

IN THE UNITED STATES DISTRICT COURT FOR THE  
MIDDLE DISTRICT OF ALABAMA  
EASTERN DIVISION

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UNITED STATES OF AMERICA, )  
 )  
 Plaintiff, )  
 )  
 v. )  
 )  
 KENYA HENDRIX ADAMS, )  
 )  
 Defendant. )

DEBRA P. HACKETT, CLK  
U.S. DISTRICT COURT  
MIDDLE DISTRICT ALA

Civil Case No. 3:13-cv-161-MEF

COMPLAINT FOR PERMANENT INJUNCTION

The United States of America alleges as follows:

1. The United States brings this complaint to enjoin Kenya Hendrix Adams, and any other person working in concert or participation with her, from directly or indirectly:
  - (a) preparing, assisting in the preparation of, or directing the preparation of federal income tax returns, amended returns, or other tax-related documents and forms, including any electronically-submitted tax returns or tax-related documents, for any entity or person other than herself;
  - (b) engaging in activity subject to penalty under 26 U.S.C. §§ 6694, 6695, 6700, and 6701; and
  - (c) engaging in conduct that substantially interferes with the proper administration and enforcement of the tax laws.
  
2. This action has been requested by the Chief Counsel of the Internal Revenue Service, a delegate of the Secretary of the Treasury, and commenced at the direction of a delegate of the Attorney General of the United States pursuant to 26 U.S.C. §§ 7401, 7402, 7407, and 7408.

### **Jurisdiction and Venue**

3. Jurisdiction is conferred on this Court by 28 U.S.C. §§ 1340 and 1345 and 26 U.S.C. §§ 7402(a), 7407, and 7408.
4. Venue is proper in this Court pursuant to 28 U.S.C. § 1391 and 26 U.S.C. § 7407(a) because Adams resides within this judicial district, prepares tax returns within this judicial district, and a substantial part of the events giving rise to this claim occurred within this judicial district.

### **Summary of Defendant's Activities**

5. Adams resides in Montgomery, Alabama. She prepares income tax returns, including Form 1040, "Individual Income Tax Return," for other taxpayers from an office location at 21 First Street, Shorter, Alabama, 36075.
6. Adams was previously employed by H&R Block and Jackson Hewitt, where she received training in tax laws and tax return preparation.
7. Adams has conducted her tax return preparation business under the trade names "Shorter Tax Service" and "Professional Income Tax Service."
8. IRS records show that, from 2008 to 2012 (the most recent year for which figures are available), Adams prepared approximately 1,988 Form 1040 returns. The number of returns Adams prepared each year was as follows:

<u>Year</u>	<u>Number of Returns</u>
2012	175
2011	378
2010	554
2009	514
2008	367

9. Since at least 2008, most of the income tax returns prepared by Adams have understated the filing taxpayer's liability by falsely claiming or inflating tax credits or fabricating

deductions. The improper credits Adams claimed for clients include the under the Earned Income Tax Credit (“EITC”) (26 U.S.C. § 32), the First-Time Homebuyer credit (26 U.S.C. § 36(a)), education credits (26 U.S.C. § 25A); and the additional child credit (26 U.S.C. § 24).

10. Adams has repeatedly and continually improperly claimed the EITC on her clients’ returns to generate large and erroneous refunds for her clients. The EITC is a refundable credit, which means that it can generate a refund exceeding the amount of income tax paid by an individual taxpayer.
11. Adams has repeatedly and continually improperly claimed the First-Time Homebuyer credit on her clients’ returns to generate large and erroneous refunds for her clients. The First-Time Homebuyer credit was available to certain people who purchased a home as their primary residence in 2008, 2009, and 2010 and was a refundable credit. For residences purchased in 2008, the credit was effectively a zero-interest loan in the form of a refundable tax credit, but in subsequent years the loan-like features of the credit were removed. The false or overstated First-Time Homebuyer credit claims reported by Adams on her clients’ returns generate corresponding decreases in tax liability or increases in refunds, regardless of whether the individual client paid any taxes during the year.
12. In addition to preparing returns that improperly claim credits, Adams has continually and repeatedly failed to comply with the due diligence requirements set forth in 26 U.S.C. § 6695(g), and accompanying regulations, for determining eligibility and amount of these EITCs. The due diligence a preparer must undertake includes, *inter alia*, the duty to make reasonable inquiries if the information provided by the taxpayer appears to be incorrect,

incomplete, or inconsistent, as well as a duty to contemporaneously document the inquiries made and the responses to these inquiries.

13. Adams has also prepared returns that improperly claim an education credit and an additional child tax credit for ineligible taxpayers.
14. The understatements of liability on the returns Adams prepared were not solely the result of credits Adams knew to be false. Adams has also prepared returns that claim income tax deductions for fictitious expenses.
15. In February, 2008, an IRS Revenue Agent conducted an E-File monitoring visit on Adams, who was doing business at that time under the name "Professional Income Tax Preparation." As a result of that visit, the IRS suspended Adams' Electronic Filing Identification Number, which is required to file returns electronically for others, because Adams had failed to comply with the EITC due diligence requirements set forth in 26 U.S.C. § 6695(g), and accompanying regulations.
16. In April, 2011, an IRS Revenue Agent conducted another E-File monitoring visit at Adams' location. At that time, Adams was operating under the name "Shorter Tax Service" and returns were being filed through an Electronic Filing Identification Number obtained under the name of Adam's sister, Sylvia Hendrix. As a result of the visit, Hendrix was assessed penalties of \$23,500 for failing to adhere to the EITC due diligence requirements set forth in 26 U.S. C. § 6695(g). Adams subsequently stated to employees of the IRS that Hendrix did not prepare any income tax returns.
17. In February, 2012, a follow-up E-File monitoring visit was conducted at Adams' location. As a result of that visit, Adams was assessed penalties of \$13,200 for failing to adhere to the EITC due diligence requirements set forth in 26 U.S. C. § 6695(g).

18. The IRS has completed examinations of 315 returns prepared by Adams for the 2008 and 2009 tax years. Of those returns, the IRS determined that approximately 88% understated the filing taxpayer's liability and the average understatement was \$3,150 per return.

#### **Examples of Adams' Fraudulent Schemes**

19. The returns described in paragraphs 20 through 39, below, demonstrate the schemes employed by Adams on hundreds of returns she has prepared for her clients.

#### **EARNED INCOME TAX CREDIT**

20. Adams primary scheme for underreporting her clients' liability or overstating their claim to a refund is to report false information pertaining to the Earned Income Tax Credit.
21. Adams has employed several methods to fraudulently increase her clients' EITC claims, including reporting fraudulent income on a Schedule C or as "HSH" wage income on her clients' returns. Adams also prepares returns that falsely claim that a "qualifying child" resides with the taxpayer, which increases the maximum allowable amount of the EITC.
22. The amount of the EITC that a taxpayer may claim increases in proportion to a taxpayer's wages or other earned income up to a certain dollar amount. As such, there is a "plateau" of earned income that will result in the maximum possible EITC a taxpayer may claim. Because that "plateau" amount may be more than the income the taxpayer actually earned, a return falsely overstating income will, in certain circumstances, generate a larger refund.
23. In some instances, Adams falsely overstates her clients' income in order to maximize their EITC claim by overstating income from a sole proprietorship or reporting false income from a fictitious sole proprietorship on a "Schedule C, Profit or Loss From Business (Sole Proprietorship)," filed with the return.

24. The return prepared by Adams for M.C. for the 2011 tax year demonstrates how Adams falsely reports income on a schedule C in order to fraudulently inflate the taxpayer's EITC. That return reported employment wages of \$4,261, and Schedule C income in the amount of \$8,500. While the wage figure represents the amount reported on the Form W-2 issued by M.C.'s employer, there was no documentation for the \$8,500 in Schedule C income which was purportedly derived from cash payments received in M.C.'s business. Based on the information reported on the return, M.C. received an EITC of \$4,870 and a refund of \$3,937. An IRS Revenue Agent investigating returns filed with Sylvia Hendrix's e-filing number contacted M.C., who stated that he did not own a business in 2011 and did not know why the \$8,500 of false income was reported on the Schedule C. Without the false income, M.C.'s EITC would have been less than \$2,000.
25. Adams also prepares returns that report false "HSH" income on the wages section of the Form 1040. The "HSH" designation is intended to document income earned by a taxpayer as a household employee, i.e. "household help," in situations where the employer does not provide a W-2. As such, "HSH" income is not directly verifiable through a third-party reporting document such as a W-2 or 1099.
26. Adams prepared returns for taxpayer R.C. for the 2008 and 2009 tax years which reported entirely fictitious HSH income in the amount of \$12,000 in each year in order to increase R.C.'s claim to the EITC. Each return claimed an EITC of \$4,810, and sought a refund of this amount (plus additional amounts based on other items reported on the return), even though R.C. paid no tax on the reported HSH income. The sole purpose for reporting that income was to claim an EITC credit to which R.C. was not entitled. The IRS examined

R.C.'s 2008 and 2009 income tax returns and, after R.C. failed to provide any information to support the HSH income or EITC claims, disallowed the EITC in full.

27. Adams prepared returns for taxpayer R.T. which demonstrate the breadth of Adams' fraudulent manipulation of the EITC.
- a. For the 2010 tax year, the return prepared by Adams reported wages of \$2,100 and Schedule C income of \$8,888. The return also claimed an increased EITC based on a qualifying child identified on the return as the taxpayer's son, who was reported as "permanently and totally disabled" on the return. The 2010 return claimed a refund of \$2,306.
  - b. For the 2011 tax year, the return prepared by Adams reported wage income of \$9,120 and an increased EITC based on the same qualifying child identified on the 2010 return, but for 2011 the child was identified as the taxpayer's brother. The 2011 return claimed a refund of \$3,094.
  - c. The IRS examined R.T.'s 2010 and 2011 returns and determined that the claimed refunds should be fully disallowed. R.T. agreed with the IRS' determination.
  - d. During the examination, R.T. provided a sworn affidavit stating that he had no wage or business income in either 2010 or 2011 and that he had not provide any information indicating otherwise to Adams, who prepared his returns. He stated that the person claimed as a qualifying child on his returns was his nephew, not his son or brother as had been indicated on the returns, and that his nephew was not permanently and totally disabled. R.T. stated that Adams did not provide him with a copy of either of his returns or inform him of the amount of refund claimed on the returns.

FIRST-TIME HOMEBUYER CREDIT

28. Adams has repeatedly prepared returns that improperly claim a first-time homebuyer credit under 26 U.S.C. § 36(a).
29. The first-time homebuyer credit is a refundable credit available to certain home buyers who purchased a home as their primary residence in 2008, 2009 or 2010 and met the statutory requirements for claiming the credit. For residences purchased in 2008, the credit took the form of a no-interest loan of up to \$7,500. For residences purchased in 2009 or 2010, the maximum amount of the credit was \$8,000 and it did not require repayment in the same manner as homes purchased in 2008.
30. The return prepared by Adams for taxpayer K.B. for the 2008 tax year demonstrates Adams' method for fraudulently claiming the first-time homebuyer credit. That return claimed the maximum credit, \$7,500, as well as an EITC of \$1,737, against K.B.'s withholdings of \$883.00 from legitimate wage income (reported by third parties on W-2's) of \$23,147. As a result of the first-time homebuyer and EITC credits, K.B. received a refund of \$9,409, which greatly exceeded the tax K.B. actually paid. Upon being contacted by an employee of the IRS, K.B. stated that she did not purchase a home in 2008, but was told by Adams that she could claim the credit regardless.
31. Adams prepared at least 19 returns for the 2008 tax year that improperly claimed the first-time homebuyer credit. The IRS determined that those 19 returns alone claimed improper first-time homebuyer credits of \$137,350.

ADDITIONAL SCHEMES: ADDITIONAL CHILD TAX CREDIT, EDUCATION CREDIT, FALSE SCHEDULE C LOSSES

32. IRS examination of returns prepared by Adams have turned up several additional schemes employed by Adams.



33. The Additional Child Tax Credit is a refundable credit for taxpayers who have a qualifying child but are unable to claim the full amount of the standard Child Tax Credit.
34. Adams' primary method of overstating her client's claim to the Additional Child Tax Credit is to falsely overstate the number of qualifying children of the taxpayer. As described in the example in paragraph 26, above, this can also have the effect of increasing the maximum amount of the EITC the taxpayer can claim if the child is also reported as a "qualifying child" for that purpose.
35. Adams prepared at least 30 returns for the 2008 tax year and 25 returns for the 2009 tax year that wrongfully claimed the additional child tax credit.
36. Adams also prepared 11 returns for the 2009 tax year that wrongfully claimed an education credit.
37. For the 2009 tax year, the American Recovery and Reinvestment Act modified the existing Hope Credit for education to make it available to a broader range of taxpayers. Generally, 40% of the credit for that year is refundable, meaning that a taxpayer would be able to receive an education credit of up to \$1,000 even if he owed no taxes.
38. In some instances, Adams would prepare returns that reported a false loss on a Schedule C in order to reduce the taxpayer's reported adjusted gross income and maximize the amount of the EITC.
39. An example of Adams' reporting of false losses is the return she prepared for R.A. for the 2010 tax year. That return reported a false net loss on Schedule C of \$18,355, against bona fide wages of \$28,874. R.A.'s 2010 return was examined by the IRS and R.A. provided an affidavit stating that the Schedule C items on the return were false.

**Harm to the United States**

40. Adams has caused harm to the United States by creating substantial revenue losses through inflating or fabricating claims to refundable credits and falsifying deductions on the returns she prepares through the schemes described above.
41. In addition, Adams' actions have forced the United States to expend significant resources to examine and correct the returns she prepared.
42. In many instances, Adams' clients had taxes withheld during the reporting years and Adams' understatement of those clients' liabilities caused the United States to issue refunds that the clients were not entitled to receive.
43. Because most of the tax credits wrongfully claimed by Adams are refundable, the returns prepared by Adams caused the United States to make a tax refund payment in some instances to taxpayers who had little or no income tax liability and were actually not entitled to any refund.
44. Given the number of returns prepared by Adams and the high percentage of returns that understated the client's tax liability, the loss to the United States Treasury caused by Adams' return preparation business is in the millions of dollars.

**COUNT I**

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

45. The United States incorporates by reference the allegations in paragraphs 1 through 44.
46. Section 7407 of the Internal Revenue Code authorizes a district court to enjoin a person who is a tax return preparer from engaging in certain prohibited conduct or from further acting as a tax return preparer. The prohibited conduct justifying an injunction includes, *inter alia*, the following:

- (a) Engaging in conduct subject to penalty under 26 U.S.C. § 6694, which penalizes a tax return preparer who prepares a return that contains an understatement of tax liability or an overstatement of a refund due to an unreasonable position that the return preparer knew or should have known was unreasonable;
- (b) Engaging in conduct subject to penalty under 26 U.S.C. § 6695(g), which penalizes a tax return preparer for failing to exercise due diligence in determining eligibility for the EITC; and
- (b) Engaging in any other fraudulent or deceptive conduct which substantially interferes with the proper administrations of the Internal Revenue laws.

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

- (a) The tax return preparer engaged in the prohibited conduct; and
- (b) Injunctive relief is appropriate to prevent the recurrence of such conduct.

48. If a tax return preparer's conduct is continual or repeated and the court finds that a narrower injunction would not be sufficient to prevent the preparer's interference with the proper administration of the internal revenue laws, the court may permanently enjoin the person from acting as a tax return preparer. *See* 26 U.S.C. § 7407(b).

49. Adams has continually and repeatedly engaged in conduct subject to penalty under 26 U.S.C. § 6694 by preparing returns that understate the filers' tax liabilities and overstate their refunds based on unreasonable and reckless positions. As described in paragraphs 20 through 37, above, Adams prepares returns that claim credits to which the taxpayer is not entitled. Adams does so with the knowledge that the positions she took on the returns

were unreasonable and lacked substantial authority. Adams has thus engaged in conduct subject to penalty under 26 U.S.C. § 6694(a).

50. Adams engaged in conduct subject to penalty under 26 U.S.C. § 6695(g) by failing to exercise due diligence in determining eligibility for the EITC. Among other violations, Adams does not keep a proper record of the client's eligibility for the EITC and does not obtain verification for questionable sources of income.
51. Adams has continually and repeatedly engaged in conduct that violates 26 U.S.C. §§ 6694 and 6695 and which substantially interferes with the administration of the internal revenue laws. Injunctive relief is necessary to prevent this misconduct because, absent an injunction, Adams is likely to continue preparing false federal income tax returns.
52. As described above, the IRS has conducted multiple site visits and determined that Adams failed to comply with the EITC due diligence rules. The IRS assessed penalties against Adams and Hendrix, who worked in concert with Adams, for failing to comply with the EITC due diligence requirements. Despite these enforcement efforts, Adams has continued to prepare improper returns.
53. A narrower injunction would be insufficient to prevent Adams' interference with the administration of the federal tax laws because she abuses the tax code through both widely-known schemes and short-term or new tax credits. To date, she has focused primarily on the Earned Income Tax Credit, however her misuse of the First-Time Homebuyer credit and refundable education credits underscores the need to enjoin Adams' from all tax return preparation. In addition, the IRS may not yet have identified

all of the schemes used by Adams to understate her clients' liabilities or inflate their refund claim.

54. Failure to permanently enjoin Adams will require the IRS to spend additional resources to uncover all of Adams' future schemes. The harm resulting from these schemes includes both the expenditures of these resources and the revenue loss caused by the improper credits Adams claims on returns she prepares. Accordingly, only a permanent injunction is sufficient to prevent future harm. Adams should be permanently enjoined from acting as a tax return preparer

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

55. The United States incorporates by reference the allegations contained in paragraphs 1 through 44.
56. Section 7408 of the Internal Revenue Code authorizes a district court to enjoin any person from engaging in conduct subject to penalty under 26 U.S.C. § 6701, which penalizes a person who aids or assists in the preparation of tax returns that the person knows will result in an understatement of tax liability.
57. Adams has engaged in conduct subject to penalty under 26 U.S.C. § 6701 by preparing or directing the preparation of income tax returns that claim a tax credit when she knew that the taxpayer was not entitled to the credit, or the credit in the full amount claimed.
58. Adams' repeated actions such as those described in paragraphs 20 through 44, above, fall within 26 U.S.C. § 7408(c)(1), and injunctive relief is appropriate to prevent recurrence of this conduct.

59. Accordingly, Adams should be permanently enjoined from preparing any returns that improperly claim or inflate a claim to a tax credit.

COUNT III:

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

60. The United States incorporates by reference the allegations contained in paragraphs 1 through 44.
61. Section 7402(a) of the Internal Revenue Code authorizes a court to issue orders of injunction as may be necessary or appropriate for the enforcement of internal revenue laws.
62. Adams has repeatedly and continually engaged in conduct that interferes substantially with the administration and enforcement of internal revenue laws.
63. If Adams continues to act as a tax return preparer, her conduct will result in irreparable harm to the United States, and the United States has no adequate remedy at law.
64. Adams' conduct has caused and will continue to cause substantial tax losses to the United States Treasury, much of which may be undiscovered and unrecoverable. Moreover, unless Adams is enjoined from preparing returns, the IRS will have to devote substantial and unrecoverable time and resources auditing his clients individually to detect false, fraudulent, or overstated refund claims in future returns.
65. The detection and audit of erroneous tax credits claimed on returns prepared by Adams will be a significant burden on IRS resources.

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

A. That the Court find that Kenya Hendrix Adams has repeatedly and continually engaged in conduct subject to penalty under 26 U.S.C. §§ 6694 and 6695(g) and that injunctive relief is appropriate under 26 U.S.C. § 7407 to prevent recurrence of that conduct;

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

C. That the Court find that Adams has repeatedly and continually engaged in conduct that substantially interferes with the proper enforcement and administration of the internal revenue laws, and that injunctive relief against Adams is appropriate to prevent the recurrence of that conduct pursuant to 26 U.S.C. § 7402(a);

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

- (1) preparing, assisting in the preparation of, or directing the preparation of federal income tax returns, amended returns, or other tax-related documents and forms, including any electronically-submitted tax returns or tax-related documents, for any entity or person other than herself;
- (2) engaging in activity subject to penalty under 26 U.S.C. §§ 6694, 6695, 6700, and 6701; and
- (3) engaging in conduct that substantially interferes with the proper administration and enforcement of the tax laws;

E. That the Court enter an injunction requiring Adams:

1. At her own expense, to notify each person for whom he prepared federal income tax returns or any other federal tax forms after January 1, 2008, of this action and

provide each person with a copy of the final injunction entered against, as well as a copy of the Complaint setting forth the allegations as to how Adams fraudulently prepared federal income tax returns;

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

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

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

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

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

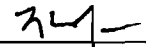


G. That the Court grant the United States such other and further relief as the Court deems appropriate

Dated: March 14, 2013

Respectfully submitted,

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