gross receipts necessary to maximize the customers' EITC.

21. After its 2006 investigation, the IRS assessed \$10,000 in penalties against Gonzalez for her 100 separate violations of 26 U.S.C. § 6695(g). Gonzalez agreed to the penalties and paid them in full on February 21, 2007.

22. In 2010, the IRS contacted Gonzalez and requested 10 random customer files to determine whether she was in compliance with the due diligence requirements with respect to preparing income tax returns claiming the EITC. The government's review of these customer files revealed that Gonzalez was not only failing to comply with the due diligence requirements, but was also fraudulently claiming the EITC.

23. On June 23, 2010, Gonzalez told the IRS that if her customer does not have any documentation, she takes her customer's word alone as proof regarding EITC residency and relationship requirements. Gonzalez also said that when creating Schedule Cs, if a customer does not have a copy of a Form 1099 for "Miscellaneous Income" (1099-MISC), she merely takes the customer's word regarding the amount of money the customer earned, and she does not ask the customer about any business expenses they might have incurred.

24. After the 2006 investigation, Gonzalez began filling out and maintaining Forms 8867 in some customers' files. Gonzalez also created two separate forms: one which purports to verify the customer's head of household filing status ("head of household verification worksheet") and

the other which purports to substantiate the customer's earned income ("earned income verification worksheet"). However, a review of the implementation of these worksheets reveals that, at best, Gonzalez is making only a superficial attempt to comply with the due diligence requirements. Gonzalez fills out these forms in an identical manner for each of her customers, revealing that the only purpose behind the forms is to make it appear as though she is fulfilling the due diligence requirements and to avoid further penalties.

25. The 10 customer files reviewed in 2010 revealed various examples of Gonzalez's failure to adhere to the due diligence requirements and/or demonstrate Gonzalez's willingness to falsify information and documents in order to maximize the EITC for customers:

- i. Of the ten returns, five include claims for the EITC based on purported qualifying children who were neither the son nor daughter of the taxpayer (e.g., nephew, niece, brother, sister, etc.). Although these individuals could potentially qualify as dependants supporting an EITC claim, there is no documentation in the files to prove the listed relationship or to show that Gonzalez made a sincere inquiry to verify that these alleged dependants were qualifying children for the purposes of the EITC. More importantly, without claiming those dependants, customers would have had a lower EITC, or in some cases, not have qualified for the EITC at all.
- ii. Seven of the ten tax returns include a Schedule C reporting gross receipts, but no expenses. Other than 1099s-MISC found in only four of those files, there is no evidence to show how Gonzalez ascertained or calculated the gross income figures on the Schedule Cs. For six of those seven returns,

the reported Schedule C income resulted in the maximum EITC for the taxpayer. Had any expenses been reported on any of those six Schedule Cs, the amount of the EITC would have been reduced.

- iii. Eight of the ten customers' files include a head of household verification worksheet, a document created and filled out by Gonzalez. For each of these customers, Gonzalez filled out the form in an identical manner, providing the same responses for each of the questions. For all 8 of these customers, Gonzalez reported that they were "Never married,"¹ and to substantiate that her customers contributed to half the cost of maintaining the home (a head household filing requirement), Gonzalez checked the same four (out of six) boxes indicating she reviewed: (1) Utility bills, (2) Grocery receipts, (3) Rent receipts or mortgage interest statement, and (4) Other household bills. The IRS recently disallowed the head of household status for one of those customers because she could not show that she paid more than fifty percent of the household's expenses.
- iv. Only five of the ten customer files contained an earned income verification worksheet. The worksheet purports to substantiate customers' earned income and serves to document Gonzalez's purported effort to verify the ostensible existence of a Schedule C business. On each of these forms,

¹This defies statistical probabilities. According to U.S. Census data, the percentage of individuals in the United States over the age of 15 who have never been married is only 30.8%. Here, 100% of the eight individuals selected at random who claimed head of household status claimed they were never married.

Gonzalez checked the same three boxes (out of six) indicating she examined (1) Business cards, (2) Receipts or receipt book (with company header), and (3) Advertisements (newspaper, flyer, yellow pages, etc.).

Yet, none of the files contain copies of any of these records.

- v. In response to the question on the earned income verification worksheet that asked “Were satisfactory records of income and expense provided?” Gonzalez responded, “Yes.” Gonzalez then checked the same four boxes (out of seven) to indicate she personally examined (1) Accounting records, (2) Paid Invoices/receipts, (3) Car/truck expenses, and (4) Business bank accounts to verify business income and/or expenses. Yet, none of the files contain copies of any of these records, nor anything to suggest that customers actually provided Gonzalez with any of these records. Furthermore, Gonzalez failed to report any expenses on any of the Schedule Cs she prepared for her customers.

- vi. Gonzalez told the IRS that she does not ask customers who lack 1099s-MISC about business expenses. Yet, for two customers who lacked 1099s-MISC, Gonzalez filled out earned income verification worksheets in which she claimed to have reviewed “(1) Accounting records, (2) Paid Invoices/receipts, (3) Car/truck expenses, and (4) Business bank accounts.” One of those customers was Elizabeth Marrero. Gonzalez prepared a 2009 federal income tax return for Marrero. The 1040 prepared by Gonzalez showed wages of \$7,965 from a W-2 (not in the file) and

\$6,000 in business income. The attached Schedule C lists \$6,000 of purported income from babysitting, with no expenses. Gonzalez also prepared an earned income verification worksheet in the manner referenced above, claiming to review business cards, receipts, advertisements, accounting records, paid invoices, car/truck expenses, and business bank accounts to substantiate the “babysitting” business. None of these documents was in the file. Gonzalez also checked a box indicating that the taxpayer had a 1099-MISC to support the income, but that form is not in the file. Thus, it appears that this customer never had a 1099-MISC and Gonzalez only created the Schedule C and the earned income verification worksheet to create a phony paper trail to fraudulently claim the EITC.

26. In sum, the income verification worksheet created by Gonzalez serves no purpose other than to make it appear as though she is complying with the due diligence requirements. Gonzalez fills out the sheet in a way that verifies eligibility for the EITC without regard to the veracity of the answers.

27. Given these facts, Gonzalez created Schedule Cs showing income that was likely never earned and claiming no expenses so that she could claim her customers had the requisite amount of income to claim the maximum EITC. Gonzalez then fabricated the head of household and earned income verification worksheets to make it appear as though she was satisfying the due diligence requirements and to thwart future IRS due diligence investigations.

28. Gonzalez is failing to adhere to the EITC due diligence requirements, and even worse, Gonzalez is falsifying information to achieve the maximum allowed EITC for her customers and fabricating documents to deceive the IRS.

29. As stated previously, because of the way the EITC is calculated, claiming more income, up to a certain point, allows customers to receive a larger refundable credit. Conveniently, in 9 of the 10 returns examined, the Schedule C income Gonzalez claimed on customers' returns allowed the customers to maximize the EITC. Also, despite customers claiming to own businesses that would clearly have operating expenses (i.e. construction, cleaning business), none of their Schedule Cs claimed expenses (expenses would offset income and lower the EITC).

30. One example clearly demonstrates Gonzalez's willingness to falsify information in order to maximize her customers' EITC. Gonzalez prepared a 2009 federal tax return for Maria F. Taveras Gonzalez. Ms. Taveras Gonzalez's file contained a 1099-MISC issued by CTS showing nonemployee compensation of \$6,500. Ms. Taveras Gonzalez also had a W-2 showing \$10,315.82 in wages. The 1040 should have reported \$16,816 in earned income. Instead, Gonzalez prepared a Schedule C for Ms. Taveras Gonzalez reporting only \$4,500 in gross receipts (clearly erroneous given the nonemployee compensation of \$6,500). Since Gonzalez's own company, CTS, prepared the 1099-MISC, Gonzalez knew, or should have known, the actual amount Taveras Gonzalez received in nonemployee compensation. By under-reporting the income, though, Gonzalez claimed the maximum EITC on Ms. Taveras Gonzalez's 1040.²

²For 2009, earned income between \$12,570 and \$16,420 for a taxpayer with 2 dependents resulted in the maximum EITC of \$5,028, which is what Ms. Taveras Gonzalez claimed on her 1040. For taxpayers with earned income levels greater than \$16,420, the amount of the EITC is

31. Congress imposed due diligence requirements on tax preparers to ensure they take measures to verify a customer's eligibility for the EITC. This requires, at a minimum, verifying head of household status, obtaining documentation regarding dependency status, and verifying the existence of Schedule C businesses, none of which Gonzalez has done.

32. Not only does Gonzalez fail to adhere to the due diligence requirements, but she is falsifying information in order to maximize the EITC for her customers.

33. Gonzalez's actions, and more importantly, her inactions, show an intentional disregard for the due diligence requirements under I.R.C. § 6695(g) and demonstrate her unwillingness to ever comply with the requirements.

Harm Caused by Gonzalez

34. Gonzalez's customers have been harmed because they paid her fees and relied on her to prepare proper tax returns. Instead, Gonzalez prepared returns that substantially understated their correct tax liabilities. As a result, many of them now face large income tax deficiencies and may be liable for sizeable penalties and interest.

35. Gonzalez's conduct harms the United States because her customers are under-reporting their correct tax liabilities and in many cases receiving unwarranted refunds, thereby diminishing tax revenues.

36. In addition to the direct harm caused by preparing tax returns that understate customers' tax liabilities, Gonzalez's activities undermine public confidence in the administration of the federal tax system and encourage noncompliance with tax laws.

gradually phased out using a formula that reduces the EITC proportionate to higher levels of income. Had Ms. Taveras Gonzalez reported the full amount of her nonemployee compensation, or the additional \$2,000, she would have had a lower EITC.

37. Gonzalez further harms the United States because the IRS must devote its limited resources to investigating Gonzalez, identifying her customers, ascertaining her customers' correct tax liabilities, recovering any refunds erroneously issued, and collecting any additional taxes and penalties.

Count I
Injunction Under § 7407 for Conduct
Subject to Penalty Under §§ 6694(b) and 6695(g)

38. Plaintiff incorporates by reference the allegations in paragraphs 1 through 37.

39. The Internal Revenue Code (Code) authorizes the United States to seek an injunction against any tax preparer who, among other things, has engaged in any conduct subject to penalty under §§ 6694 or 6695. 26 U.S.C. § 7407.

40. If a tax return preparer's conduct is continual and/or repeated and the court finds that a narrower injunction (*i.e.*, prohibiting specific enumerated conduct) would not be sufficient to prevent the preparer's interference with the proper administration of federal tax laws, the court may enjoin the person from acting as a return preparer.

41. Section 6694(b) of the Code penalizes a tax return preparer who prepares a return or claim for refund with respect to which any part of an understatement of liability is due to

- a. a willful attempt to understate the liability for tax on the return or claim or
- b. a reckless or intentional disregard of rules or regulations.

42. The Treasury regulations promulgated under Section 6695(g) of the Code, prohibit a return preparer from claiming the EITC without first conducting proper due diligence and documenting his or her compliance with the due diligence requirements. *See* 26 C.F.R. § 1.6995-2 (2010).

43. Gonzalez's failure to comply with the due diligence requirements for the EITC violates Treasury Regulations and her willingness to falsify information to obtain the EITC for her customers shows a reckless and/or intentional disregard of the IRS rules and regulations.

44. Gonzalez has continually and repeatedly prepared federal income tax returns that claim EITCs for which Gonzalez has not conducted, let alone, documented the required due diligence procedures.

45. Even after the IRS assessed \$10,000 in penalties against Gonzalez for conduct subject to penalty under § 6695(g) in 2006, Gonzalez continued to claim EITCs for customers on 2007, 2008 and 2009 returns (prepared during 2008, 2009 and 2010, respectively) for which she failed to conduct or document the required due diligence procedures.

46. Injunctive relief under 26 U.S.C. § 7407 is necessary to prevent this misconduct because, absent an injunction, Gonzalez is likely to continue preparing federal income tax returns for customers that understate their federal tax liabilities and enable them to receive greater refunds than what they are legally entitled.

47. Gonzalez should be permanently enjoined under 26 U.S.C. § 7407 from acting as a tax return preparer because a more limited injunction would be insufficient to stop her repeated interference with the proper administration of the tax laws.

Count II
Injunction under I.R.C. § 7408 for Conduct
Subject to Penalty Under § 6701

48. Plaintiff incorporates by reference the allegations in paragraphs 1 through 47.

49. Section 7408 of the Code authorizes a district court to enjoin any person from engaging in conduct subject to penalty under I.R.C. § 6701 if injunctive relief is appropriate to prevent recurrence of such conduct.

50. Section 6701(a) of the Code penalizes any person who aids or assists in, procures, or advises with respect to the preparation or presentation of a federal tax return, refund claim, or other document knowing (or having reason to believe) that it will be used in connection with any material matter arising under the internal revenue laws and knowing that if it is so used it will result in an understatement of another person's tax liability.

51. If not enjoined, Gonzalez will likely continue to prepare bogus Schedule Cs as a means of maximizing the EITC for her customers. This, coupled with Gonzalez's unwillingness to comply with the EITC due diligence requirements, will continue to result in her customers receiving unwarranted or improperly inflated refunds.

52. Gonzalez has not altered her behavior despite already being assessed penalties for similar conduct. Injunctive relief is appropriate under I.R.C. § 7408 because Gonzalez will likely continue to engage in conduct subject to penalty under I.R.C. § 6701.

Count III
Injunction under I.R.C. § 7402(a)
Necessary to Enforce the Internal Revenue Laws

53. Plaintiff hereby incorporates by reference the allegations in paragraphs 1 through 52.

54. Section 7402 of the Code authorizes a district court to issue orders of injunction as may be necessary or appropriate for the enforcement of the internal revenue laws.

55. Gonzalez, through the actions described above, has engaged in conduct that substantially interferes with the enforcement of the internal revenue laws.

56. Unless enjoined, Gonzalez is likely to continue to engage in such improper conduct and interfere with the enforcement of the internal revenue laws. If Gonzalez is not enjoined from engaging in fraudulent and deceptive conduct, the United States will suffer harm by issuing unwarranted federal income tax refunds.

57. Enjoining Gonzalez is in the public interest because an injunction, backed by the Court's contempt powers if needed, will stop Gonzalez's illegal conduct and the harm it causes the United States and its citizens.

58. The Court should impose injunctive relief under 26 U.S.C. § 7402(a).

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

A. That the Court find that Carmen Gonzalez has continually and repeatedly engaged in conduct subject to penalty under I.R.C. §§ 6694 and 6695, and has continually and repeatedly engaged in other fraudulent or deceptive conduct that substantially interferes with the administration of the tax laws, and that a narrower injunction prohibiting only this specific misconduct would be insufficient;

B. That the Court, pursuant to I.R.C. § 7407, enter a permanent injunction prohibiting Carmen Gonzalez from acting as a federal tax return preparer;

C. That the Court find that Carmen Gonzalez has engaged in conduct subject to a penalty under I.R.C. § 6701, and that injunctive relief under I.R.C. § 7408 is appropriate to prevent a recurrence of that conduct;

D. That the Court find that Carmen Gonzalez has engaged in conduct that interferes with the enforcement of internal revenue laws, and that injunctive relief is appropriate to prevent the recurrence of that conduct pursuant to the Court's inherent equity powers and I.R.C. § 7402(a);

E. That the Court, pursuant to I.R.C. §§ 7402(a), 7407, and 7408, enter a permanent injunction prohibiting Carmen Gonzalez, and all those acting in concert with her, from:

- a. acting as a federal tax return preparer or requesting, assisting in, or directing the preparation or filing of federal tax returns, amended returns, or other related documents or forms for any person or entity other than herself;
- b. Engaging in any activity subject to penalty under 26 U.S.C. §§ 6694, 6701, or any other section of the Internal Revenue Code;
- c. Engaging in any activity subject to penalty under 26 U.S.C. § 6695, including § 6695(g), which penalizes claiming an Earned Income Tax Credit (EITC) for customers without complying with the due diligence requirements imposed by Treasury regulations;
- d. Engaging in other conduct that substantially interferes with the proper administration and enforcement of the internal revenue laws.

F. That the Court, pursuant to I.R.C. §§ 7402(a), 7407, and 7408, enter an order requiring Carmen Gonzalez to contact, within fifteen days of the Court's order, by United States mail and, if an e-mail address is known, by e-mail, all persons for whom she prepared federal tax returns or claims for a refund for tax years 2006 through 2009 to inform them of the permanent injunction entered against her;

G. That the Court, pursuant to I.R.C. §§ 7402(a), 7407, and 7408, enter an order requiring Carmen Gonzalez to produce to counsel for the United States, within fifteen days of the Court's order, a list that identifies by name, social security number, address, e-mail address, and

telephone number and tax period(s) all persons for whom she prepared federal tax returns or claims for a refund for tax years 2006 through 2009;

H. That the Court, pursuant to I.R.C. §§ 7402(a), 7407, and 7408, enter an injunction requiring Carmen Gonzalez to provide a copy of the Court's order to all of Carmen Tax Service's employees within fifteen days of the Court's order, and provide to counsel for the United States within 30 days a signed and dated acknowledgment of receipt of the Court's order for each person whom Gonzalez provided a copy of the Court's order;

I. That the Court retain jurisdiction over Carmen Gonzalez and over this action to enforce any permanent injunction entered against her;

J. That the United States be entitled to conduct discovery to monitor Gonzalez's compliance with the terms of any permanent injunction entered against her; and

K. That the Court grant the United States such other and further relief, including costs, as is just and reasonable.

DATED: February 7, 2011

Respectfully submitted,

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