UNITED STATES DISTRICT COURT
MIDDLE DISTRICT OF FLORIDA
TAMPA DIVISION

USA,

Plaintiff,

v. Case No: 8:13-cv-1170-T-35TBM

JEANNE COVINGTON and JEANNE'S TAX PREPARATION AND BOOKKEEPING, INC.,

Defendants.

ORDER

THIS CAUSE comes before the Court for consideration of Plaintiff's Motion for Default Permanent Injunction. (Dkt. 29) Upon consideration of all relevant filings, case law, and being otherwise fully advised, the Court **GRANTS** Plaintiff's Motion for Default Permanent Injunction.

I. Background

On May 1, 2013, Plaintiffs brought this action to obtain an injunction permanently barring Jeanne Covington, any other person working in concert or participation with her, and her company, Jeanne's Tax Preparation And Bookkeeping, Inc., ("Jeanne's Tax") (collectively, "Covington"), from directly or indirectly preparing tax returns for others. (Dkt. 1) In sum, Plaintiff alleges that since at least 2005, Covington has prepared numerous returns that understate her client's tax liability or overstate their claim to refundable credits, leading to substantial financial harm to the United States.

On May 16, 2013, Plaintiff filed two Affidavits of Service providing that on May 10, 2013, Defendants were served with copies of the Summons and Complaint. (Dkts. 9,

10) Initially, Defendants answered the complaint through their counsel, B. Gray Gibbs. (Dkt. 11) Thereafter, Mr. Gibbs withdrew as counsel for both defendants, stating that they were "nonresponsive to requests from counsel for responses to Plaintiff's discovery requests." (Dkt. 19) Plaintiff asserts that after counsel withdrew, it attempted to contact Covington directly numerous times but never received any response. (Dkt. 29 at 3) Thus, on February 21, 2014 the United States moved to compel Covington's response to the discovery requests. (Dkt. 21) Covington failed to respond to the motion to compel or appear at the hearing on the motion. (Dkt. 23) In the Order compelling the responses, the Court advised that "upon Ms. Covington's failure to comply with this Order, the undersigned will recommend that default be entered against Defendants." (Dkt. 24) Defendants subsequently failed to comply with the Order, (Dkt. 25), and Magistrate Judge McCoun then entered a *sua sponte* Report and Recommendation ("R&R") recommending that a default be entered against Defendants due to their refusal to comply with their discovery obligations and the Court's Order, and their complete abandonment of a defense. (Dkt. 26) Subsequently, this Court adopted the Magistrate Judge's R&R, ordered the Defendants' Answer stricken, directed the clerk to enter default against both Defendants, and directed the United States to file a motion for a permanent injunction. (Dkt. 27)

A review of the docket also reveals that all orders mailed to Covington since May 9, 2014, have been returned as undeliverable, including both the Order compelling the discovery responses and the R&R recommending default. Likewise, Plaintiff notes that "[m]ail sent to her address has been returned to the United States." (Dkt. 29 at 3 n.3) Plaintiff represented to Judge McCoun that some of the mail it sent to Covington was

"returned as refused," and it also attempted to contact Covington via a telephone number that had been provided by former defense counsel, but no response was received from Defendants, despite Plaintiff leaving voicemails. (Dkt. 26 at 3)

II. Legal Standard and Analysis

Pursuant to Rule 55, to enter a default judgment, there must be a sufficient basis in the pleadings to support the relief sought. "The defendant is not held to admit facts that are not well-pleaded or to admit conclusions of law. In short . . . a default is not treated as an absolute confession of the defendant of his liability and of the plaintiff's right to recover." Nishimatsu Constr. Co., Ltd. v. Houston Nat'l Bank, 515 F.2d 1200, 1206 (5th Cir. 1975).[1] If the facts in the complaint are sufficient to establish liability, then the court must conduct an inquiry to ascertain the amount of damages. See Adolph Coors Co. v. Movement Against Racism & the Klan, 777 F.2d 1538, 1543-44 (11th Cir. 1985). Damages may be awarded only if the record adequately reflects the basis for the award via a hearing or a demonstration of detailed affidavits establishing the necessary facts. See id. at 1544.

Plaintiff brought a three-count Complaint for a permanent injunction against Defendants, seeking (1) an injunction under 26 U.S.C. § 7407 for conduct subject to penalty under 26 U.S.C. § § 6694, 6695; (2) an injunction under 26 U.S.C. § 7408 for conduct subject to penalty under 26 U.S.C. § 6701; and (3) an injunction under 26 U.S.C. § 7402 for unlawful interference with the enforcement of internal revenue laws. In the instant motion, Plaintiff seeks an injunction under sections 7407 and 7402 only. (Dkt. 29

1 In Bonner v. City of Prichard, 661 F.2d 1206, 1209 (11th Cir. 1981), the Eleventh Circuit adopted as binding precedent all decisions of the former Fifth Circuit handed down prior to the close of business on September 30, 1981.

at 10 n.6) ("Count II seeks an injunction against specified conduct pursuant to 26 U.S.C. § 7408. If the relief herein is granted, there will be no need for an injunction to issue under that section.")

"[I]n order to issue an injunction pursuant to § 7407, three prerequisites must be met: first, the defendant must be a tax preparer." United States v. Ernst & Whinney, 735 F.2d 1296, 1303 (11th Cir. 1984). "The term 'tax return preparer' means any person who prepares for compensation, or who employs one or more persons to prepare for compensation, any return of tax imposed by this title or any claim for refund of tax imposed by this title." 26 U.S.C. § 7701(a)(36)(A). "Second, the conduct complained of must fall within one of the four areas of proscribed conduct, § 7407(b)(1); and third, the court must find that an injunction is 'appropriate to prevent the recurrence' of the proscribed conduct, § 7407(b)(2)." Ernst & Whinney, 735 F.2d at 1303. Here, Plaintiff argues that Covington repeatedly ran afoul of conduct proscribed by § 7407(b)(1)(A), that is, conduct in violation 26 U.S.C. § 6694, which prohibits a "tax return preparer" from preparing any return or claim of refund that results in an "understatement of liability,"[2] and is done without "substantial authority for the position." 26 U.S.C. § 6694(a). Willful or reckless violations of § 6694 result in penalties of $5,000 or "50 percent of the income derived (or to be derived) by the tax return preparer with respect to the return or claim," for each such claim or return. 26 U.S.C. § 6694(b).

Because section 7407 "expressly authorizes the issuance of an injunction, the traditional requirements for equitable relief need not be satisfied." United States v.

2 "[T]he term 'understatement of liability' means any understatement of the net amount payable with respect to any tax imposed by this title or any overstatement of the net amount creditable or refundable with respect to any such tax." 26 U.S.C. § 6694(e).

Gleason, 432 F.3d 678, 682 (6th Cir. 2005); see also, e.g., United States v. Estate Pres. Services, 202 F.3d 1093, 1098 (9th Cir. 2000) ("The traditional requirements for equitable relief need not be satisfied since Section 7408 expressly authorizes the issuance of an injunction."); United States v. Prater, 96 A.F.T.R.2d 2005-6284, at *5 (M.D. Fla. 2005) ("Because IRC §§ 7407 and 7408 set forth the criteria for injunctive relief, the United States need only meet those criteria, without reference to the traditional equitable factors, for an injunction to issue under these sections.").

Conversely, "the decision to issue an injunction under § 7402(a) is governed by the traditional factors shaping the district court's use of the equitable remedy." Ernst & Whinney, 735 F.2d at 1301. This section has been "used to enjoin interference with tax enforcement even when such interference does not violate any particular tax statute." Id. Section 7402 gives the district courts power to issue injunctions as may be necessary or appropriate for the enforcement of the internal revenue laws of the United States. Id. at 1300; Prater, 96 A.F.T.R.2d 2005-6284, at *5.

Thus, to succeed on this claim, Plaintiff must demonstrate:

> (1) that it has suffered an irreparable injury; (2) that remedies available at law, such as monetary damages, are inadequate to compensate for that injury; (3) that, considering the balance of hardships between the plaintiff and defendant, a remedy in equity is warranted; and (4) that the public interest would not be disserved by a permanent injunction.

eBay Inc. v. Mercexchange, L.L.C., 547 U.S. 388, 391 (2006).

The Complaint alleges the following: Covington prepares income tax returns, including Form 1040, "Individual Income Tax Return," for other taxpayers through her company, Jeanne's Tax. (Dkt. 1 at ¶¶ 5–6) Covington has prepared tax returns for others for approximately ten years. Before operating her own business, she worked for

a local office of Liberty Tax Service. She is a college graduate with degrees from North Carolina State University and the University of South Florida. (Id. at ¶ 7) Covington promoted her business through the website www.reduceyourtaxesfl.com, which is no longer active. (Id. at ¶ 8) Covington has falsely stated to some of her customers that she is a CPA or former employee of the Internal Revenue Service ("IRS"). (Id. at ¶ 9)

In 2007, the IRS opened a preparer project against Covington. (Id. at ¶ 4) As part of that project, investigators audited some of Covington's customers and discovered that many of their returns reported expenses that were grossly inflated or fictitious, and in many cases Covington's customers could not provide substantiation for the items Covington included on their returns. (Id.) Based on its findings in the preparer project, the IRS assessed $355,000 in preparer penalties against Covington under 26 U.S.C. § 6694(b). (Id. at ¶ 15) The penalties were based on over 85 returns prepared by Covington for the tax years 2005 through 2008. (Id.)

IRS records show that from calendar years 2009 to 2012, Covington prepared approximately 4,045 Form 1040 returns. The number of returns Covington prepared in each calendar year is as follows:

Year	Number of Returns
2012	918
2011	1,025
2010	889
2009	1,213

(Id. at ¶ 10) Most of the income tax returns prepared by Covington that the IRS has examined understate the filing taxpayer's liability by falsely claiming or inflating tax credits or fabricating deductions. (Id. at ¶ 11) IRS investigators examined a second sample of over 500 returns prepared by Covington for tax years 2009 through 2011. (Id. at ¶ 17) Of those returns, all but nine were found to have either underreported tax liability or overstated the amount of the refund to which the taxpayer was entitled—a 98% error rate. (Id.) On average, the erroneous returns that Covington prepared for tax years 2009 through 2011 understated the client's liability by over $3,700. (Id. at ¶ 18)

The returns prepared by Covington for Daniel Burtch and Sarah Isbell are fair exemplars of Covington's scheme. (Id. at ¶¶ 19–29) Covington reported the following deductions:

Deduction	Amount reported on return (year)
Medical expenses	$5,880 (2010)
Cash contributions to charity	$1,500 (2009) $1,000 (2010)
Employee-business expenses	$15,208 (2009) $8,536(2010)
Schedule C operating expenses	$7,472 (2010)

Burth and Isbell did not provide Covington or her office with any medical-expense information, charitable cash contribution documentation, or schedule C business operating expenses documentation, and only provided $327.70 worth of employee-business expenses documentation. (Id. at ¶¶ 22–26) Thus, Covington knew or should have known that the returns overstated those deductions. (Id.) Likewise, Covington also caused Burtch and Isbell's 2009 income tax returns to falsely claim a $1,500 residential energy credit available to taxpayers who make certain energy-saving

improvements to their home, despite Burtch and Isbell never having made such expenditures nor indicating to Covington that they had. (Id. at ¶ 27) Plaintiff alleges that Burtch and Isbell's "returns are typical of the vast majority of returns prepared by Covington in that they report deductions which are false or unsubstantiated and claim tax credits to which the taxpayer is not entitled." (Id. at ¶ 29)

By virtue of the default, each of the above allegations are admitted. The admitted allegations amply show that Covington prepared tax returns that significantly understated tax liability. Likewise, these understatements were without substantial justification and were done either recklessly or willfully, in light of the fact that the individuals provided no documentation for the deductions and/or credits. Further, because Covington continued to prepare false returns even after the IRS levied significant penalties against her, the Court finds that an injunction is necessary to prevent the recurrence of the proscribed conduct. Moreover, the Court agrees with Plaintiff that a narrow injunction, limited solely to preventing further understatements of liability, would be insufficient to prevent Covington's interference with the proper administration of the internal revenue laws. The Court finds that Covington has continually and repeatedly engaged in conduct proscribed by § 7407, that an injunction prohibiting such conduct would not be sufficient to prevent Covington's further interference with the proper administration of the internal revenue laws, and thus the Court will enjoin Covington from acting as a tax return preparer.

The Court also finds that Plaintiff has met its burden for an injunction under 26 U.S.C. § 7402. Covington's continuous and repeated filing of federal tax returns with fraudulent claims on behalf of her customers constitutes irreparable harm. Unless enjoined, Covington will likely continue to engage in improper conduct and interfere with

the enforcement of internal revenue laws. Plaintiff will suffer irreparable harm by paying federal income tax refunds to individuals who are not entitled to receive them and by devoting its limited resources to identifying future customers, ascertaining their correct tax liabilities, recovering any refunds erroneously issued, and collecting any additional taxes and penalties. (Dkt. 1 at ¶¶ 30–34) Covington's customers will be harmed because they pay Covington fees to prepare tax returns that substantially understate their correct tax liabilities.

The Court finds that considering the balance of hardships between the Plaintiff and Defendants, a permanent injunction is warranted, and that such an injunction would serve the public interest by preventing Covington from further damaging the Plaintiff and the individuals for whom Covington prepares tax returns.

III. Conclusion

Upon consideration of the foregoing, it is hereby **ORDERED** as follows:

1. Plaintiff's Motion for Default Permanent Injunction (Dkt. 29) is **GRANTED.**
2. Pursuant to 26 U.S.C. §§ 7402(a) and 7407 defendant Jeanne Covington, and any other person working in concert or participation with her directly or indirectly, is **PERMANENTLY ENJOINED** from directly or indirectly preparing, assisting in the preparation of, or directing the preparation of federal income tax returns, amended returns, claims for refund, 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;
3. The United States will be allowed full post-judgment discovery to monitor compliance with the permanent injunction; and

4. The Court will retain jurisdiction over this action for purposes of implementing and enforcing the permanent injunction and any additional orders necessary and appropriate to the public interest.

5. The **CLERK** is directed to **TERMINATE** any pending motions and **CLOSE** this case.

DONE and **ORDERED** in Tampa, Florida, this 17th day of September, 2014.

MARY S. SCRIVEN
UNITED STATES DISTRICT JUDGE

Copies furnished to:
Counsel of Record
Any Unrepresented Person