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

UNITED STATES OF AMERICA Plaintiff, v. CHARLES G. KLINK 15723 Park House Drive, Unit No. 39 Fontana, California 92336 STEVEN BLOCK 14905 Landmark Drive Louisville, KY 40245 CALEB S. GRODSKY 1818 Pelham Avenue Los Angeles, CA 90025 Defendants.	)))))))))))))))))))	Civil No.

<u>COMPLAINT FOR PERMANENT INJUNCTION AND OTHER RELIEF</u>

Plaintiff, United States of America, for its complaint against defendants Charles G. Klink, Steven Block, and Caleb S. Grodsky states as follows:

Nature of the Action

1. Defendants promote and implement an intermediary transaction tax scheme in which they fraudulently effect the purchase of stock of closely-held companies belonging to their customers and the sale of those companies' assets in order to evade the payment of corporate income taxes. Defendants also help to establish and participate in a distressed asset trust (DAT) tax scheme as a means of concocting bogus losses that offset gains and facilitate the evading of corporate income taxes. Defendants have customers who are located throughout the United States.

2. The United States is bringing this complaint under 26 U.S.C. §§ 7402(a) and 7408 of the Internal Revenue Code (I.R.C.) to enjoin defendants and anyone acting in concert with them from directly or indirectly:

a. Organizing, promoting, marketing, or selling any plan or arrangement – including but not limited to the intermediary transaction tax scheme described in this complaint or any similar scheme– that advises or assists others in violating or attempting to violate the internal revenue laws or unlawfully evading the assessment or collection of their federal tax liabilities;

b. Engaging in conduct subject to penalty under I.R.C. § 6700, *i.e.*, organizing or selling any plan or arrangement and in connection therewith (a) making a gross valuation overstatement or (b) making or furnishing false or fraudulent statements regarding the allowability of certain deductions, the excludability of income, or the securing of tax benefits derived from participation in a plan or arrangement, when he knows and/or has reason to know the statements are false or fraudulent as to a material matter;

c. Engaging in conduct subject to penalty under I.R.C. § 6701, *i.e.*, preparing or assisting in the preparation of, or advising with respect to a document related to a matter material to the internal revenue laws that includes a position that he knows will, if used, result in an understatement of tax liability;

d. Engaging in conduct subject to penalty under I.R.C. § 6707(a), *i.e*., failing to file a return or statement with the IRS that identifies and describes any reportable or listed transaction, any potential tax benefits expected to result from that transaction, as well as other information required by statute;

e. Engaging in conduct subject to penalty under I.R.C. § 6708, *i.e.*, failing to furnish the IRS with a list that identifies all customers who have participated in a listed transaction when the IRS requests such a list and the list is required to be maintained pursuant to statute;

f. Engaging in any other conduct that interferes with the administration or enforcement of the internal revenue laws, including but not limited to implementing and participating in the intermediary transaction, DAD, DAT or any similar tax schemes using sham fees, sham entities and/or sham transactions.

3. An injunction is warranted based on defendants' conduct as promoters of the intermediary transaction tax scheme, which defendants have promoted since at least the late-1990s, and based on defendants' ongoing implementation and promotion of the intermediary transaction tax scheme and their implementation of and participation in the DAT tax scheme. Defendants' intermediary transaction tax scheme has caused substantial harm to the government. The Internal Revenue Service is harmed because it must continuously devote limited resources to detecting and examining inaccurate tax returns that defendants have caused numerous corporations to file as a function of the intermediary transaction and DAT tax shelters. As part of their intermediary transactions, defendants deplete these corporations of funds and render them insolvent so that they are unable to pay their income taxes. As a result, in many cases, the IRS is forced to devote its limited resources to the substantial efforts of collecting these unpaid taxes from other sources. Defendants have caused the target corporations they acquire to improperly deduct more than $112 million of distressed consumer receivables as bad debt on federal tax returns. The resulting amount of tax loss resulting from defendants' promotion of the

intermediary transaction tax schemes and bad debt write-downs is estimated to exceed $40 million.

Jurisdiction and Venue

4. Jurisdiction is conferred on this Court by 28 U.S.C. §§ 1340 and 1345, and by I.R.C. §7402(a).

5. This action for injunctive relief is brought at the request of 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 I.R.C. §§ 7402 and 7408.

6. Venue is proper in this Court under 28 U.S.C. § 1391 because a substantial part of the events giving rise to this suit took place in this district, including the promotion, execution and completion of at least one intermediary transaction, involving customers, real estate and a corporation all located within the Camden division of this district.

Introduction

7. For more than a decade, through an intricate web of trusts and corporations that they control, defendants have promoted an intermediary transaction tax scheme involving transactions that use disregarded conduit entities, have no economic substance, are sham transactions, and violate numerous provisions of the Internal Revenue Code. The intermediary transaction tax scheme is designed so that corporations illegally evade paying their corporate income taxes on the gains received from the sale of corporate assets. Defendants have promoted their intermediary transactions through Acquisitions Strategies International, Inc. (ASI), which Klink

and Block co-own and for whom Grodsky works as an associate counsel. Defendants also have promoted these transactions using other means.

8. To date, the IRS has learned that defendants promote their intermediary transaction scheme to individuals who own closely-held corporations and seek to sell their corporations' low-basis, high-value assets. Defendants advertise that their intermediary transaction scheme allows individuals, who own these corporations, to avoid paying corporate income taxes on the large capital gains that result when these corporations sell their low-basis, high-value assets.

9. In the intermediary transaction tax scheme, defendants, through intermediary companies that they control, purchase all of the stock of their customers' closely-held corporations (target corporations) either immediately before or immediately after those corporations sell their low-basis, high-value assets. After the assets are sold, each company is a shell corporation that only has a large amount of cash, sizeable corporate tax liabilities, but no other assets or means to conduct any business. Nearly all of the cash in the target corporation at the time of the acquisition is used to pay for defendants' purchase of the shares of stock.

10. The sale of these low-basis, high-value assets generates large capital gains for the target corporations on which corporate income taxes are owed. When they purchase the stock of each target corporation, defendants falsely or fraudulently promise the sellers, who are their customers, that defendants will be responsible for payment of the corporation's income taxes. Defendants imply that they intend to pay these income taxes, but defendants never pay these taxes.

11. Defendants require that the target corporations retain cash reserves at the time that they purchase the corporation in order to give the appearance that the company has adequate

funds to pay its tax liabilities. To finance the purchase of the target corporation's stock, defendants obtain short-term bridge loans which defendants repay within days of the stock purchase using cash which comprises a large percentage of this cash reserve.

12. Defendants cause each company to enter into sham contracts with defendants' businesses for the purported provision of legal and consulting services in exchange for fees that defendants pay themselves using funds from the target corporation's cash reserves. Ultimately, defendants use up all or nearly all of the cash reserves in each target corporation, depleting each target corporation's funds and rendering, by design, each corporation insolvent and unable to pay its income taxes.

13. After they purchase the target corporations, defendants implement a loss-creating tax scheme that generates fake losses. Most recently, defendants have implemented the DAT abusive tax scheme. To this end, defendants purport to re-engineer each target corporation into a viable debt-collection business in order to implement this loss-creating scheme. The DAT scheme involves purchasing and allocating Brazilian retail debt (distressed consumer receivables), such as debt from bad checks, through trusts and sub-trusts. Shortly after defendants acquire the debt and allocate it to a target corporation as part of its purported entry into the debt-collection business, defendants contend, without having any basis for doing so, that nearly all of this debt is not collectable and constitutes bad debt. Defendants then concoct a bogus write-off for each target corporation in an amount that offsets all or nearly all the gains from the proceeds of the low-basis, high-value asset sale.

14. Defendants cause each target corporation to offset its taxable gains with bogus losses purporting to eliminate each corporation's tax liabilities. Defendants never pay or intend to pay

the taxes owed by any of the target corporations that they acquire as part of their intermediary transaction tax scheme.

15. The IRS has expended substantial resources to recoup these lost corporate tax liabilities. These efforts often involve tracking down each corporation's original owners, who are defendants' customers, and the asset buyers, when appropriate, and then assessing these individuals with the corporate income taxes. Neither defendants nor their customers disclose the intermediary transactions to the IRS, as they are required to do by law, thus making it significantly harder for the IRS to detect and identify the existence of these transactions. Moreover, often defendants' customers are foreign nationals or otherwise reside abroad, which further complicates IRS efforts and makes it nearly impossible for the IRS to recoup all of these losses.

DEFENDANTS

Charles G. Klink

16. Defendant Charles G. Klink does business at 15723 Park House Drive, Unit No. 39, Fontana, California 92336.

17. Klink is an attorney who is licensed to practice law in California and New York. He graduated from the University of California at Los Angeles School of Law in 1992 and from Pomona College in 1987.

18. Klink is the general counsel of ASI, which he also co-owns and co-manages with Block.

19. Klink is the sole owner of Klink & Associates, LLC, a legal practice based in Southern California that employs Klink and at least one other employee, who functions as Klink's paralegal.

20. On information and belief, Klink also is the sole owner and operator of Carpevino LLC, a Nevada limited liability company. Carpevino is an entity that purports to trade and store wine for the target corporations, draining remaining funds from the target corporations after defendants purportedly re-engineer these companies.

21. Earlier in his career, Klink practiced law at several large corporate law firms. Between 1992 and 1996 and between 1997 and 1999, Klink was an associate specializing in bankruptcy, corporate finance and asset-securitization law in the New York and Los Angeles offices of Brown & Wood, LLP (now Sidley Austin LLP). In 1999, Klink started working in the Los Angeles office of Manatt, Phelps & Phillips, LLP where he practiced corporate and securities law and became a partner.

22. When he worked at Manatt, Phelps & Phillips, Klink started providing legal advice to Fortrend International LLC, which was a firm client that promoted and helped to organize intermediary transactions. Klink advised Fortrend about its intermediary transactions.

23. In or around 2003, Klink left Manatt, Phelps & Phillips. On June 16, 2003 he founded Klink & Associates, which purports to provide legal services in connection with the intermediary transactions that defendants promote. Klink & Associates receives purported legal fees from the target corporations that defendants acquire.

24. Also in 2003, former Fortrend associates formed MNA Holdings, LLC to promote and implement intermediary transactions. Klink worked as outside counsel for MNA Holdings until he co-founded ASI with Block.

25. Klink has promoted intermediary transaction tax schemes in his individual capacity, as well as through ASI, MNA Holdings, and Fortrend International.

Steven Block

26. Defendant Steven Block does business at 14905 Landmark Drive, Louisville, Kentucky 40245.

27. Block attended St. John's University from which he graduated in 1985 with undergraduate degrees in Finance and Economics.

28. Block co-owns and co-manages ASI with Klink.

29. Block has held numerous jobs in the financial industry. He worked at Merrill Lynch in the 1980's, and throughout the 1980's and at different times during the 1990's, he worked with other New York-based securities firms, mainly in the capacity of broker or wholesaler.

30. Starting in the late 1980's Block began working with Fortrend International LLC as a wholesaler.

31. In 2003, Block became MNA Holdings' director of strategic development.

32. In 2004, Block co-founded ASI with Klink and left MNA Holdings.

33. Also in 2004, Block formed his own consulting firm, Blairington LLC, which purports to consult on the intermediary transactions that defendants promote. Blairington receives purported consulting fees from the target corporations after defendants acquire them.

34. Block has promoted the intermediary transaction tax schemes through a number of companies, including ASI, MNA Holdings, and Fortrend International.

Caleb S. Grodsky

35. Defendant Caleb S. Grodsky does business at 1818 Pelham Avenue, Los Angeles, California 90025. Grodsky is an attorney and a member of the California bar. He graduated from Pepperdine School of Law in 1996 and before that from the University of California at Los Angeles with a Bachelor's Degree in economics.

36. Grodsky practiced law at Battle Fowler LLP's Los Angeles office, and later at the Los Angeles office of Manatt, Phelps & Phillips, as an associate in the corporate securities department. Grodsky became acquainted with Klink at Manatt, Phelps & Phillips. On information and belief, Grodsky worked at Manatt, Phelps & Phillips until late 2003 or early 2004.

37. In or around 2003 or 2004 Grodsky started his own law firm, the Grodsky Law Firm which he still maintains. In addition, he also is an associate counsel at ASI.

38. Grodsky has helped Klink and Block assemble and promote numerous intermediary transaction tax schemes, including those schemes that ASI has promoted. In connection with this assistance, Grodsky has received substantial fees. For example, in one intermediary transaction in which Klink and Block served as lead promoters, Grodsky received at least $100,000 in fees.

39. Grodsky also has been the lead promoter of at least four intermediary transactions that Klink and Block referred to him and for which Klink and Block provided assistance and

received fees. In addition, the Grodsky Law Firm also has received purported legal fees for services rendered in connection with the Grodsky-led intermediary transactions.

Related Entities

40. Defendants have incorporated a number of entities that facilitate the promotion of their intermediary transaction tax scheme.

Acquisitions Strategies International, LLC

41. On June 8, 2004, Klink and Block incorporated ASI in Nevada. Klink and Block each own 50% of ASI.

42. Klink and Block have described ASI as a "boutique investment firm specializing in tax-advantaged acquisition strategies."

43. At ASI, Klink typically attends to legal issues and coordinates the general strategies for implementation of the intermediary transaction tax scheme. Block typically handles advertising and customer contacts for ASI. Klink and Block both take part in implementing the intermediary transaction.

44. ASI, at the direction of Klink and Block and with the assistance of Grodsky, has been the lead promoter of at least nine intermediary transactions, and it has received at least $2.5 million in fees, which are in addition to the fees that Klink, Block, Grodsky and their legal and consulting businesses have each received.

Oceanus Solutions, LLC

45. Klink and his wife founded Oceanus Solutions, LLC, which is a single member liability company incorporated in California on October 9, 2002. Oceanus is a purported

consulting company. Oceanus also is the sole owner of the intermediary companies that acquire the target corporations as part of the ASI-led intermediary transaction tax scheme.

46. Oceanus is also a grantor for Nevada-based trusts that are created as part of the DAT abusive tax scheme that defendants implement after they acquire the target corporations in the ASI-led transactions.

47. In November of 2004, Klink and his wife sold Oceanus to Transpac Enterprises Co., Ltd, which is a Taiwanese company. The president of Oceanus and Transpac is a relative of Klink's wife who is based in Taipei, Taiwan. Transpac's bank accounts are also based in Taiwan.

Finamco, LLC

48. On April 29, 2005, Klink and Block formed a Nevada company called Finamco, LLC for the purported purpose of aiding in the collection of Brazilian retail consumer debt.

49. Finamco entered into collection services agreements with defendants' Nevada-based trusts that are created as part of the DAT abusive tax scheme .

50. Among other things, these services agreements require Finamco to provide, "administrative and collection services," to "manage[] the portfolios of accounts . . . in order to help maximize collection and recovery," and to provide the Trust "summary collection and expense reports" at least once every six months. For these services, Finamco is to receive 25 percent of the revenue from collections of Brazilian retail debt.

51. Finamco also has paid Grodsky for his services as a trustee for the Nevada-based trusts and sub-trusts through which defendants have allocated Brazilian retail debt as part of the DAT tax scheme in which defendants participate after they acquire a target corporation.

Arvaco, LLC

52. Grodsky formed Arvaco, LLC in Nevada on November 15, 2006, naming himself as managing member and Klink as registered agent on information and belief. Arvaco purportedly serves to aid in the collection of Brazilian retail consumer debt for Grodsky-led intermediary transactions.

DEFENDANTS' INTERMEDIARY TRANSACTION TAX SCHEME

53. Defendants have promoted numerous intermediary transactions. After defendants, through their intermediary companies, acquire their customers' corporations, as part of the intermediary tax scheme, defendants implement and participate in the DAT tax scheme in order to offset gains illegally and to evade the payment of corporate income taxes.

54. Starting in 2004, Klink and Block have frequently promoted intermediary transactions through ASI.

55. Klink and Block also have referred intermediary transactions to Grodsky that he promotes with their substantial assistance and support. Grodsky, in turn, also has helped Klink and Block promote intermediary transaction tax schemes.

Mechanics of the Intermediary Transaction Tax Scheme

56. Defendants regularly seek new customers by attending trade association meetings and by sending unsolicited emails to trade associations, accounting firms, and tax attorneys that tout the purported tax benefits of their intermediary transaction tax scheme. These emails describe the intermediary transaction and promise falsely and/or fraudulently that these transactions are a lawful way to avoid the payment of corporate income taxes.

57. One such email that defendants have frequently circulated advertises that ASI is "actively seeking situations in which a buyer desires to purchase only the assets of a company and not the stock, but the company is structured as a C corporation and thus there needs to be a stock sale to avoid the 'DOUBLE TAXATION' problem."

58. The scenario described in this promotional email arises when a closely-held C corporation sells only its assets but not its corporate stock.

59. In the wake of an asset-only sale, the closely-held corporation's owners generally liquidate the corporation and receive a distribution of the company's funds. In this liquidation scenario, the corporation pays income taxes on the gains received from the sale of its assets. The corporation's owners also pay taxes on the gain received from sale of the corporation's stock. This is the so-called "double taxation" referred to in the email described above.

60. Defendants specifically seek out customers who own companies that are C corporations which pay taxes at the corporate level (as opposed to S corporations or LLCs in which the income from those entities passes through to the shareholders who pay taxes on that income at the individual level).

61. When an individual or corporation sells a capital asset and has gains on that asset, it must pay taxes on that gain. *See* I.R.C. §§ 1201 *et seq*. A capital asset is an asset that is real property, securities or any other type of non-real property.

62. Defendants advertise that their intermediary transaction tax schemes allow customers to avoid the so-called "problem of double taxation" by avoiding the payment of corporate level taxes. Rather, as defendants advertise, with the intermediary transaction, their customers pay taxes only at the individual level.

63. In the intermediary transaction tax scheme, defendants, through intermediary companies that they control, purchase the shares of a target corporation. With the intermediary transaction, there is no liquidation scenario, because the company's owners do not liquidate the company after the asset sale.

64. As part of the scheme, defendants agree to be responsible for the target corporation's income taxes after they acquire these corporations.

65. In a second intermediary transaction scenario, defendants, through intermediary companies that they control, purchase the shares of a target corporation's stock *immediately before* that corporation's assets are sold. Defendants also tout the tax benefits of this second scenario, such as in one standard promotional email:

> [A]nother scenario in which ASI has been quite successful is the purchase of 'C' corporations that hold portfolios of appreciated marketable securities. In such situations, ASI or its designee will purchase the stock of such a corporation with those marketable securities still owned by the corporation. The advantage is that, even with the potential tax liability from the appreciation of those assets, ASI, as stock purchaser, will pay a premium above what another seller would pay for the stock of the company.

66. In the first scenario of the intermediary transaction tax scheme, the asset at issue is typically real property, and the target corporation sells this asset *before* defendants' intermediary companies purchase the corporation. In the second scenario, the target corporation's assets are typically marketable securities or other types of non-real property, and these assets are sold *after* defendants' intermediary companies purchase the target corporation's shares of stock.

67. In both scenarios, defendants promote their intermediary transaction tax scheme as a plan that contemplates and involves the sale of each target corporation's assets. Indeed, as part of the intermediary transaction tax scheme, defendants negotiate with their customers to execute a stock sale with the full knowledge that the target corporation intends to sell its assets. The

asset sale and the stock sale are related steps that are part of a larger plan, which is the intermediary transaction tax scheme as it is designed to evade the payment of federal corporation income taxes.

Intermediary Transaction Tax Scheme Steps

Step One

68. In the first step of the intermediary transaction scheme, defendants contact their customers and their customers' accountants, attorneys or other representatives to discuss the details of the intermediary transaction, including the expected asset sale, stock purchase and tax consequences stemming from the scheme. Typically, this step occurs before there is any asset sale.

69. Defendants work with their customers directly and with their customers' representatives to develop a larger plan to implement the intermediary transaction scheme.

Step Two

70. Next, defendants request specific financial information from their customers to determine a purchase price for the target corporation's stock. Defendants request copies of the target corporation's financial statements, which estimate the value of corporate assets and liabilities, as well as copies of draft pro forma corporate tax returns which reflect the target corporation's projected tax liabilities for the tax year in which the asset sale is expected to occur. Defendants also request from their customers asset sales information.

71. When the target corporation's stock sale precedes the asset sale, defendants request that their customers provide them with a portfolio summary of the target company's marketable securities before defendants propose a stock price.

72. Defendants review the specific financial information that they receive from their customers in order to propose a price for the target corporation's stock.

73. Defendants calculate a proposed stock purchase price by determining the value of the target corporation's assets and subtracting from that value the corporation's non-tax liabilities, as defendants did with the stock purchase price they proposed to the I. G. B. & G. Corporation's controlling shareholder in an October 15, 2004 letter of intent. Defendants then further subtract from that number approximately fifty percent of the target corporation's projected federal and state income tax liability for that tax year, as reflected on the pro forma corporate income tax returns provided at defendants' request. The remaining dollar amount is the stock purchase price that defendants offer to pay for the target corporation.

74. Defendants advertise that this fifty percent figure that they deduct to arrive at the proposed stock value is a so-called premium payment, meaning that defendants' customers get to retain in the form of a higher stock price the other fifty percent that is not deducted when calculating the stock purchase price; defendants tout this premium payment as their customers' corporate income tax savings. To this end, defendants falsely and fraudulently state that after the stock sale, they alone are responsible for the target corporation's income taxes.

Step Three

75. Defendants then typically draft and send to their customers a letter of intent to purchase the stock of the target corporations. The letter of intent states a proposed stock sale which is calculated using the formula described in step two.

Step Four

76. Next, defendants draft and then send to their customers a proposed stock purchase agreement. The agreement includes a preliminary stock price, which stems from defendants' more thorough review of the target company's finances, books and records.

77. The stock purchase agreements also contain provisions mandating that defendants' customers (as sellers of the target corporation stock) are responsible for that company's non-tax liabilities; that defendants (as buyers of the target corporation) are responsible for paying the company's corporate income taxes; and that defendants promise that the company will continue actively to engage in business for three - five years from the date of sale in order to give the appearance that defendants are purchasing the stock of the target corporation with the intention of turning that corporation into a viable business.

78. In addition, starting with the Alicia Holdings transaction in November 2005 (discussed below), defendants added a provision to their stock purchase agreements that provides that "[f]or federal income tax purposes, neither Seller, Buyer nor Company, nor their respective Affiliates, will report the transactions contemplated by this Agreement (separately or in combination) as direct or indirect participation by them in a reportable transaction for purposes of Treasury Regulations Sections 1.6011-4." The intermediary transaction, however, is a reportable transaction, as discussed below. *See supra* at ¶¶159-172.

79. Defendants' stock purchase agreements also mandate that the target corporation retain a minimal amount of cash reserves at the time of its sale. Defendants determine the amount of cash reserves largely by determining the projected federal and state corporate income tax liabilities for that year and ensuring that the cash reserves cover the anticipated tax liabilities.

80. This cash reserve requirement helps induce customers to participate in the intermediary transaction. This requirement is designed to give the appearance that, on paper, the target corporation has adequate funds to cover its projected tax liabilities at the time of the stock sale.

81. In actuality, defendants never intend to pay and never do pay the target corporation's income taxes.

82. Defendants also provide their customers with a due- diligence list and a working-group list, such as the documents attached to an August 31, 2005 email that Klink sent to a New Jersey-based customer, whose company, Mt. Royal, Inc., had real estate holdings (discussed below), outlining post-asset sale steps. The due-diligence list seeks substantial information about the target corporation, including additional information about the company's finances, general organization, tax returns, securities filings, and any other liabilities arising from pending or threatened litigation, or any antitrust, environmental or insurance issues.

Step Five

83. Defendants establish separate limited liability companies in Nevada to function as intermediary companies; these companies are the entities that actually purchase the stock of the target corporations. Defendants control these intermediary companies.

84. In seven of ASI's most recent intermediary transactions, defendants have formed at least five Nevada-based LLCs for the purpose of serving as intermediary companies: Spaco LLC, Spefiaco LLC, Artura Ventures LLC, Bactar LLC, and Actol LLC.

85. Defendants' earlier intermediary transactions did not involve separate intermediary companies. Rather, ASI also functioned as an intermediary company.

86. Klink and Block try to disguise the fact that they own and control the intermediary companies that are incorporated in Nevada, where state laws make it relatively difficult to detect a company's true owners. In addition, Oceanus is listed as being the sole member of each of the Nevada-based intermediary companies that ASI has incorporated. Transpac is, in turn, Oceanus' sole member and is operated by a relative of Klink's wife in Taipei, Taiwan.

87. Grodsky caused the formation of at least four Nevada-based LLCs for the purpose of serving as intermediary companies: Cross Shore Asset Holdings, LLC; Novastad LLC; Tegmar LLC; and Dalmar LLC.

88. Similarly, Grodsky also tries to disguise the fact that he owns and controls the intermediary companies that he has formed in Nevada. For example, Alterbridge Ventures Ltd. Co., a separate entity established in the Philippines, is listed as each of these intermediary company's sole member. In actuality, Alterbridge Ventures uses the same Los Angeles mailing address that Grodsky maintains.

Step Six

89. The intermediary companies purchase each target corporation with the assistance of short-term bridge loans. Defendants and their business associates fund these short-term bridge loans. Defendants, in turn, issue promissory notes to themselves and their associates which use each target corporation's cash (received from the asset sale) as collateral for the loan.

90. When the asset sale precedes the stock sale, almost immediately – often within 1 or 2 days – after defendants retain formal control of the target corporations, they use the asset sales proceeds retained by the corporation to repay these bridge loans. Defendants typically repay

their bridge loans almost immediately after an asset sale when the stock sale precedes the asset sale.

91. When defendants repay these bridge loans, defendants also pay their lenders, including themselves, a so-called facility fee, which often equals 1-1.5% of the total loan amount and sometimes, a so-called accounting fee, which may equal 7-8% of the original loan amount.

92. For example, in one transaction involving Mt. Royal Plaza, defendants' business associate and accountant lent the intermediary company, Spaco LLC, $525,000 to help purchase Mt. Royal's shares of stock. Defendants issued a promissory note to the lender which used Mt. Royal's cash assets as collateral for the loan. Within two days after making this loan, this business associate received a $567,875 wire transfer, which included a repayment of the loan, a $7,875 purported facility fee, and $35,000 for a purported accounting fee. In this same transaction, Klink made a $400,000 bridge loan to Spaco LLC, and he received a $6,000 purported facility fee, as well as repayment of the $400,000 loan within a few days after defendants took control of the target corporation.

Step Seven

93. Immediately after defendants, through their intermediary companies, complete their purchase of the target corporation's shares of stock and take control of the corporation, defendants transfer the target corporation's cash reserves into a bank account that they control.

94. The target corporation's former owners, who are defendants' customers, resign from their officer and director positions at the target corporation, and defendants replace these former owners, becoming the officers and directors of each target corporation.

Step Eight

95. Right before they purchase a target corporation, defendants cause the intermediary company, which they control, to execute retainer letters with Klink & Associates, Blairington LLC and often with the Grodsky Law Firm, for the purported performance of either legal services, management services or consulting services that relate to execution of the intermediary transaction.

96. Shortly after defendants' intermediary companies purchase a target corporation, and pursuant to these retainer letters that each intermediary company executes, defendants pay themselves legal fees, consulting fees and other types of fees, effectively siphoning off the target corporation's cash reserves into defendants' bank accounts and rendering the target corporation insolvent. As a result, the target corporation has no funds with which to pay its corporate income taxes that are due on account of the low-basis, high-value asset sale.

Step Nine

97. In the next step of the intermediary transaction tax-fraud scheme, defendants implement a loss-creating tax scheme. Most recently, defendants have implemented the DAT scheme. To effect this implementation, defendants purport to re-engineer the business of the target corporations that they purchase by turning each of these companies into a debt-collection business. Defendants cause each target corporation to pass a resolution authorizing, by written consent, entry into the debt-collection business.

98. Next, defendants cause each target corporation to obtain a portion of a portfolio of distressed assets comprised of distressed consumer account receivables from Brazilian retail establishments, such as Lojas Arupua, a Brazilian consumer electronics retailer. This typically

happens within a few days after one of defendants' intermediary companies purchases the stock of the target corporation.

99. Defendants cause these distressed account receivables to be contributed to each target corporation's asset portfolio as distressed assets. Defendants purport to have each target corporation enter into the business of collecting on the debt comprising this distressed asset portfolio.

100. Thus, defendants cause each target corporation to participate in a DAT abusive tax scheme, the mechanics of which are discussed below.

Step Ten

101. The DAT scheme that defendants implement is promoted by John Rogers, an attorney in Chicago, Illinois. The United States recently filed a complaint against Rogers in United States District Court for the Northern District of Illinois seeking to enjoin Rogers under I.R.C. §§ 7402 and 7408. As the complaint alleges, Rogers is a long-time promoter of the DAT scheme and also has promoted other related tax schemes.

102. The sole purpose of any DAT transaction, like other loss-creating tax schemes, is to enable an entity to claim sham losses on its tax return in an effort to offset all or some of that entity's gains and thus reduce or eliminate that entity's income tax liability.

103. Defendants implement and then participate in the DAT scheme in connection with their promotion and establishment of the intermediary tax scheme. The DAT scheme ensures that defendants profit from the sale of the target corporation's assets and use of the intermediary transaction tax scheme by purportedly eliminating all or nearly all of the acquired corporation's tax liabilities.

104. For the ASI-led intermediary transactions, defendants have established at least three Nevada-based trusts to acquire the portfolios of Brazilian retail debt. These Nevada-based trusts are called the Distressed Asset Recovery Business Trust (DARB Trust), the Aggregated Receivables Business Trust (ARB Trust) and the Stedco Business Trust (Stedco Trust).

105. For the Grodsky-led intermediary transactions, Grodsky also has established at least two Nevada-based trusts to acquire the portfolios of Brazilian retail debt. These trusts are the Conrev Business Trust (Conrev Trust) and the Broad Asset Spectrum Business Trust (Broad Asset Spectrum Trust). In addition, the Stedco Trust also is used in the Grodsky-led intermediary transactions.

106. Sugarloaf Fund LLC, West End Fund LLC and Warwick Trading LLC are three LLCs that John Rogers operates and manages, and they are designated grantors for the Nevada-based trusts. These three LLCs purportedly have contributed distressed assets in the form of Brazilian retail debt to the Nevada-based trusts. Each Nevada-based trust, in turn, transfers through a sub-trust a beneficial interest in that retail debt to each target corporation. Each target corporation deducts nearly the entire value of the contributed debt portfolio on its federal income tax return, which offsets the corporation's gains from its low-basis, high-value asset sale and purportedly eliminates its income tax liabilities as to those gains.

107. Oceanus also is a designated grantor for the trusts used in the ASI-led transactions, and Alterbridge Ventures is a designated grantor for the trusts used in the Grodsky-led transactions.

108. Sugarloaf Fund LLC, West End Fund LLC and Oceanus are the grantors for the DARB Trust. Sugarloaf Fund LLC, Warwick Trading LLC, and Oceanus Solutions are the

grantors for the ARB Trust. Warwick Trading LLC and Oceanus Solutions are the grantors for the Stedco Trust. Sugarloaf LLC and Alterbridge Ventures are the grantors for the Conrev Business Trust, and Warwick Fund LLC and Alterbridge Ventures are the grantors for the Broad Asset Spectrum Business Trust.

109. Grodsky is the trustee for the DARB Trust, ARB Trust and Stedco Trust. And Oceanus, the sole member of certain intermediary companies, also is the beneficiary for each of these trusts. Klink and Block, through their company Finamco, paid Grodsky a trustee fee of $4,000 per trust for each year between 2006 and 2008.

110. A relative of Grodsky's former girlfriend is the trustee for the Conrev Trust and the Broad Asset Spectrum Trust, and Alterbridge Ventures, the sole member of certain intermediary companies used in Grodsky-led transactions, also is the beneficiary for these two trusts.

111. When defendants establish their Nevada-based trusts, they do so by creating a trust agreement that the trustee and individuals representing the purported trust grantors execute. For example, the trust agreement that creates the Stedco Trust was executed on May 26, 2006. John Rogers, as manager of Warwick Trading, the president of Oceanus Solutions (a relative of Klink's wife) and Grodsky, who was the trustee of the Stedco Trust, all signed this trust agreement.

112. At defendants' direction, the trustee of each trust purports to allocate a portion of each trust's debt portfolio to a number of separate sub-trusts.

113. Defendants direct the creation of sub-trusts through the execution of supplemental sub-trust agreements that "create a separate sub-trust and identify and allocate a separate portfolio of trust assets." Each sub-trust is identified by the year in which it was formed and a

letter designation. For example, on November 6, 2006, the 2006-C Supplement to the Trust Agreement for the Conrev Trust created the 2006-C sub-trust, which allocated a portion of the debt portfolio from the Conrev Trust to Indian Creek Vineyards, Inc., one of the target corporations that Grodsky acquired as part of an intermediary transaction tax scheme that he promoted; this transaction involved the sale of a California vineyard (discussed below).

114. Grodsky executed this sub-trust agreement in his capacity as secretary of Indian Creek after defendants, through intermediary companies that they control, acquired this target corporation. Rogers executed this sub-trust agreement in his capacity as manager of Sugarloaf LLC and the trustee of the Conrev Trust (a relative of Grodsky's former girlfriend) also executed the sub-trust agreement. In short, the sub-trust agreement allocated a portion of the Brazilian retail debt that Rogers contributed through Sugarloaf LLC to Indian Creek so that Grodsky could use that debt to generate bogus losses that offset Indian Creek's gains received from the proceeds of its asset sale.

115. Each sub-trust agreement also includes an addendum that is a Beneficial Interest Certificate which purports to designate the target corporation as the sole beneficiary of the portfolio of the retail debt specifically allocated to that sub-trust. For example, Indian Creek is designated as the sole designated beneficiary of the 2006-C sub-trust of the Conrev Trust.

Step Eleven

116. After each target corporation receives an allocation of the Brazilian retail debt through its beneficiary interest in a designated sub-trust, defendants cause each trust to enter into a purported collection agreement that services this allocated debt. Multicred Investimentos LTDA, a company based in Brazil, is the company with which defendants have most frequently

contracted for the purported purpose of collecting the distressed consumer receivables allocated to each target corporation.

117. Multicred was founded in 2003 and is based in Sao Paulo, Brazil. Defendants have worked with Multicred for a number of years, but they have undertaken no due diligence to ascertain whether or how Multicred collects the distressed consumer account receivables.

118. Shortly after defendants cause the trusts to enter into a purported service agreement with Multicred, defendants or one of their representatives sends Multicred a letter for the purported purpose of ascertaining an "estimate as to the collectability on the loans" that comprise the debt portfolios owned by each sub-trust. Defendants regularly request that Multicred provide a so-called "rough estimate" from the Collection Agent as to the general prospects for future collections. Defendants seek this information by the end of the calendar year for tax purposes.

119. These letters seeking estimates of loan collectability, such as the June 20, 2006 letter that Grodsky sent to Multicred in his capacity as trustee for the Stedco Business Trust and concerning the "loans that have been allocated to the 2006-A-Sub-trust," are form letters; each letter contains the same language. That language includes a statement that the representatives of the target corporation understand that a statement of collectability "would not be an exact statement of the future prospects for collections" of the sub-trust's allocation of distressed assets, and that the target corporation "has acknowledged that this is the case and, for accounting and financial planning purposes, simply wishes to obtain a rough estimate from the Collection Agent as to the general prospects for future collections" of the distressed assets.

120. Defendants purport to receive a response from Multicred that describes the relative collectability of the debt portfolio allocated to a particular target corporation. In actuality,

Multicred has never identified a precise or even rough percentage of the distressed asset portfolio that is collectable debt.

121. Nevertheless, defendants regularly determine that approximately 75%-82% of a purported sub-trust debt portfolio is not collectable, and thus, should be written off as bad debt. These bad debts are then deducted as losses on the target corporation's tax returns; these claimed losses purport to offset the gains that the target corporation receives from the asset sale proceeds.

Step Twelve

122. Defendants also purport to re-engineer some of their target corporations into a wine-trading business after they acquire these corporations. These wine-trading businesses are in addition to the debt-collection businesses that defendants purport to establish.

123. Defendants cause the target corporations to pass corporate resolutions that authorize each company to enter into the "additional business line of buying and selling fine wines in the private market involving wine collectors and others." This is standard language that defendants use in numerous such resolutions, like the resolution passed by Alicia Holdings, a corporation that owned real estate and was based in California (discussed below). The standard language in that resolution also states that the intermediary company, as sole shareholder of Alicia Holdings, and the company's director, who was Block, had "deemed it to be in the best interest of the Corporation [Alicia Holdings]. . . to actively pursue investments in, and business opportunities involving, the acquisition and collection of fine wines in the private market."

124. Defendants cause some target corporations to execute a wine-trading services agreement with Klink's company, Carpevino. These agreements are executed by Block, as an officer of each target corporation, and Klink as owner of Carpevino.

125. Defendants purport to authorize entry into the wine business because they determine that a target corporation "may, over time, be able to realize significant profits in such business activities."

126. In actuality, there is no indication that any of the target corporations have ever participated in any wine-trading services business, let alone made profits from such a business. Rather, the wine-trading services agreement that defendants execute is designed and used to transfer funds from certain target corporations to the defendants.

Step Thirteen

127. As part of the intermediary transaction tax scheme, defendants typically ensure that they purchase the target corporations during the same tax year in which the target corporation's assets are sold.

128. As part of the intermediary transaction tax scheme, defendants also ensure that after they purchase a target corporation, that corporation is purportedly re-engineered into a debt-collection business and wine-trading business during that same tax year. This means that often defendants' intermediary transactions happen in a compressed time frame, so that defendants also "have sufficient time [during that] year to re-engineer [the company] into the new line of business as we do when we acquire companies, " as Klink explained in an October 27, 2005 email to Texas-based customers who owned a company with interests in the health-care sector.

129. The purported losses generated by the newly-re-engineered target corporation's debt-collection businesses must be claimed in the same year in which the target corporation obtains gains from the sale of its assets in order to offset the corporation's gains on that year's corporate income tax returns.

130. As part of the intermediary transaction tax scheme, defendants cause the target corporations to file deliberately inaccurate federal income tax returns. Typically, one of defendants' business associates, who finances some of defendants' bridge loans, prepares the corporations' income tax returns, which are filed after defendants acquire the target corporations through intermediary companies.

131. In every instance and by design, these tax returns have the following common characteristics: (1) the tax returns report little or no corporate income; (2) the tax returns report a large dollar amount of bad debts from defendants' participation in the DAT tax scheme; and (3) the tax returns also report a high dollar amount of other deductions, which are comprised largely of deductions for legal, professional and management fees, a substantial portion of which defendants have paid to themselves for purportedly providing services.

132. For example, Mt. Royal Plaza (discussed below) filed a federal tax return in 2005. That tax return reflects a total of $1,013,021 in capital gain net income received from the sale of Mt. Royal's real estate holdings immediately before defendants acquired the corporation. The 2005 tax return claims a $905,000 deduction for purported bad debt, which was a result of the DAT tax scheme that defendants implemented as part of the company's purported re-engineering. The 2005 Mt. Royal income tax return also reflects $241,000 in other deductions of which $133,000 is for purported legal and professional fees, and $44,000 is for purported management fees. Defendants paid themselves at least a substantial portion of this $241,000.

133. Defendants cause each target corporation to file a tax return that reports no income or virtually no income, due to the purported bad debt deduction that defendants cause each

corporation to claim and the deductions for fees for purported services that defendants pay to themselves.

134. Thus, by design and as a function of the intermediary transaction and DAT schemes, defendants' customers' corporations sell low-basis, high-value assets, obtain substantial gains on these asset sales, and then these corporations illegally pay no (or very little) income tax on these gains. Moreover, the defendants drain the corporations of virtually all cash or other assets, leaving the corporation insolvent by the time the IRS discovers the defendants' fraud.

DEFENDANTS' HISTORY OF UNLAWFUL CONDUCT SPANS MORE THAN A DECADE

135. Klink's and Block's unlawful promotional activities predate ASI. In or around 1999, Klink and Block began promoting intermediary transactions through Fortrend International, when, on information and belief, they first became acquainted with each other.

136. At Fortrend, Klink and Block implemented and participated in a few different illegal tax schemes that were designed to create bogus losses for the target corporations acquired through the intermediary transactions that Klink and Block promoted. Like the DAT tax scheme, these other tax schemes also were designed to offset the gains generated by low-basis, high-value asset sales. These loss-creating tax schemes predated defendants' use of the DAT tax scheme. Klink and Block implemented and participated in one of these loss-creating tax schemes until they believed that the IRS would catch up to them, and then defendants implemented and participated in a new and different loss-creating tax scheme. For example, in 2001 and 2002, Klink and Block, while at Fortrend, implemented and participated in the Son of Boss tax scheme in connection with the intermediary transactions that they promoted. The Son

of Boss tax scheme generated bogus losses, but in the early-mid 2000's, this transaction came under enhanced scrutiny, and defendants moved on to other schemes.

137. In 2003, after Fortrend International went out of business, Klink and Block began working with MNA Holdings, through which they promoted the intermediary transaction scheme. MNA Holdings was comprised mainly of former Fortrend employees, and it coordinated intermediary transactions that it also promoted. At MNA Holdings, Klink and Block used the distressed asset debt (DAD) tax scheme to import losses into the acquired target corporations. The DAD tax scheme functions like the DAT scheme, except that the DAD tax scheme involved partnership interests, instead of beneficial interests in trusts and sub-trusts.

138. In 2004, Klink and Block formed ASI, through which they have continued to promote the intermediary transaction scheme. In 2004, after the IRS became aware of the DAD scheme's prevalence, defendants moved to the DAT tax scheme.

139. As the IRS has become increasingly aware of the DAT scheme's prevalence, defendants continue to search for new and different loss-creating tax schemes. For example, in or around late 2007 or 2008, Block prepared a PowerPoint presentation for potential customers that touts a transaction that allocates distressed debt using a securitization partnership as a means of offsetting gains from defendants' intermediary transactions.

DEFENDANTS' TAX SCHEMES ARE UNLAWFUL

140. The intermediary transaction scheme is an illegal tax arrangement under at least four separate judicial doctrines: (1) the substance-over-form doctrine; (2) the doctrine of economic substance; (3) the sham transaction doctrine; and (4) the step-transaction doctrine. In addition, defendants' schemes violate numerous internal revenue code provisions, a few of which are discussed below.

Substance-Over-Form

141. The doctrine of substance-over-form " requires [a] court to determine the 'true nature' of the transaction to ensure that tax consequences are based upon a transaction's actual substance and not mere labels." *Consol. Edison Co. of New York, Inc. v. United States,* 90 Fed. Cl. 228, 266 (Fed. Cl. 2009) (citations omitted). To this end, transactions and their attendant tax consequences may be re-characterized to reflect the true nature of the transaction. *See Enbridge v. United States*, 2009 WL 3753540 at *3 (5th Cir., Nov. 10, 2009).

142. Under the substance-over-form doctrine, defendants' intermediary companies are disregarded conduit entities. Defendants' transaction is re-characterized and income taxes are paid on the gains from the asset sale.

No Economic Substance

143. The intermediary transaction is disregarded under the economic substance doctrine. The doctrine of economic substance involves a two-prong test that a taxpayer must meet. First, the taxpayer must meet an objective test and show that the transaction has profit potential. Second, the taxpayer must meet a subjective test that shows that a taxpayer has a non-tax motive for the transaction. *See In re*: *CM Holdings, Inc.*, 301 F. 3d 96, 103, 105, 106 (3d Cir. 2001) (citations omitted); *ACM Partnership v. Comm'r*, 157 F. 3d 231, 251, 253 (3d Cir. 1998).

144. Defendants' intermediary transaction has no economic substance. Defendants' intermediary transaction has no objective reasonable possibility of producing any profits, and there is no non-tax motive for this transaction.

Sham Transaction Doctrine

145. Defendants' tax schemes also are sham transactions. A sham transaction is a transaction that never actually occurs, and is, thus, disregarded. *See In re*: *CM Holdings, Inc.* at 108.

146. Numerous aspects of defendants' tax schemes involve sham transactions, such as defendants purported re-engineering of the target corporations into viable debt-collection businesses and wine-trading businesses. In actuality, defendants never re-engineer the target corporations into viable businesses.

Step-Transaction Doctrine

147. The intermediary transaction is also disregarded under the step transaction judicial doctrine. Under the step-transaction doctrine, "interrelated yet formally distinct steps in an integrated transaction may not be considered independently of the overall transaction" if there is no reasonable economic justification for those steps to stand alone. *Comm'r v. Clark*, 489 U.S. 726, 739 (1989). *See also True v. United States*, 190 F.3d 1165, 1175-76 (10th Cir. 1999).

148. Defendants' intermediary transaction is comprised of numerous steps that are part of a larger plan that is designed to evade the payment of corporate income taxes, and these steps have no economic justification for standing alone.

Defendants' Schemes Violate Numerous I.R.C. Provisions

149. Defendants' intermediary transaction tax scheme also violates a number of provisions of the Internal Revenue Code, including but not limited to I.R.C. §§ 269, 482 and 165.

I.R.C. § 269

150. Section 269 of the Code provides that when a person or entity acquires directly or indirectly control of a corporation or property of another corporation "and the principal purpose for which such acquisition was made is evasion or avoidance of Federal income tax," then any tax benefits stemming from such an acquisition are disallowed. I.R.C. § 269(a).

151. Defendants acquire target corporations solely for the purpose of effecting the intermediary transaction scheme and evading the payment of corporate income taxes. At the time that defendants acquire the target corporations, these companies no longer have (or will imminently no longer have) any assets or other means by which to conduct business.

152. There is no non-tax reason for defendants to purchase any of the target corporations.

153. Defendants' intermediary transactions violate I.R.C. § 269.

I.R.C. § 482

154. Section 482 of the Code provides that when there are two or more businesses "owned or controlled directly or indirectly by the same interests," the IRS may allocate income as necessary "to prevent the evasion of taxes or clearly to reflect the income" of the business, when, among other reasons, transactions are not arm's length transactions. I.R.C. §482; Treas. Reg. § 1.482-1(b)(1).

155. The intermediary transaction is not an arm's length transaction for a number of reasons. Defendants control the intermediary companies that purchase the target corporations. Defendants determine the total cash reserves each target corporation will retain post-acquisition, and defendants control all aspects of how these cash reserves are spent. After they acquire the

target corporations, defendants use the cash reserves to pay off the bridge loans that they made to themselves. Defendants also draft non-arm's length agreements that state that each newly-acquired target corporation will pay defendants fees for services that defendants purportedly will render. By design, these fees deplete each target corporation's funds and help render the companies insolvent and not able to pay their corporate taxes. Defendants' intermediary transaction violates I.R.C. § 482.

I.R.C. § 165

156. Section 165 of the Code provides that a taxpayer may claim a deduction for any loss that the taxpayer sustains during that tax year, provided that the loss is not "compensated by insurance or otherwise." I.R.C. § 165. The loss that may be claimed must be a bona fide loss, which means that the loss must "be evidenced by closed and completed transactions, fixed by identifiable events," and except in a few specific circumstances, "actually sustained during the taxable year. Substance and not mere form shall govern in determining a deductible loss." Treas. Reg. § 165-1(b). *See also ACM Partnership*, 157 F.3d at 251, 252.

157. As part of the DAT scheme that defendants implement, they cause the target corporations to claim a deduction for the losses they incur from the purported bad debts that each target corporation acquires as part of that corporation's purported entry into the debt-collection business. These claimed losses are not bona fide losses within the meaning of I.R.C. § 165.

158. In violation of I.R.C. § 165, defendants or individuals acting at their direction, nevertheless, deduct improperly these losses on each target corporation's tax return.

THE INTERMEDIARY TRANSACTION TAX SCHEME IS A LISTED TRANSACTION

159. In January 2001, the IRS issued Notice 2001-16, which states that intermediary transactions like the ones defendants promote are "listed transactions." This means that defendants' intermediary transactions are the "same or substantially similar to one of the types of transactions that the IRS has determined to be a tax avoidance transaction." *See* Treas. Reg.1.6011-4.

160. The Code and Treasury Regulations require that taxpayers who participate in listed transactions disclose their participation by filing certain forms with their federal income tax returns. *See* I.R.C. §6111.

161. Defendants have knowingly, falsely and fraudulently advised their customers that defendants' intermediary transaction is not a listed transaction. Indeed, defendants have required that their customers contract not to report these transactions to the IRS and to agree that these transactions are not reportable transactions within the meaning of Treasury Regulation 1.6011-4. *See infra* at ¶ 78.

162. A material advisor as to a listed transaction also is required to file a report with the IRS identifying and describing the listed transaction and the potential tax benefits expected to result from the transaction. A material advisor must furnish the IRS with this information as to each occurrence of each listed transaction that he promotes. If a material advisor fails to provide the IRS with this information, he is subject to penalties. *See* I.R.C. §§ 6111, 6707(a).

163. Defendants are material advisors as to the intermediary transactions within the meaning of I.R.C. § 6111, and thus, they are required to maintain and file a listed transaction disclosure report concerning this transaction with the IRS. *See* I.R.C. §§ 6111, 6707(a).

164. Defendants have failed to file any such reports with the IRS as to the intermediary transactions that they have promoted. All of the intermediary transactions that defendants have promoted and assembled for their customers are listed transactions within the meaning of Notice 2001-16.

165. During most of 2004 and in prior years, the federal tax laws required promoters of tax shelters, such as defendants, to register their tax shelters with the IRS, and also to provide the IRS with a description of the potential tax benefits expected to result from these tax shelters. Promoters were required to provide the IRS with all of this information no later than the day on which the promoter first offered the tax shelter (or an interest in the tax shelter) for sale to customers. If a promoter failed to provide the IRS with this information by the date on which it was due, he was subject to penalties. *See* I.R.C. § 6707 (prior version; effective for tax returns due before October 22, 2004).

166. The intermediary transactions that defendants promoted, helped to promote and assembled for their customers prior to October 22, 2004 were tax shelters within the meaning of the prior version of I.R.C. § 6707.

167. Defendants failed to register any such tax shelters with the IRS. They also failed to provide the IRS with any information describing the tax shelters' tax benefits. They, thus, have engaged in conduct subject to penalty under I.R.C. §6707.

168. In addition, a material advisor as to a listed transaction also is required to maintain a list of all customers who participate in a listed transaction that must be furnished to the IRS upon request. *See* I.R.C. §§ 6112, 6708.

169. Pursuant to I.R.C. §§ 6111 and 6112, each defendant was required to maintain a separate list of customers who entered into the intermediary transactions that he promoted and then to furnish the IRS with such a list when requested. *See* I.R.C. §§ 6112, 6708.

170. When the IRS requested that Block provide this list, he provided the IRS with an incomplete list of the intermediary transactions that he promoted. Specifically, Block failed to list the Searington transaction (discussed below) and the transaction involving Progress, Inc., an Ohio-based corporation whose main assets were securities.

171. When the IRS requested that Grodsky provide this list in a September 26, 2009 letter, Grodsky failed to respond. He has never responded to the IRS's request or furnished the IRS with a list of customers who participated in the intermediary transactions that he promoted.

172. Block and Grodsky have engaged in conduct subject to penalty under I.R.C. § 6708.

DEFENDANTS HAVE MADE NUMEROUS FALSE OR FRAUDULENT MATERIAL STATEMENTS WHILE PROMOTING THE INTERMEDIARY TRANSACTION TAX SCHEME IN VIOLATION OF I.R.C. § 6700

173. Section 6700 of the Code penalizes anyone who makes a false or fraudulent material statement about tax benefits in connection with the participation in, organization of, or promotion of a tax arrangement. This provision of the Code also pertains to omissions– those instances when defendants have omitted material information from their customers in connection with their promotion of the intermediary transaction tax scheme.

174. A material statement is any statement about tax benefits that would have a substantial impact on a reasonably prudent investor's decision to participate in a particular tax

arrangement, such as a statement that concerns tax benefits resulting from a particular tax arrangement.

175. Defendants have made numerous false or fraudulent statements in connection with the participation in, organization of, or promotion of a tax arrangement, including some of the statements discussed below.

176. In one example, an unsolicited promotional email, dated June 13, 2007, that ASI's representatives sent to a tax attorney at a prominent law firm, claims that "ASI will purchase 100% of the stock [of a C corporation] in cash, after the assets are sold, taking on the seller['s] corporate level of tax liability." The email further states falsely and fraudulently that "[w]hat we do for C-Corp owners works and can be validated." In actuality, the intermediary transaction that ASI's email describes is not lawful, not valid, and defendants never pay or intend to pay their customers' corporate tax liability.

177. In a June 6, 2005 email that Block sent to a customer's accountant, whose firm is based in Orange, California, in connection with a promotion of an intermediary transaction, Block included a three page description of how ASI's intermediary transaction tax scheme works by using the example of a retired couple who seek to sell their low-basis, high-value assets owned by their corporation and then to live off of those sale proceeds. In this example, the couple cannot afford to do this because of the corporate level taxes that they will incur.

178. The narrative attached to the June 6, 2005 email describes a "creative solution" in which the Smiths, the retired couple, sell the operating assets of their corporation in one transaction, leave the cash from the asset sale in their corporation, and then sell their corporation stock in an all-cash sale for a value equal to the cash received from selling the assets, minus

approximately 50% of the corporate tax on gain from the asset sale. The narrative further explains falsely and fraudulently that, among other things, "[s]ubsequent to the purchase of the stock of the Company, Stock Purchaser [defendants] then changes the name of the business, if necessary, and re-engineers the Company into a new line of business that is expected to be profitable. As the new owner of the Company, Stock Purchaser is responsible for running the Company on an ongoing basis and satisfying the current and future corporate tax liabilities of the Company."

179. The statements that defendants make in this narrative are false and/or fraudulent statements. The narrative about the Smiths fails to mention that the described transaction is illegal under several judicial doctrines and numerous Code provisions, including those provisions cited above.

180. Defendants' promotional narrative also states falsely and fraudulently that the re-engineered target corporation "is expected to be profitable." Rather, by design, defendants re-engineer each target corporation into an unprofitable business for the express purpose of generating losses and draining cash from the corporation.

181. Indeed, in other statements aimed at promoting the intermediary transaction, defendants have acknowledged their intention to generate tax losses. For example, in a September 30, 2005 email Klink acknowledged this point when he responded to a query from an attorney at the Sheppard Mullin firm representing a customer in the Alicia Holdings transaction (discussed below). The attorney noted that the amount of cash remaining in the target corporation post-acquisition was expected to be $1.575 million but that the "company owes approximately $4 MM in taxes for 2005 which Buyer [ASI] is to pay." The attorney further

noted that "[a]ccording to my math, this leaves the Buyer in the hole to the tune of $3.25MM. What am I missing?" Klink responded: "As far as the raw economics on the face of things, you have things true on rough numbers. The 'missing' part is that the buyer will be able to substantially reduce/offset the result of the built-in gains by means of the new line(s) of business that are involved once we re-engineer the company post-acquisition."

182. As part of their promotional efforts and in response to customers' concerns, defendants routinely furnish customers and potential customers with an analysis that purports to explain why defendants' intermediary transactions are not the same as or substantially similar to the listed transactions described in Notice 2001-16. Defendants falsely and/or fraudulently contend that their intermediary transactions "fall outside of the parameters [of Notice] 2001-16," as Klink did in an October 25, 2005 email to a customer's representatives, who were an attorney affiliated with the Locke Liddell & Sapp, LLP firm in Texas and an employee of a Dallas-based private equity firm. Defendants also routinely offer their customers a "summary comparative analysis" that expands on this false assertion that defendants' intermediary transaction is not a listed transaction.

183. The "summary comparative analysis" contains numerous false and/or fraudulent statements that defendants know and have reason to know are false and/or fraudulent statements, including the following: (1) defendants claim that "there is no pre-arranged plan between stock buyer, the selling shareholder, the target corporation and the asset buyer. The asset sale takes place independent of stock buyer and the stock purchase"; (2) defendants claim that "[c]ash is left in the target corporation to engage in this new line of business on a going-forward basis"; (3) defendants claim that "[t]here are no confidentiality provisions regarding the tax aspects of stock

buyer's stock purchase transactions"; and (4) "the target corporation is solvent" and "holds funds that are well in excess of any potential tax liability of the target corporation at the time of the stock purchase," and "[t]his helps protect the selling shareholders from assertions of transferee liability in connection with the stock purchase."

184. These statements comprising the "summary comparative analysis" are false and/or fraudulent. First, by design, there is a pre-arranged plan between the defendants (as purchaser of the target corporation), their customers who first sell their corporation's assets and then their stock in the target corporation, and the asset sale and the target corporation sale. Second, the cash left in the target corporation is used through fees for sham services to pay defendants and their associates who help facilitate the intermediary transaction. By design, after these pay-outs, there is no money left in the target corporation to start or run a business. Third, defendants decline to provide information to sellers regarding the company's "new line(s) of business" following the purchase of the target corporation; they describe such information as being "proprietary and confidential," as Klink did in a September 30, 2005 email to the representative for the Alicia Holdings customer. Fourth, the summary comparative analysis is misleading because it suggests that the target corporations will have adequate funds to pay corporate income taxes and that defendants intend to pay these corporate taxes, thus insulating customers from transferee liability. In actuality, defendants specifically design the intermediary transaction so that the corporations do not and cannot pay income taxes, thus exposing their customers to transferee liability.

185. In another email, dated May 19, 2006, concerning the Searington transaction involving a Washington D.C.-based office building (discussed below), Klink falsely assured his

customers' counsel, an attorney with Loeb Block & Partners LLP in New York, that "[f]or a number of reasons that we have discussed in the past with you, we are very comfortable that this is not a listed transaction and have performed an ongoing internal analysis of this issue." Klink also referred that counsel to representations and warranties in the proposed Stock Purchase Agreement which state that neither party received advice that the stock sale qualifies as a reportable transaction, including a listed transaction.

186. Another standard promotional email that defendants, through ASI, have regularly sent to customers and potential customers announces that ASI is "actively seeking situations in which a buyer desires to purchase only the assets of a company and not the stock." This solicitation falsely and fraudulently claims that "ASI create[s] business-driven transactions that also minimize corporate-level tax problems by eliminating the economic and structural gaps between sellers and buyers in stock versus asset sale transactions."

187. In actuality, ASI's transactions are only tax-driven and not business-driven. Defendants' ASI solicitation email also fails to mention that defendants' intermediary transaction is unlawful, is a listed transaction, is disregarded under several judicial doctrines and violates numerous Code provisions.

188. In another example, Grodsky sent a November 18, 2005 email to a customer's representatives, who were affiliated with Grant Thornton, an accounting firm. The customer owned commercial real estate interests in Hurst, Texas. Grodsky's email explained that "we need to complete the stock purchase by November 29th [of 2005] in order for Buyer to have sufficient time this year to re-engineer [the target corporation] into the new line of business as we do when we acquire companies." Grodsky made a nearly identical statement in an October 9,

2006 email to customers and their representatives who were selling their interests in Indian Creek, a vineyard in California (discussed below). This statement has been Grodsky's standard explanation as to why all stock sales for his customers need to happen quickly and why there is little, if any, time to negotiate the terms of the stock purchase agreements that defendants draft.

189. Grodsky's statement in his November 18, 2005 email, like so many similar statements he has repeatedly made to customers and their representatives, is false and/or fraudulent. The buyers of each target corporation, namely defendants through their sham entities, have no intention of actually re-engineering any target corporation into a viable business, and thus, defendants do not require a certain amount of time to undertake this task. In actuality, the real purpose for defendants' urgency is to ensure that the DAT tax scheme is in place before the end of the tax year so that taxes can be evaded.

190. Similarly, in an April 18, 2006 email to an attorney with the Kutak Rock, LLP firm who represented a customer who owned a company with real estate holdings in Arizona, Grodsky falsely and fraudulently stated that "Buyer is keeping the Company open after the stock purchase and will file the tax returns of the Company on a go-forward basis." In actuality, defendants keep the target corporations only nominally open, as defendants routinely drain the target corporations' funds and never intend for the target corporations to be viable business endeavors. Moreover, defendants do not file tax returns that accurately reflect each target corporation's tax liabilities.

191. Grodsky also has made false and/or fraudulent statements that inaccurately tout the tax benefits of the intermediary transaction, as he did in an October 11, 2006 email to his customers concerning the Indian Creek transaction. Grodsky provided the Indian Creek

customers with a "spreadsheet setting forth the calculations pursuant to which the cash portion of the purchase price [for Indian Creek's stock] is set," and noted that "Buyer's [defendants'] premium paid to the selling shareholder is $711,889 above what would otherwise be realized." The so-called $711,889 premium offered by Grodsky is, in fact, 50% of the approximately $1 million of federal and $270,000 of state corporate income taxes evaded as a result of the transaction. Here, Grodsky's statement that this $711,899 is a "premium" is false and/or fraudulent because it implies falsely that Grodsky is splitting the corporate income tax costs with the customer, and that Grodsky is intending to pay the corporation's income taxes.

192. As part of defendants' promotion efforts, Block also has spoken at conferences where he promotes intermediary transactions, including at the New England Business Brokers Association meeting held on October 4, 2006. The simple description of that speaking engagement encompassed false and/or fraudulent statements. During that association's meeting, Block made a presentation titled "Cutting the Tax Penalty of an Asset Sale by a 'C' Corp. – How to reduce tax penalties by up to 50% vs. a stock sale." Specifically, the brochure advertised that Block "will discuss ways that sellers of C corporations can have significant (up to 50%) tax savings." Block's promotion never mentions that the intermediary transaction is illegal.

193. Klink and Block have been promoting their intermediary transactions using false and/or fraudulent statements even before they founded ASI. For example, in a March 22, 2002 email that Block sent to a potential customer's attorney, he explained the intermediary transaction that Fortrend promoted, which was virtually identical to the transaction that Klink and Block have subsequently promoted through ASI: "Fortrend International LLC will purchase the stock of the C corp. after the assets are sold. Fortrend then contributes into the C corp.

certain assets to offset the C corp. gain while keeping the company open for a period of 4-5 years. In addition, investing our own money into the C corp. through a debt-collection business which has historically yield[ed] a 25-30% return. Thus, creating additional business purpose."

194. In actuality, just like the promotional emails defendants subsequently sent to their customers and potential customers, the email sent through Fortrend International also was false and/or fraudulent. The purported debt-collection business was a sham business that yielded no profit and had no business purpose. Defendants continued in this vein making false and/or fraudulent statements long after this 2002 email was sent to a potential customer's attorney.

195. Klink, Block and Grodsky have routinely made false and/or fraudulent material statements in connection with their organizing, selling and helping to establish their intermediary transaction tax schemes. Defendants know and have reason to know that all of these material statements are false and/or fraudulent. Klink and Grodsky are attorneys who have substantial experience with corporate transactions, and Block has extensive experience in the financial services sector.

196. In addition, Klink, Block and Grodsky also have caused others, including individuals affiliated with ASI or one or more of defendants' other companies, to make false and/or fraudulent statements in connection with organizing, selling and helping to establish their intermediary transaction tax schemes. Klink, Block and Grodsky each know and have reason to know that the material statements about tax benefits that they have caused others to make are also false and/or fraudulent statements.

DEFENDANTS HAVE PREPARED OR HELPED TO PREPARE NUMEROUS DOCUMENTS THAT HAVE CAUSED AN UNDERSTATEMENT OF TAX LIABILITY IN VIOLATION OF I.R.C. § 6701

197. In connection with their promotion of the intermediary scheme, defendants have prepared and helped to prepare numerous documents that have been used in connection with a material matter arising under the internal revenue laws. These documents or portions of these documents have caused the understatement of federal corporation income tax liabilities. Defendants know that these documents or portions of these documents, if used, would result in an understatement of federal corporation income tax liability.

198. Defendants have drafted and helped to draft numerous documents that implement the intermediary transaction scheme and cause the target corporation to understate its federal income tax liabilities. Defendants knew that these documents would result in the understatement of federal corporation income taxes.

199. For example, Klink regularly drafts the stock purchase agreements that govern the purchase terms and price that defendants pay for target corporations in ASI-promoted intermediary transactions. These agreements are crucial to the intermediary transaction, as they govern its terms and induce customers to participate in the tax-fraud scheme. In an August 31, 2005 email to the customer who owned Mt. Royal Plaza in New Jersey (discussed below), Klink congratulated the customer on “a successful asset sale,” and stated that he “will draft and circulate a preliminary version of the Stock Purchase Agreement,” which became the final stock purchase agreement that governed the terms of the stock sale, including the price that defendants paid for the target corporation’s stock.

200. Similarly, on December 8, 2006, Grodsky sent an email to representatives for his customers who owned the Searington target corporation (discussed below), in anticipation of an imminent stock sale. Grodsky noted that "Chuck [Klink] will be sending you the final copies of . . . documents later today," including a copy of the "Klink & Associates Legal Opinion," along "with a final version of the SPA [Stock Purchase Agreement] with the final purchase price, note amount, wire instructions, etc."

201. Stock purchase agreements define the terms of the intermediary transaction, including the price that defendants agree to pay their customers for the target corporation's stock, accounting for the corporate income tax liabilities that defendants falsely and fraudulently promise to pay. Stock purchase agreements are used in connection with a material matter arising under the internal revenue laws. Defendants draft and help prepare these agreements, and they know that these documents will result in the understatement of federal corporation income taxes.

202. Klink also has drafted a purported legal opinion letter and furnished his customers with copies of this document. This legal opinion letter purports to provide legal support for the intermediary transaction, even though the transaction is not legal. This opinion letter is used in connection with a material matter that arises under the internal revenue laws, as the letter asserts falsely and/or fraudulently that the intermediary transaction is a legal way to avoid payment of federal corporation income taxes.

203. Klink, Block and Grodsky also prepare sham engagement letters that purport to define the parameters of legal services or consulting services that each defendant will provide for each target corporation as part of the intermediary transaction tax scheme. The payments of consulting and legal fees pursuant to these letters are payments for sham services that deplete the

target corporations' funds. These letters are used in connection with a material matter arising under the internal revenue laws. Ultimately and by design, none of the target corporations has adequate funds to pay its federal corporation income taxes.

204. For example, Block, as president of the intermediary company, Spaco, LLC, prepared and then executed a September 5, 2005 engagement letter with Klink, the president and sole partner in his law firm, Klink & Associates, for the purported provision of "corporate legal services in connection with the proposed acquisition of Mt. Royal Plaza, Inc. . . by Spaco, LLC." The engagement letter states that Klink will be paid $300 per hour for his legal work, and the total legal costs "should be somewhere in the range of $20,000 to $30,000." Klink submitted an October 18, 2005 invoice for legal work that he purportedly performed for a total of $30,000; he provided no detail of the work he purportedly performed.

205. Similarly, Grodsky, as the member of the Grodsky Law Firm, and Block, in his capacity as president of Actol, LLC, an intermediary company, each helped to prepare and then executed a sham October 2, 2006 Acquisition Services and Management Agreement concerning the Searington transaction (discussed below). The agreement provides that Grodsky's firm "has provided certain advice, expertise and professional services to Actol with respect to various preliminary matters relating to the Acquisition . . . and the proposed management and operations of Searington after the Acquisition." The agreement also provides that Grodsky's firm will receive $100,000 for its acquisition and management services in connection with the Searington transaction.

206. Klink, Block and Grodsky have prepared or assisted in the preparation of sham legal services and consulting services agreements that are used to help implement their

intermediary transactions. These agreements have depleted the target corporations of funds and caused the target corporations to understate their federal income tax liabilities. Defendants knew that these documents would result in the understatement of federal corporation income taxes.

207. When defendants purportedly re-engineer the target corporations, their intermediary corporations execute trust agreements and sub-trust agreements that allocate a portion of distressed assets to each target corporation. These agreements are used in connection with a material matter arising under the internal revenue laws, as the agreements allow for the purported allocation of Brazilian debt, which causes each target corporation to purport to offset gains and reduce or evade altogether the payment of taxes. Defendants have drafted and executed numerous trust and sub-trust agreements, and they knew that these documents would result in the understatement of federal corporation income taxes.

208. For example, Grodsky, in his capacity as trustee of the Stedco Trust, helped to prepare and then executed the trust agreement that created the Stedco Trust on May 26, 2006. Grodsky, in his capacity as trustee of the Stedco Trust, also executed the December 12, 2006 2006-D Supplement to Trust Agreement (sub-trust agreement) that allocated a portion of distressed assets to Searington, LLC, which was the designated beneficiary. Block, in his capacity as a member of Searington also helped to prepare and then executed this sub-trust agreement.

209. Block subsequently helped to prepare and executed a document, dated December 29, 2006, that purports to be a Written Consent of the Operating Manager of Searington, LLC to write-down certain loans as bad debt. Pursuant to this sham consent, Searington wrote off

72.25% of one portfolio of distressed assets allocated to Searington, and Block executed this agreement in his capacity as operating manager of Searington.

210. As part of the intermediary transaction scheme, defendants have prepared or assisted in the preparation of trust agreements, sub-trust agreements and purported consent agreements that are used to enable each target corporation to offset its gains and reduce or eliminate its tax liabilities. These documents have caused target corporations to understate their federal income tax liabilities, and defendants knew that these documents would result in the understatement of federal corporation income tax liabilities.

211. In connection with defendants' purported re-engineering of the target corporations that they acquire through intermediary companies under their control, defendants also cause the target corporations to enter into sham wine-trading services agreements which have standard language that defendants have drafted. For example, Block, in his capacity as president of Mt. Royal, Inc., the New Jersey-based target corporation, and Klink, in his capacity as president and member of Carpevino, Inc., executed a sham wine-trading services agreement.

212. The agreement allows Carpevino to acquire and dispose of "certain wine on behalf of " Mt. Royal, and Carpevino also is tasked with "assum[ing] the role of manager and trader for such wine activities" for Mt. Royal. This purported wine-services agreement requires that Mt. Royal pay Carpevino a monthly fee for purported services rendered. In this way, Mt. Royal's funds are further depleted and transferred to defendants, and Mt. Royal is able to claim additional improper deductions on its tax return.

213. Klink and Block have prepared or assisted in the preparation of wine-trading services agreement that are used as part of the intermediary transactions and that have caused

target corporations to understate their federal income tax liabilities. Defendants knew that these documents would result in the understatement of federal corporation income tax liabilities.

Examples of Defendants' Intermediary Transaction Tax Schemes

Searington

214. In or around May 2006, defendants promoted their intermediary transaction scheme to representatives of Zinnia Capital, Limited (Zinnia) for the purchase of all of the stock of Zinnia's subsidiary, Searington Limited, which was a member of Searington, LLC (Searington). Searington intended to sell its primary asset, a 345,000 square foot, twelve-story office building located at 1401 H Street Northwest in Washington, D.C.

215. Zinnia was a British Virgin Islands entity that was capitalized with the shares of Searington Limited through an offshore trust. The settlor of that trust and an ultimate owner of the H Street Building is a citizen of Hong Kong who, on information and belief, resides outside the United States.

216. Defendants advised the Zinnia customers and their representatives about the intermediary transaction scheme before the sale of the Washington, D.C. building for $205 million.

217. On September 29, 2006, the H Street office building was conveyed to a buyer, and the sale resulted in a capital gain of $52.7 million for Searington.

218. As part of the intermediary transaction scheme, defendants, acting through Oceanus, incorporated Actol LLC (Actol) in Nevada to serve as the intermediary entity in this transaction. The agreement incorporating Actol names Block as president and Grodsky as vice president, treasurer and secretary of the LLC.

219. Following its establishment, Actol, through its officers, then entered into self-dealing retainer agreements with Klink & Associates, Blairington, and Grodsky's law firm to provide purported services to implement the stock sale. Specifically, Actol contracted with Klink & Associates "to perform all legal work," with total fees estimated to exceed $200,000. Actol contracted with Blairington for purported consulting services, also for fees estimated to exceed $200,000. Actol signed a second agreement with Blairington that promised to pay Blairington an additional $1 million acquisition advisory fee and $432,000 for "management and consulting advice and services as well as providing Searington LLC with candidates to serve as officers and representatives." Finally, Actol contracted with the Grodsky Law Firm for a $100,000 fee for Grodsky to perform purported legal and other professional services.

220. Defendants offered no evidence that they ever performed the services contracted for in these agreements. Rather, the consulting and legal services agreements that defendants drafted and executed between Actol and Klink & Associates, Blairington, and the Grodsky Law Firm were shams, designed to drain funds from Searington and transfer the funds to defendants, ultimately leaving Searington with sham tax deductions and insufficient assets to satisfy its corporate tax obligations once the IRS discovered and unraveled the fraud.

221. Actol financed the stock purchase through several promissory notes, including notes in favor of Dalmar ($300,000), one of Grodsky's intermediary companies, Block ($500,000) and Klink ($1.7 million). Under the terms of the promissory notes in favor of Dalmar, Block and Klink, Actol would pay interest as well as "facility fees" of $6,750 to Dalmar, $11,250 to Block and $38,250 to Klink. Defendants' business associates, at defendants'

request, also financed the stock sale. Additional financing for the stock sale was obtained by a $28.6 million promissory note issued by defendants' company Actol in favor of Zinnia.

222. Defendants caused Actol to purchase the Searington Limited stock for $33.6 million in cash, and the transaction closed on or about December 11, 2006. At the time of the closing, Searington Limited was the sole member of Searington, LLC, whose only asset was $44.6 million in cash assets, per defendants' requirements for the transaction.

223. After defendants paid $33.6 million to Zinnia and made subsequent payments to themselves and their companies, Searington lacked adequate funds to pay its tax obligations, contrary to defendants' statements made to the Zinnia customers and their representatives while promoting the transaction.

224. As part of the intermediary transaction, defendants in the twenty remaining days of 2006, purported to re-engineer Searington by turning it into a debt-collection business. To this end, during these twenty days, defendants endeavored to give the appearance that they were re-engineering the corporation into a bona fide debt collection business. Defendants (1) took control of the corporation; (2) became the corporation's officers; (3) executed a sub-trust agreement that made Searington the beneficiary of certain allocated Brazilian retail debt; (4) turned the corporation into an entity tasked with collecting this debt; (5) purported to ascertain how much of this debt could be collected; (6) purported to collect some portion of this debt with the help of a third party; (7) purported to determine what percentage of this debt could not be collected; and (8) claimed this percentage of uncollectable debt as a write-off for so-called bad debt. In short, during these twenty days, defendants implemented a DAT tax scheme in order to unlawfully offset Searington's sizeable gains received from the sale of its real estate holding.

225. In December of 2006, defendants executed a contribution agreement with a Brazilian retail outlet, SMS Technologia Electronica LTD (SMS), for the contribution of its retail debt to Searington.

226. Defendants used the Stedco Trust, of which Grodsky was the trustee, and three sub-trusts, the 2006-C, 2006-D, and 2006-E sub-trusts, to allocate $32.5 million, $15 million, and $2.5 million of SMS retail debt to each sub-trust, respectively. Each sub-trust agreement identifies Searington as one-hundred percent beneficiary of "[a]ll right, title and interest in" the distressed assets.

227. In addition, Klink and Block caused their company, Finamco LLC, to contract with Grodsky as trustee of the Stedco Trust to manage collections for the three debt portfolios in exchange for 25 percent of collections. Under a Collection Services Agreement between Finamco and the Stedco Trust, Finamco was purportedly "engage[d]" to provide "professional services," including "administrative and collection services" for assets of the Stedco Trust, to "assist in managing the portfolios of accounts" that comprise the Trust assets "to help maximize collection and recovery," and to provide summary collection reports.

228. On December 11, 2006, Block, as operating manager of Searington, executed a written consent for the company to enter into the debt-collection business based upon his bogus "determin[ation] that, with the assistance of outside legal, accounting and financial advisors, the Company may, over time, be able to realize significant profits in such business activities." Searington's purpose for entering into the debt-collection business was not to "realize significant profits," but to evade its tax obligations resulting from the September 29, 2006 asset sale.

229. On December 12, 2006, Block re-domiciled Searington from Washington, D.C. to the State of Nevada.

230. A mere ten days after Searington entered the debt-collection business via a purported resolution, Grodsky, by correspondence dated December 21, 2006, informed Multicred that Searington required a letter with a "rough estimate" as to the "collectability of the loans that have been allocated to" each sub-trust. On information and belief, Multicred never responded to Searington's query, let alone quantified the collectability of the loans.

231. Nevertheless, on December 29, 2006, only a few weeks after entering the supposedly profitable debt-collection business and contracting with a debt-collection agent, Block, as an officer and director of Searington, determined that "it would be in the best interest of the corporation [Searington] to treat a large portion" of the debts held by the Stedco sub-trusts as bad debt before the close of the 2006 fiscal year.

232. Block authorized Searington to write-down nearly all of the $50 million of Brazilian retail debt that defendants had purportedly allocated to the company as part of its entrance into the debt-collection business. Ultimately, the total write-downs taken by Searington were 78.5% for the $32.5 million debt portfolio ($25,512,500), 77.25% for the $15 million debt portfolio ($11,587,500), and 76% for the $2.5 million debt portfolio ($1.9 mill), totaling $39 million.

233. On its federal income tax return for 2006, signed by Grodsky as an officer of Searington, the company reported a $52.7 million capital gain, $39 million in purported bad debts and $14.6 million as other deductions. A sizeable percentage of these other deductions pertained to the purported management fees and fees for purported professional and legal

services that defendants paid to themselves. Searington's reported 2006 federal taxable income was negative $171,528, with a $6,769 tax refund purportedly due to the company. In short, Searington paid no income taxes on its $52.7 million capital gain.

Mt. Royal Plaza

234. In or around July of 2005, defendants, through ASI, promoted an intermediary transaction to representatives of Mt. Royal Plaza, Inc. (Mt. Royal), a New Jersey corporation, for the purchase of all stock of the company. Defendants' customers, who were the stockholders of Mt. Royal and heirs to the Estate of Dominick Borelli, intended to sell the company's principal asset, real estate including office buildings located in East Greenwich, New Jersey.

235. On July 16, 2005 – shortly after defendants conferred with the Mt. Royal customers about the intermediary transaction – the accountant for these customers sent Klink financial information that he had requested, namely information about the anticipated asset sale, the corporation's tax basis in those assets, the corporation's anticipated cash flow and its contingent liabilities.

236. The Mt. Royal customers also retained counsel to represent them in the transaction. To this end, their attorney, who had conferred with Klink about the intermediary transaction, analyzed ASI's proposed stock purchase in an August 29, 2005 letter, noting that ASI was intending to purchase Mt. Royal "while the corporation is 'pregnant' with a tax liability from the sale of the corporation's assets," but "[c]learly, at the time of the sale, the Corporation has liquid assets sufficient to satisfy its tax liability." The attorney advised the Mt. Royal customers that their tax compliance responsibilities would transfer to defendants post-acquisition, and, therefore, "[i]t will be important to review the stock sale agreement to ensure that it assigns to

the purchaser all of the Corporation's tax compliance responsibilities and that it relieves the historical shareholders, officers and directors of the Corporation of those responsibilities." If such contractual protections were in place, the attorney concluded that "I do not think that it is necessary for us to satisfy ourselves that the purchaser's plans with respect to the utilization of tax benefits available to it are watertight."

237. The Mt. Royal customers and defendants agreed to delay additional negotiations for the stock sale until Mt. Royal sold the New Jersey property. Counsel for the Mt. Royal customers explained in his August 2005 analysis that "Chuck [Klink] stated, and I agree, that detailed discussions with respect to the Stock purchase should not be initiated before the sale of the corporate assets. I believe Chuck [Klink] may be concerned with a step transaction argument that could impact his post acquisition transactions." The customers' attorney agreed that "[a]t this point, I will step back and wait to be contacted after the asset sale is completed."

238. On August 31, 2005, Mt. Royal sold its property for $1.6 million, with a reported capital gain of more than $1 million.

239. On September 30, 2005, ASI and the Mt. Royal customers executed a letter of intent for the purchase of all issued and outstanding stock of Mt. Royal. Among its terms, ASI agreed to purchase Mt. Royal's stock for a sum initially calculated at $927,137 on condition that "at least $1,174,519" in cash assets remain in the company, and Mt. Royal would "have no liabilities other than income tax liabilities due for the current fiscal year." The defendants, through ASI, also falsely stated that they "shall satisfy any obligations for income taxes, for the current fiscal year of the Company and all future fiscal years of the Company."

240. In September and October of 2005, Klink and Block executed a series of non-arm's-length agreements with Spaco, the intermediary company that purchased Mt. Royal's stock. Block served as Spaco's president and secretary, and Klink was vice president and treasurer.

241. Spaco engaged ASI to provide Spaco with "acquisition services" and "management services" in connection with Spaco's acquisition of Mt. Royal and "advice and services to assist Spaco and Mt. Royal in connection with the re-engineering of Mt. Royal into such new business operations," "candidates" to serve as officers and directors of "Spaco and/or Mt. Royal," and "general management and consulting advice and services to Spaco and Mt. Royal to assist in ongoing operations." ASI was to receive 3.5% of the "aggregate value" of Mt. Royal's assets for its "Acquisition Services" and $3,500 for "Management Services." Klink signed the agreement as president of ASI, and Block signed as president of Spaco. Spaco also contracted with Klink & Associates "to perform all legal work as requested and directed by [Spaco]" at an hourly rate of $300 per hour, with total fees estimated to exceed $20,000. Block signed the agreement with Klink & Associates as president of Spaco, and Klink signed the agreement for his firm. Finally, Spaco contracted with Block's consulting firm, Blairington, to provide "consulting services in connection with the proposed acquisition" at an hourly rate of $300 per hour, with total fees estimated to exceed $20,000. Klink signed the agreement as vice president of Spaco, while Block, the president of Spaco, signed as president of Blairington.

242. These purported contracts between Spaco and Klink, Block and their companies did nothing more than transfer funds from Mt. Royal to Klink and Block, thus leaving the corporation with insufficient assets to satisfy its federal tax obligations.

243. On October 12, 2005, defendants, through their intermediary company Spaco, and the Mt. Royal customers executed a Stock Purchase Agreement for the sale of all Mt. Royal stock for $933,750, funded by $925,000 of promissory notes in favor of Klink and at least one other business associate and pledge agreements between Spaco and each lender.

244. Among the terms of the Stock Purchase Agreement, defendants falsely represented, that: (a) "No representation or warranty by Buyer contained in this Agreement and no schedule, certificate or exhibit required to be furnished to Sellers pursuant to this Agreement contains or will contain any untrue statement of a material fact or omits or will omit any material fact necessary in order to make the statements and information contained therein not misleading"; (b) "The representations and warranties of Buyer contained herein shall be true and correct in all material respects as of the date of this Agreement and shall be true and correct in all material respects on the Closing Date"; (c) "[E]xecution, delivery and performance by Buyer of this Agreement ... do not contravene in any material respect any Requirement of Law"; and (d) "For a period of three (3) years following the Closing Date, Buyer will cause the Company to: (i) maintain its corporate existence and not be dissolved, liquidated, or otherwise wound up; and (ii) engage in and maintain an active trade or business."

245. The same day the Stock Purchase Agreement took effect, as president and secretary of Spaco, Block appointed himself the sole director of Mt. Royal. As sole director, Block, in turn, appointed himself president of Mt. Royal and Klink as treasurer and secretary.

246. On October 14, 2005, as sole director of Spaco, Block authorized repayment of the promissory notes in favor of Klink and at least one other business associate, including payment

of fees, on information and belief, using a portion of the $1.2 million of cash assets remaining in Mt. Royal following the stock sale.

247. By defendants' design, after the $933,750 payment to their customers for the purchase of the shares of stock, as well as the payments to defendants' business associates, Mt. Royal no longer had sufficient assets to pay its corporate income taxes.

248. Also on October 14, 2005, Block executed a written consent authorizing the purported re-engineering of Mt. Royal into the debt-collection business. The consent falsely states that the purpose of entering the debt-collection business is to "realize significant profits in such business activities." The actual reason for Mt. Royal's entry into the debt-collection business was to evade Mt. Royal's tax obligations resulting from the August 31, 2005 asset sale.

249. On October 17, 2005, by written consent, Mt. Royal purportedly entered into the wine-trading business after Block, as director, reviewed "proposals" to enter into this "business line" and determined that Mt. Royal may "be able to realize significant profits in such business activities." Three days later, Mt. Royal executed a Wine Trading Services Agreement with Carpevino. Block signed the Wine Trading Services Agreement as president of Spaco, and Klink signed as president and member of Carpevino.

250. Pursuant to the terms of the Wine Trading Services Agreement, in exchange for fees provided by Mt. Royal, Klink agreed to become Mt. Royal's "service provider" in the "wine trading business," supplying services that include "purchase, sale and collection related services" using Mt. Royal's funds, "managing" portfolios of wine, and providing written reports "regarding the Wine Assets" to Mt. Royal at least every six months. Klink purchased wine with Mt. Royal funds and stored that wine at his home.

251. The Wine Trading Services Agreement executed by Klink and Block was not designed for Mt. Royal to realize "significant profits," but rather to transfer funds held by Mt. Royal to Klink.

252. On November 10, 2005, three individuals executed a trust agreement that formed the ARB Trust: the president of Oceanus (a relative of Klink's wife); John Rogers, the manager of Sugarloaf and Warwick Trading, and Grodsky, the trustee. That day, Grodsky, Warwick Trading, and Klink as secretary and treasurer of Mt. Royal, established a 2005-A Supplement to Trust Agreement that assigned to Mt. Royal a 100 percent interest in a debt portfolio of 4,814 loans with a claimed aggregate value of $1.2 million.

253. Defendants understood that the $1.2 million of debt contributed to Mt. Royal had no value or was near worthless. Defendants acquired the debt not to make a profit but so that Mt. Royal could evade payment of its 2005 corporate tax liability by writing off the debt.

254. To purportedly administer collection activities for the debt portfolio, Grodsky, as trustee of the ARB trust, entered into an "Agreement for Collection Services" with Multicred on November 11, 2005 and a "Collection Services Agreement" with Finamco on December 1, 2005.

255. On December 20, 2005, purportedly at Mt. Royal's request and as trustee of the ARB Trust, Grodsky informed Multicred that Mt. Royal required "a letter" with a "rough estimate" as to the "collectability of the loans that have been allocated to the 2005-A Sub-Trust." On information and belief, Multicred never provided a "rough estimate" as to the "collectability of the loans."

256. On December 29, 2005, Block, after having purportedly "received the advice of Multicred Investimentos Ltd., in its capacity as the collection agent for certain loans in which the

Corporation holds a beneficial interest," determined that it would "be in the best interest of the corporation to treat a large portion" of the debt held by the ARB Trust as "bad debt" before the close of the 2005 fiscal year. Block authorized Mt. Royal to write-down 82.27% of the debt portfolio held by the 2005-A sub-trust.

257. On its federal income tax return for 2005, Mt. Royal reported over $1 million in capital gains, $905,000 in bad debts and $241,076 as other deductions, including $133,063 for legal and professional service fees, most of which was paid to defendants and their businesses. Mt. Royal reported $5,490 in federal income on its 2005 federal income tax return on which $824 in taxes were due, even though Mt. Royal earned more than $1 million in capital gains from the sale of its assets.

258. As of December 31, 2007 – more than two years after defendants authorized Mt. Royal's purported good faith entry into the debt-collection business – a mere $1,912 or 0.16% of the $1.2 million conveyed to the 2005-A sub-trust had been reported as collected and received by Mt. Royal.

Alicia Holdings

259. In November 2004, defendants, through ASI, promoted an intermediary transaction to representatives of the owner of Alicia Holdings, Inc. (Alicia Holdings). Defendants' customer, who was the owner of Alicia Holdings, planned to sell the corporation's principal asset, a six-building office campus in Laguna Hills, California.

260. At this time, a tax advisor for the Alicia Holdings customer began discussions with defendants about their proposed intermediary transaction and about whether that transaction was prohibited by Notice 2001-16. Defendants falsely assured the Alicia Holdings customer and his

representative that the defendants' intermediary transaction did not fall within the scope of Notice 2001-16.

261. Defendants also provided the Alicia Holdings customer and his representative with defendants' standard "Summary Comparative Analysis" that purports to differentiate ASI's proposed purchase of Alicia Holdings' stock with the reportable transaction under 2001-16.

262. In response to queries from the Alicia Holdings customer and his representative, defendants falsely described the intermediary transaction: "On a basic level, Stock Buyer's [defendants'] transactions are business-driven transactions that have a substantial profit motive." The claimed basis for a profit motive was that defendants purportedly "re-engineer[] [the acquired company] into a new line of business from which it is expected that substantial revenues will be generated."

263. On or about December 3, 2004, defendants provided the Alicia Holdings customer and his representative with the following items relating to the proposed intermediary transaction: (1) a preliminary stock purchase proposal between ASI and Alicia Holdings; (2) contact information for ASI references involved in previous intermediary transactions promoted by defendants; (3) tables illustrating the "premium" the Alicia Holdings shareholder would receive on the stock sale if he completed a stock sale with ASI compared to a liquidation of the company following an asset sale; and (4) the "SUMMARY COMPARATIVE ANALYSIS" purporting to differentiate an ASI purchase of Alicia Holdings' stock and a reportable transaction under 2001-16.

264. On July 1, 2005, Alicia Holdings entered into a $22.2 million purchase and sale agreement for the sale of its Laguna Hills office campus, the corporation's principal asset, yielding $10.4 million in capital gains.

265. After the asset sale, defendants furnished the Alicia Holdings shareholder and his tax advisor and attorney with a copy of their proposed stock purchase agreement, which among other things, included a provision that required that neither defendants nor the Alicia Holdings customer report the intermediary transaction to the IRS as a reportable transaction. *See infra* at ¶78.

266. On September 30, 2005, counsel for the Alicia Holdings customer and Klink exchanged e-mails addressing "the major concern" the Alicia Holdings customer and his counsel had "regarding the proposed transaction." The customer's attorney wrote as follows: "I need to understand the economics of the transaction as far as the Buyer is concerned. As I understand it, the corporation will have cash equal to the difference between $16.4MM (cash held by the company) and the purchase price of $14.825MM ($100K over amount in letter of intent because cash is more than $16.3MM). The difference is $1.575MM. However, the company owes approximately $4MM in taxes for 2005 which the Buyer is to pay. According to my math, this leaves the Buyer in the hole to the tune of $3.25MM. What am I missing?" Klink responded to this query and acknowledged his intention to offset the target corporation's gains:

> As far as raw economics on the face of things, you have things true on rough numbers. The "missing" part is that buyer will be able to substantially reduce/offset the result of the built-in gains by means of the new line(s) of business that are involved once we re-engineer the company post-acquisition. We keep the corporation open for a significant period of time and file all necessary tax returns to report the gains from ongoing operations.

Klink also explained that the defendants' purported method for re-engineering the target corporation's business is "proprietary and confidential":

> You correctly read from the [Stock Purchase Agreement] that Buyer is responsible for satisfying any and all liabilities of the company on a go-forward basis, including any taxes due from income/gains recognized during 2005. Seller is not involved in or responsible for Buyer's post-acquisition tax planning or operations of the corporation. We understand that seller needs to be comfortable that Buyer will take care of its post-closing obligations but certain aspects of how such things take place are proprietary and confidential. We are used to folks asking and are happy to talk in general terms about such things.

267. On October 7, 2005, in preparation for the purchase of Alicia Holdings' stock, Oceanus entered into a limited liability agreement establishing the intermediary company Spefiaco in Nevada and naming Klink as vice president, treasurer, and registered agent and Block as president and secretary.

268. Spefiaco also executed agreements with: (1) ASI to provide "Acquisition Services" in exchange for 2.75% of the aggregate value of Alicia Holdings' assets at the time of the stock sale and $17,500 for "Management Services"; (2) Klink & Associates to "undertake all legal work ... in order to complete the Acquisition" of Alicia Holdings for hourly fees estimated to total $50,000 to $100,000; and (3) Blairington to "provide consulting services" to Spefiaco in exchange for a $75,000 to $125,000 fee, based on Block's hourly billable rate.

269. These purported contracts between Spefiaco and Klink, Block and their companies did nothing more than drain funds from Alicia Holdings and transfer them to Klink and Block, thus leaving the corporation with insufficient assets to satisfy its federal tax obligations once the IRS unraveled the fraud and assessed proper tax liabilities.

270. On November 1, 2005, Spefiaco and Alicia Holdings executed a Stock Purchase Agreement for the sale of all Alicia Holdings stock for $14.2 million. Per the conditions of the Agreement, $15.8 million in cash remained in the corporation. The same day, Block appointed himself the sole director of Alicia Holdings and, as sole director, appointed himself president of Alicia Holdings and Klink its treasurer and secretary.

271. On November 2, 2005, as sole director of Spefiaco, Block authorized payment of expenses incurred from the acquisition of Alicia Holdings.

272. By defendants' design, Alicia Holdings no longer had sufficient assets to pay its corporate income tax liability after defendants paid themselves and their companies for purported services and after defendants repaid their lenders.

273. Also on November 2, 2005, Block executed a written consent that purported to authorize Alicia Holdings' entry into the debt-collection business.

274. On November 4, 2005, by written consent, Alicia Holdings also purportedly entered into the wine-trading business and subsequently executed a Wine Trading Services Agreement with Carpevino. Block signed the Wine Trading Services Agreement as president of Spefiaco, and Klink signed as president and member of Carpevino.

275. The Wine Trading Services Agreement executed by Klink and Block was not designed for Alicia Holdings to realize "significant profits," but rather to drain funds from Alicia Holdings and transfer them to Klink.

276. On November 10, 2005, pursuant to a 2005-A Supplemental Trust Agreement to the already-established DARB Trust, Alicia Holdings received 100 percent ownership of a Brazilian debt portfolio of 38,742 loans purportedly valued at $11.6 million. Rogers of West End Fund

and Klink on behalf of Alicia Holdings signed the 2005-A Supplement To Trust Agreement. Grodsky was the trustee for this sub-trust.

277. Defendants understood that the purported $11.6 million of debt contributed to Alicia Holdings had no value or was near worthless. Klink and Block acquired the debt to claim a bogus bad-debt deduction to eliminate Alicia Holdings' tax liability for 2005, rather than for any legitimate business purpose.

278. In a December 19, 2005 letter, purportedly sent at the request of Alicia Holdings, the trustee of the 2005-A sub-trust requested a "rough estimate" as to the "collectability of the loans that have been allocated to the 2005-A Sub-Trust." On information and belief, Multicred never provided a "rough estimate" as to the "collectability of the loans."

279. Nevertheless, on December 30, 2005, Block, purportedly in response to Multicred's "rough estimate" of the "collectability of the loans," determined that it would "be in the best interest of the corporation to treat a large portion" of the debt as "bad debt" before the close of the 2005 fiscal year. Block authorized Alicia Holdings to write-down 85.27% of the debt portfolio.

280. On its 2005 federal income tax return, Alicia Holdings reported $9.9 million in bad debts and $2 million as other deductions, including $377,320 for purported legal and professional service fees and $663,247 for purported management fees, much of which was paid to defendants and their businesses. Alicia Holdings' reported taxable income was $9,242 on which it reported it owed $1,386 in taxes. In actuality, the corporation earned more than $10.4 million in capital gains from sale of its office park on which it paid almost no income taxes.

281. As of December 31, 2007 – more than two years after defendants authorized Alicia Holdings' purported good-faith entry into the debt-collection business – a mere $11,799 or 0.10% of the $11.6 million conveyed to the 2005-A sub-trust had been reported as collected and received by Alicia Holdings.

I. G. B. & G.

282. In July 2004, defendants, through ASI, promoted an intermediary transaction to representatives of I. G. B. & G. Corporation (I. G. B. & G.), a Delaware corporation, for the purchase of all stock of the company. The stock purchase preceded the corporation's asset sale in this intermediary transaction.

283. Prior to the sale of its stock, I. G. B. & G. was owned by over twenty members of a single family and operated as a personal holding corporation with assets consisting of cash and various marketable securities.

284. In September 2004, Klink sent the I. G. B. & G. customers' representative, a Pennsylvania-based private wealth manager, information concerning the intermediary transaction including: (1) a draft Letter of Intent (LOI) with proposed terms of a sale of I. G. B. & G.'s stock; and (2) ASI promotional materials that the customers' representative had requested from Block, including company background on ASI. The ASI "company background" includes an overview of how ASI purchases the stock of companies from "shareholders that wish to liquidate the business operations of [a] Target corporation." The promotional material falsely asserts that "[s]ubsequent to the acquisition of the Target corporation, ASI and its affiliates re-engineer the operations of the Target corporation in order to put it into a new line of business for a significant period of time post-closing."

285. On September 30, 2004, the I. G. B. & G. customers and their representative, whom they had tasked with exploring possible methods for selling and distributing the corporation's retained earnings and assets to all shareholders, acknowledged through an agreement that the representative had "identified a means for the stockholders of the Company [] to liquidate their collective stock in the Company . . . through a cash sale to a buyer [] identified by [the representative]." The representative had conferred with defendants about the intermediary transaction, and the representative then contemplated that I. G. B. & G. would realize an estimated savings of $450,000 to $500,000 "versus an orderly liquidation of the Company's holdings" that would yield no such savings.

286. In or about September and early October of 2004, defendants and the I. G. B. & G. customers' representative negotiated the terms of a final LOI, which was executed on October 15, 2004.

287. Among other items, the final LOI sets forth the formula that defendants used to determine the stock sale price for I. G. B. & G. which preceded the asset sale: (1) "the opening price for those assets of the Company that Sellers and Purchaser agree are marketable and liquid securities . . . at the close of business on the business day immediately preceding the closing date"; (2) other assets, such as cash and unpaid dividends and interest accrued by I. G. B. & G. as of the closing date, "minus" I. G. B. & G. liabilities; and (3) "the product of seventeen point two percent (17.2%) times the total unrealized gain on the Company Securities as of the Closing Date." This was defendants' effort to approximate the corporate assets' value in advance of the stock sale.

288. To effectuate the sale of I. G. B. & G.'s stock, the I. G. B. & G. customers established a limited liability company, I. G. B. & G. of Delaware LLC (the LLC), and transferred their shares of I. G. B. & G. stock to the LLC. The LLC served as the entity selling the corporation's stock.

289. Pursuant to a Stock Purchase Agreement executed on November 10, 2004, defendants caused ASI, acting as intermediary company, to purchase all I. G. B. & G. stock for $2.8 million.

290. Defendants funded the stock purchase using promissory notes ASI issued to individuals, totaling $1 million, covered by pledge agreements issued by ASI, and defendants received additional financing from at least one financial institution. These obligations were repaid using assets held by I. G. B. & G. after the sale of its stock to defendants.

291. After the $2.8 million payment by ASI to the LLC for the I. G. B. & G. stock, plus repayment to holders of promissory notes, and sale (over two years - 2004 and 2005) of the marketable securities owned by I. G. B. & G., the target corporation no longer had sufficient assets to pay its corporate income taxes on the gains from the sale of securities.

292. Following the sale of I. G. B. & G.'s stock to ASI, Block became president and sole director of I. G. B. & G., and Klink was appointed secretary and treasurer.

293. On November 11, 2004, one day after the stock sale to ASI, Block, as sole director of I. G. B. & G., authorized a written consent to purportedly re-engineer I. G. B. & G. into a debt-collection business, commencing a distressed-asset transaction that extended into 2005. Defendants caused I. G. B. & G. to enter into the debt-collection business in order to create bogus losses to offset capital gains and evade corporate income tax liability.

294. On November 12, 2004, pursuant to a 2004-C Supplement To Trust Agreement to the DARB Trust, established earlier that month, I. G. B. & G. received 100 percent ownership of a Brazilian debt portfolio of 11,784 loans purportedly worth $2.2 million. Rogers of West End Fund and Block on behalf of I. G. B. & G., and the sub-trust's trustee, signed the 2004-C Supplement To Trust Agreement. Shortly after creation of this sub-trust, Grodsky became the trustee.

295. Defendants understood that the purported $2.2 million worth of debt in fact had no value or was near worthless. Defendants acquired the debt to claim bogus bad-debt deductions to evade I. G. B. & G.'s corporate tax liability.

296. On November 25, 2004, defendants, through ASI, sold the I. G. B. & G. stock to Oceanus for $10,000.

297. In a December 22, 2004 letter, purportedly sent at the request of I. G. B. & G, the trustee of the 2004-C sub-trust requested that Multicred provide a "rough estimate" as to the "collectability of the loans that have been allocated to the 2004-C Sub-Trust." On information and belief, Multicred never provided a "rough estimate" as to the "collectability of the loans."

298. In 2005, I. G. B. & G. re-incorporated under Nevada law, purported to enter into the wine-trading business, and executed a Wine Trading Services Agreement with Klink's company, Carpevino.

299. The Wine Trading Services Agreement executed by Klink and Block was designed to transfer funds held by I. G. B. & G. to Klink.

300. Over one year after defendants' December 2004 request to Multicred seeking a written estimate as to the "collectability" of the loans in the 2004-C sub-trust, on December 30,

2005, Block, purportedly in response to Multicred's assessment of the I. G. B. & G. debt portfolio, consented to a write-down of 80.45 percent of the portfolio as "bad debt" for the 2005 fiscal year.

301. In its federal income tax return for 2004, I. G. B. & G. reported $447,578 as total income, which included the sale of a portion of the marketable securities held by I. G. B. & G. during 2004, offset by deductions including $170,324 for legal and professional expenses and $65,000 for management fees. On its 2004 federal income tax return, I. G. B. & G. used purported professional fees to offset its 2004 gains and reported only $2,345 in federal taxes due.

302. On its 2005 federal income tax return, I. G. B. & G. reported capital gain net income of $1,808,529, which was from the proceeds of the sale of marketable securities held by I. G. B. & G. during 2005. The write-down of the 2004-C sub-trust debt occurred in 2005, and to this end, I. G. B. & G. claimed a bad debt deduction of $1,770,000. On its 2005 federal income tax return, the corporation reported that it owed $2,009 in federal taxes.

303. As of December 31, 2007 – more than three years after defendants authorized I. G. B. & G.'s purported good faith entry into the debt-collection business – a mere $4,145 or 0.19% of the $2.2 million conveyed to the 2004-C sub-trust had been reported as collected and received by I. G. B. & G.

Indian Creek Vineyards

304. Starting in September 2006, Grodsky, through his company, Dalmar, oversaw the promotion and implementation of an intermediary transaction involving the sale of all stock of Indian Creek Vineyards LLC (Indian Creek), which was owned by Mondavi Holdings Limited

(MHL), following the sale of Indian Creek's Saint Helena, California vineyard for $3.5 million. Klink and Block had referred this intermediary transaction to Grodsky.

305. Grodsky explained his role in this intermediary transaction in a September 26, 2006 email that he sent to the Indian Creek customers, who operated MHL, and their representatives: "[a]s both [a] lawyer and a corporate officer, I represent Dalmar, LLC . . . the intended buyer of the stock of Indian Creek" and "will be coordinating all of the business and legal aspects of this stock purchase transaction from the Buyer side."

306. As part of his promotion of the intermediary transaction, Grodsky requested that the Indian Creek customers: (1) provide him with information, including the "estimated amount of cash . . . that will be held by the corporation after the assets are sold, which (together with the basis in the corporate assets) will be used to calculate the estimated amount of the taxable gains of the corporation that will be realized from the corporate asset sale proceeds"; (2) establish a bank account in which to hold Indian Creek funds remaining in the company after sale of its stock; and (3) prepare a pro-forma tax return for 2006 that estimates the corporation's tax liabilities, as "[t]he stock purchase price set forth in the draft of the Stock Purchase Agreement will vary depending on the final numbers generated by the pro-forma" tax return.

307. Grodsky touted the purported financial benefits of the intermediary transaction for MHL, including his explanation of the so-called stock-price premium that Dalmar would pay to MHL (equal to fifty percent of Indian Creek's total projected corporate income tax for that tax year). Grodsky never told his customers that the transaction was not legal because it violated numerous judicial doctrines and Code provisions.

308. On November 2, 2006, Grodsky, through Dalmar, and MHL executed a Stock Purchase Agreement for the sale of all stock of Indian Creek for $3.9 million. By agreement of the parties, approximately $4.3 million in cash reserves remained in Indian Creek immediately after the sale. That day, Grodsky became vice president, treasurer, and secretary of Indian Creek, and his then-fiancee became the corporation's president and sole director.

309. Grodsky had insisted that this transaction close no later than November 2, 2006. He falsely represented, as he often has done, that "Buyer needs sufficient time to be able to re-engineer the company" into a viable business following the stock sale. In actuality, the time that Grodsky needed as buyer was not to re-engineer Indian Creek into a viable business, but to implement a DAT tax scheme prior to the close of 2006.

310. Klink also was involved with the implementation of the Indian Creek stock sale as the representative of the lenders funding Dalmar's stock purchase.

311. On November 3, 2006, defendants caused Indian Creek to purport to enter into the debt-collection business, and thus, into the DAT tax scheme.

312. On November 6, 2006, Sugarloaf, the Illinois limited liability company managed by John Rogers, entered into a Contribution Agreement with Conrev Business Trust (the "Conrev Trust"). The Conrev Trust Agreement designates Alterbridge Ventures and Warwick Trading, as the grantors and initial beneficiaries of the trust and provides that Sugarloaf transfer a distressed-asset "portfolio" to the Conrev Trust.

313. To further implement the DAT abusive tax scheme, an agreement executed on November 6, 2006 established a sub-trust to the Conrev Trust. The sub-trust agreement

identifies Indian Creek as one-hundred percent beneficiary of "[a]ll right, title and interest in and to those certain loans, including loans in the aggregate amount of US$3,200,000.00."

314. Also on November 6, 2006, the Conrev Trust entered into an Agreement for Collection Services with Multicred. In exchange for 15% of any collections of the $3.2 million Brazilian debt portfolio assigned to Indian Creek, Multicred was to deliver "professional services" that included: (1) administrative and collection services; (2) scheduled transfers of collections from Multicred to the Conrev Trust; (3) "managing the portfolios of loans and receivables to maximize collection and recovery"; and (4) "summary collection and expense reports no less frequently than once every three (3) months."

315. In a December 19, 2006 letter that the Conrev Trust trustee wrote to Multicred, she requested a "rough estimate" as to the "collectability of the loans that have been allocated to the 2006-C Sub-Trust" [for Indian Creek]. Multicred responded in a December 22, 2006 letter that describes the assets contributed to the Conrev Trust sub-trust as consumer "receivables [that] are aged." Multicred, however, provided no estimate as to what portion, if any, of the $3.2 million debt portfolio was collectable or any support that the debt was valued at $3.2 million, as claimed in the November 6, 2006 Contribution Agreement that defendants had drafted and executed.

316. Nevertheless, on December 30, 2006, by written consent of its director, Indian Creek, after purportedly having "received the advice of Multicred Investimentos Ltd., in its capacity as the collection agent for certain loans in which the Corporation holds a beneficial interest," determined that "it would be in the best interest of the corporation" to write-down 84% of the purported value of the $3.2 million as bad debt for the 2006 fiscal year.

317. In its federal income tax return for 2006, signed by Grodsky as an officer of Indian Creek, Indian Creek reported $2.7 million in bad debts and $840,521 for other deductions, including $400,000 for "due diligence" expenses, $135,000 for "management fees," $40,000 for "legal fees," and $111,729 for "other acquisition fees." A sizeable percentage of the other deductions consists of fees that defendants paid themselves for the performance of purported legal services and consulting services. As a result, Indian Creek's reported 2006 federal taxable income was negative $29,611. Indian Creek reported on its return that it had no federal income tax due for 2006.

318. On information and belief, less than $130,000 of the $2.7 million Indian Creek debt portfolio had been reported as collected by the end of 2007.

Harm to the United States

319. For at least ten years, Defendants have promoted and continue to promote the intermediary transaction tax scheme.

320. This scheme has caused substantial harm to the government. To date, the intermediary transaction tax scheme has caused tens of millions of dollars in tax harm to the public fisc.

321. The United States also is harmed because the IRS has had to devote limited resources to detect and examine the inaccurate tax returns that defendants have caused each target corporation to deliberately file.

322. As part of the intermediary transaction tax scheme, defendants have caused each corporation to claim losses falsely and fraudulently, and to deplete each target corporation's funds, rendering each corporation insolvent and unable pay its income taxes.

323. In order to recoup a mere fraction of the tax losses, the IRS has had to devote additional resources to locating other responsible entities or individuals who can satisfy each corporation's tax liability.

324. Defendants have caused the target corporations they acquire to improperly deduct more than $112 million of distressed consumer receivables as bad debt on federal tax returns. The resulting amount of tax loss resulting from defendants' promotion of the intermediary transaction tax schemes and bad debt write-downs is at least $40 million.

COUNT I: Injunction Under I.R.C. § 7408 For Violation Of I.R.C. §§ 6700, 6701, 6707 and 6708

325. The United States incorporates by reference the allegations in paragraphs 1 through 324.

326. Section 7408 of the I.R.C. authorizes a court to enjoin persons who have engaged in any conduct subject to penalty under I.R.C §§ 6700, 6701, 6707 or 6708 if the Court finds that injunctive relief is appropriate to prevent recurrence of such conduct.

327. Section 6700 of the I.R.C. penalizes any person who organizes or sells a plan or arrangement and in connection therewith makes or furnishes or causes another person to make or furnish a statement regarding the securing of a tax benefit that the person knows or has reason to know is false or fraudulent as to any material matter.

328. Through their promotion of the intermediary transaction scheme, Klink, Block and Grodsky make and furnish false and/or fraudulent material statements regarding the allowability of certain deductions, the excludability of income, and the securing of tax benefits derived from

participation in the scheme. Defendants know and/or have reason to know that these statements are false or fraudulent within the meaning of I.R.C. § 6700.

329. Section 6701 of the I.R.C. penalizes any person who prepares or aids, assists, or advises with respect to the preparation of a document that he knows or has reason to believe will be used in connection with any material matter arising under the internal revenue laws and who knows that the document, if so used, would result in an understatement of another person's tax liability.

330. Defendants have drafted and helped to draft numerous documents that implement the intermediary transaction tax scheme and cause the understatement of tax liability. Defendants know that these documents (or portions of these documents) have been used in connection with one or more material matters arising under the internal revenue laws. Defendants also know that the documents (or portions of these documents) that they draft and help to draft, if used, would result in the understatement of another person's tax liabilities.

331. Section 6707 of the I.R.C. penalizes any person who fails to file with the IRS a return or statement that identifies and describes any reportable or listed transaction, any potential benefits expected to result from that transaction, and any other information required by statute if that person is required to file this information with the IRS.

332. Defendants have failed to file with the IRS a return or statement that identifies or describes any of the reportable or listed transactions that they have continued to promote to customers. At all relevant times, defendants were required to provide this tax shelter information to the IRS. Thus, defendants have engaged in I.R.C. §6707 penalty conduct.

333. Section 6708 of the I.R.C. penalizes any person who fails to furnish to the IRS upon request a list that identifies all taxpayers for whom that person served as a material advisor concerning any reportable transaction, including any listed transaction. A material advisor is a person who materially aids or assists in the organization of a reportable transaction.

334. Grodsky and Block failed to furnish the IRS with this list when it was requested. They were required to maintain such a list because they have been material advisors as to the intermediary transactions that they have organized for their customers. Thus, Block and Grodsky have engaged in I.R.C. §6708 penalty conduct.

335. Pursuant to I.R.C. § 7408, defendants should be enjoined from engaging in any further conduct that violates I.R.C. §§ 6700, 6701, 6707 and 6708. In the absence of an injunction, defendants will continue to engage in such conduct.

COUNT II: Injunction Under I.R.C. § 7402 For Unlawful Interference With The Administration And Enforcement Of The Internal Revenue Laws And The Appropriateness Of Injunctive Relief

336. The United States incorporates by reference the allegations in paragraphs 1 through 335.

337. Section 7402(a) of the I.R.C. authorizes a court to issue orders of injunction as may be necessary or appropriate for the enforcement of the internal revenue laws.

338. Defendants, through the actions described above, have engaged in conduct that interferes substantially with the administration and enforcement of the internal revenue laws. Defendants have promoted their intermediary transaction tax scheme which has caused millions of dollars in tax harm. In order to effect their intermediary transaction tax scheme, defendants prepare sham agreements, incorporate sham entities, and execute sham contracts in order to give

the appearance that their transaction has economic substance and a business purpose. Defendants further effect their intermediary transaction tax scheme by participating in the DAT tax scheme, which is another tax scheme that they use to manufacture bogus losses. Defendants' intermediary transaction has no economic substance, is a sham transaction and violates numerous provisions of the Internal Revenue Code.

339. Defendants' ongoing promotion of the intermediary transaction tax scheme and participation in the DAT tax scheme has caused irreparable harm to the United States. Defendants' conduct is causing and will continue to cause substantial revenue loss to the United States Treasury, much of which may be unrecoverable.

340. Unless defendants are enjoined, the IRS will have to continue devoting substantial time and resources auditing each target corporation that defendants acquire, through their intermediary companies, and assessing the corporate tax penalties, some portion of which may be impossible to recover. Moreover, some of defendants' intermediary transactions go undetected because defendants fail to file the required disclosures with the IRS, and defendants also advise their customers not to file these required disclosures with the IRS. The burden of pursuing those individuals and entities who are responsible for and able to pay the unpaid corporate tax liabilities may be an insurmountable obstacle given the IRS's limited resources.

341. If defendants are not enjoined, they are likely to continue to engage in conduct subject to penalty under I.R.C. §§ 6700, 6701, 6707 and 6708 and conduct that interferes with the enforcement of the internal revenue laws.

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

A. That the Court find that defendants have engaged in conduct subject to penalty under I.R.C. §§ 6700, 6701, 6707 and 6708 and that injunctive relief under I.R.C. § 7408 is appropriate to prevent a recurrence of that conduct;

B. That the Court find that defendants have engaged in conduct interfering with the administration and enforcement of the internal revenue laws, and that pursuant to I.R.C. §7402, injunctive relief is appropriate to prevent the recurrence of that conduct;

C. That pursuant to I.R.C. §§ 7402 and 7408, defendants and anyone acting in concert with them be permanently enjoined and restrained from, directly or indirectly, by use of any means or instrumentalities:

a. Organizing, promoting, marketing, or selling any plan or arrangement – including but not limited to the intermediary transaction tax scheme described in this complaint or any similar scheme– that advises or assists others in violating or attempting to violate the internal revenue laws or unlawfully evading the assessment or collection of their federal tax liabilities;

b. Engaging in conduct subject to penalty under I.R.C. § 6700, *i.e.*, organizing or selling any plan or arrangement and in connection therewith (a) making a gross valuation overstatement or (b) making or furnishing false or fraudulent statements regarding the allowability of certain deductions, the excludability of income, or the securing of tax benefits derived from participation in a plan or arrangement, when he knows and/or has reason to know the statements are false or fraudulent as to a material matter;

c. Engaging in conduct subject to penalty under I.R.C. § 6701, *i.e.*, preparing or assisting in the preparation of, or advising with respect to a document related to a matter material to the internal revenue laws that includes a position that he knows will, if used, result in an understatement of tax liability;

d. Engaging in conduct subject to penalty under I.R.C. § 6707(a), *i.e.*, failing to file a return or statement with the IRS that identifies and describes any reportable or listed transaction, any potential tax benefits expected to result from that transaction, as well as other information required by statute;

e. Engaging in conduct subject to penalty under I.R.C. § 6708, *i.e.*, failing to furnish the IRS with a list that identifies all customers who have participated in a listed transaction when the IRS requests such a list and the list is required to be maintained pursuant to statute;

f. Engaging in any other conduct that interferes with the administration or enforcement of the internal revenue laws, including but not limited to implementing and participating in the intermediary transaction, DAD, DAT or any similar tax schemes using sham fees, sham entities and/or sham transactions.

D. That this Court, pursuant to I.R.C. §§ 7402 and 7408, enter an injunction requiring defendants to contact, within thirty days of the Court's order, all persons whom they have assisted or advised with respect to any tax scheme, including but not limited to those schemes described in this complaint or identified through further discovery, and inform these persons of the Court's findings and the fact that an injunction has been entered against them;

E. That this Court, pursuant to I.R.C. §§ 7402 and 7408, enter an injunction requiring defendants to produce to the United States, within thirty days of the Court's order, any records in their possession, custody or control, identifying the names, addresses, telephone numbers, e-mail addresses, and Social Security and federal tax identification numbers of all persons and entities who have participated in any tax scheme that defendants have promoted;

F. That the Court order that the United States is permitted to engage in post-injunction discovery to ensure compliance with the permanent injunction;

G. That this Court retain jurisdiction over this action for purposes of implementing and enforcing this Final Judgment of Permanent Injunction; and

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

Respectfully submitted,

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DATE: February 22, 2011

CERTIFICATION PURSUANT TO L.Civ.R. 11.2

I hereby certify that pursuant to L.Civ.R. 11.2, the matter in controversy herein is not the subject of any other action pending in any other court, pending arbitration or administrative proceeding.

s/ Allyson B. Baker
ALLYSON B. BAKER