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**IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF CALIFORNIA
SAN FRANCISCO DIVISION**

UNITED STATES OF AMERICA,

Plaintiff,

v.

EDWIN LICHTIG, III, individually and d/b/a, GSL ADVISORY SERVICES,

Defendant.

CV 08 5210 CW

Civil No.

Nature of Action

1. This is a civil action brought by the United States of America under §§ 7402 and 7408 of the Internal Revenue Code (26 U.S.C.) (I.R.C.) to enjoin the defendant, Edwin Lichtig, III, individually and d/b/a GSL Advisory Services, and all those in active concert or participation with him, from promoting tax-fraud schemes.

Jurisdiction

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, under the provisions of I.R.C. §§ 7402 and 7408.

3. Jurisdiction exists under 28 U.S.C. §§ 1340 and 1345 and I.R.C. §§ 7402(a) and 7408.

Defendant

4. Edwin Lichtig resides in Lafayette, California.

5. Lichtig conducts business at 1601 North Main Street, Suite 207, Walnut Creek, California, 94596, using the business name GSL Advisory Services.

6. Venue is proper in this Court under 28 U.S.C. § 1391(b)(1) because the defendant resides or conducts business within this judicial district, and a substantial part of the actions giving rise to this suit took place and are taking place in this district.

Lichtig's Promotion of His Fraudulent Schemes

7. Lichtig is an insurance salesman who individually and through his business, GSL Advisory Services, since 1992, promotes and advises customers and other insurance salesmen regarding several types of fraudulent tax schemes, which are described in detail below.

8. Lichtig and his company GSL employ and train 53 agents nationwide. These agents help Lichtig market, promote, and sell his tax schemes.

9. Lichtig promotes his schemes and advises his customers through seminars, telephone conferences, his GSL website, writing articles that are published in trade journals, promotional materials, and by training other insurance agents to market and sell his tax schemes.

10. Lichtig charges non-GSL insurance agents $4,000 plus a 40%–50% commission to sell his tax schemes/instructions to other customers.

11. Lichtig created and distributed a tax scheme video instruction package called, "Ed Lichtig, insurance actuary shows you how to buy life insurance inside a retirement plan with pre-tax dollars." The advertisement said "Watch how much easier it is to sell insurance when you show clients that the IRS will share the cost with them when they use pre-tax retirement funds." The advertisement was distributed in an e-mail dated July 12, 2005.

12. Specifically, Lichtig promotes two different tax schemes, both of which improperly use untaxed retirement dollars in IRA accounts to drastically under-report income generated by taxable transactions. Lichtig calls his tax schemes the Pension Asset Transfer (PAT) plan and the Financed Roth Conversion Strategy (FROCO) plan.

Pension Asset Transfer (PAT) Scheme

13. Lichtig's PAT scheme uses specially designed life insurance policies to sharply reduce his customers' tax liability on untaxed retirement assets.

14. More specifically, Lichtig promotes, teaches, and sells to customers and other insurance agents the following steps of his PAT scheme:

a. First, Lichtig and his promotional agents recruit customers who have retirement assets in traditional IRAs. These customers have not paid taxes on the money in their traditional IRAs because money deposited into traditional IRAs is tax exempt until it is later removed from the IRA. IRC § 219.

b. Next, Lichtig or his agents advise their customers to establish a sham business, which is needed to perform subsequent steps in Lichtig's scheme. To make the sham business appear legitimate, Lichtig and his agents instruct their customers to

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claim that the purported business purpose of the sham business is to provide leads and referrals to the life insurance agent (Lichtig or others) who helped the customer set up the scheme. And in exchange, to show a revenue in the sham business, the life insurance agent pays $500 annually into the sham business. These businesses are shams because they are set up for the sole purpose of facilitating the PAT scheme transaction. *See* Treasury Regulation 1.401-1(b)(2).

c. Next, Lichtig or his agents assists the customer in establishing a self-employed retirement plan under IRC § 401(a) for his sham business. The self-employed retirement plan is needed to facilitate subsequent steps in Lichtig's PAT scheme.

d. The customer needs a specially designed life insurance plan to take advantage of the PAT scheme, but he cannot purchase the life insurance plan using his traditional IRA money. IRC § 408(c). Therefore, Lichtig advises his customers to transfer their money out of the IRA and into the customer's self-employed retirement plan, from which they can purchase Lichtig's special life insurance plan.

e. The transfer of money from the IRA into the self-employed retirement plan is not a taxable transaction. Thus, at this stage in the scheme, the money has not yet been taxed.

f. Lichtig or agents then sell to the customer specially designed life insurance plans, which have high surrender penalties for cashing in the policy within three to five years after the customer purchases the policy. The surrender penalties are equal to 30%-50% of the total value of the policy.

g. The customer appoints himself the sole beneficiary of the life insurance policy.

h. While the life insurance policy is still subject to surrender penalties, the customer directs the self-employed retirement plan to distribute the insurance policy to himself. For this distribution, the customer must report as income the value of the life insurance plan that was distributed to him. IRC § 61.

i. However, instead of reporting the full and actual value of the life insurance policy, Lichtig and his associates advise their customers to report a lesser amount. Specifically, they instruct customers to subtract the surrender penalty amount (i.e., 30%–50%) from the total value of the life insurance policy, and report only the difference as income. As a result, the customer improperly reports as income only 50% – 70% of the actual value of the life insurance assets that were distributed to him.

j. Lichtig argues to his customers, agents, and the IRS that this reduction in value for income reporting purposes is acceptable because, at the time the life insurance policy is distributed to the customer, it is not worth the full amount. Instead, Lichtig contends, the policy is only worth the potential cash-in value at the time of the transaction, and therefore the customer should only report that reduced amount.

k. Using Lichtig's scheme, after the surrender penalty period expires, the customer can cash in the policy for the true and actual value without paying any more taxes.

l. In the end, by using Lichtig's PAT scheme, customers improperly reduce their tax liability on money in IRA accounts by 30% – 50%.

Financed Roth Conversion Strategy (FROCO) Scheme

15. The FROCO scheme is similar to the PAT scheme in that Lichtig uses both schemes to improperly reduce his customers' tax liability on retirement money held in traditional IRAs.

16. Specifically, the FROCO scheme, which Lichtig promotes, consists of the following steps:

a. First, Lichtig and his promotional agents recruit customers who have retirement assets in a traditional IRAs. Once again, these customers have not paid taxes on the money in traditional IRAs because money deposited into traditional IRAs is tax exempt until it is removed from the IRA. IRC § 219.

b. Next, Lichtig or his agents instruct the customer to purchase an annuity using the money in the traditional IRA, and keeps the annuity in the traditional IRA. Lichtig and his associates sell specially designed annuities to their customers. Similar to the life insurance policies that Lichtig uses in the PAT scheme, here Lichtig sells annuities that impose high surrender penalties if the customer cashes in the annuity before the surrender penalty period expires. The penalties attached to these annuities are 10%-25% of the value of the annuity.

c. The customer then transfers the annuity from the traditional IRA into a Roth IRA. A Roth IRA is a retirement account in which taxes are imposed before the money is deposited into the account, as opposed to being taxed when the money is withdrawn from the account, as is the case with traditional IRAs.

d. Accordingly, when the customer transfers the annuity from the traditional IRA into the Roth IRA, the customer must report as income the value of the annuity that was transferred into the Roth IRA. 26 U.S.C. § 408A(c)(1). The law allows taxpayers to transfer assets from traditional IRAs to Roth IRAs. 26 U.S.C. § 408A(c)(3)(B).

e. Instead of reporting the true value of the annuity, however, Lichtig and his associates advise their customers to report a reduced amount. Specifically, they instruct their customers to subtract the surrender penalty amount (i.e., 10%–25%) from the total value of the annuity, and only report the difference. As a result, the customer only reports as income 75% – 90% of the true value of the annuity that he

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transferred into the Roth IRA. Consequently, the customer improperly avoids paying taxes on a large portion of the transferred annuity.

f. After the surrender penalty period lapses, the customer cashes in the annuity at its full value, without paying additional tax. 26 U.S.C. § 408A(d).

g. In the end, Lichtig's FROCO scheme improperly reduces his customer's tax liability on the annuity by 10%-25%.

Lichtig's False Statements

17. Lichtig and his associates have made multiple false and fraudulent statements, written and spoken, while promoting and selling his tax schemes.

18. During a live seminar presentation to insurance agents in or around 2004, Lichtig delivered a lecture about his PAT and FROCO schemes. During the lecture, Lichtig made multiple false statements about his schemes, including (1) a false statement that it is permissible for retired customers who have not been employed for 10 years to set up businesses for the sole purpose of facilitating his PAT scheme; (2) in his PAT scheme, it is permissible for insurance agents to pay the customers $500 annually in exchange for one referral a year from the customer to make the sham business appear legitimate.

19. Lichtig's statements in paragraph 18, above, are false because Treasury Regulation 1.401-1(b)(2) states that such self-employed retirement plans cannot be "temporary." The regulation states that evidence of temporary plans includes the abandonment of the retirement plan for reasons other than business necessity, and one-time contributions to the plan. Lichtig's PAT scheme fits this definition of "temporary" because his customers abandon their self-employed retirement plans after they siphon their money through the plan. Moreover, the PAT scheme only calls for one contribution to the retirement plan,

which is additional evidence that the plan does not satisfy the Treasury Regulations detailed above.

20. In 2004, Lichtig's GSL website contained numerous false statements, including:

a. Claims that it is permissible for retired persons to set up businesses and self-employed retirement plans for the sole purpose of purchasing life insurance contracts as part of his PAT scheme. These are false statements because, as detailed above, Treasury Regulation 1.401-1(b)(2) prohibits the use of temporary self-employed retirement plans such as these;

b. Statements that the IRS had approved his improper PAT and FROCO schemes. This is false because the IRS has never approved any of Lichtig's schemes; and

c. Statements that customers can lawfully reduce their tax liability by using the life insurance policies and annuities offered in his schemes. These are false statements because Treasury Regulation 1.408A-4T makes clear that, when reporting income from transactions in which assets/annuities are transferred into a Roth IRA, a taxpayer cannot reduce the income derived from the transaction by subtracting the surrender penalty, as Lichtig has promoted and advised customers and other insurance salesmen to do. Instead, customers must claim the fair market value of the annuity using a formula set forth in Treasury Regulation 1.408A-4T.

21. On his website (www.gsladvisory.com), Lichtig posted promotional videos and seminars in which Lichtig and other agents made similar false statements in describing, promoting, and selling the PAT and FROCO schemes.

22. Lichtig has created and distributed brochures about his PAT scheme containing false statements that the PAT scheme can lawfully reduce tax liability up to 50%, and that the IRS has approved the PAT scheme.

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23. In February 2000, Lichtig co-authored an article with another employee of GSL that contained false statements concerning the PAT scheme. Specifically, Lichtig's article falsely stated that when his customers report income, they can reduce the amount reported as income by subtracting the value of the surrender penalties on the policies from the total value of the policies, as described above. This is false because, once again, Treasury Regulation 1.408A-4T prohibits such reductions.

24. In July 2005, Lichtig sent out a promotional e-mail in which he claimed that the IRS will "share the cost" of insurance purchases with his customers when the customers use pre-tax retirement funds to buy life insurance, referring to the reduced tax liabilities caused by his PAT scheme. This is false because the IRS does not "share the cost" of any such schemes, unless it does so unwillingly as a result of the unlawful schemes.

25. Lichtig also made other false statements in connection with the promotion of his tax schemes.

Knowledge

26. Lichtig has been a licensed insurance salesman for over twenty years, and during that time he held himself out as a tax expert at conferences promoting the PAT and FROCO schemes. He has an MBA in finance, and has taken additional classes in insurance, finance, and estate planning. Lichtig therefore knows or has reason to know that the statements about tax benefits that he makes in promoting the tax-fraud schemes were false or fraudulent.

27. As a practicing insurance salesman, Lichtig is knowledgeable about federal income tax laws. He has specialized in the promotion of tax-reduction strategies related to insurance annuities for over twenty years.

28. Lichtig claims he has received continuing business and tax-law education and that he has conducted personal research and self-study regarding the internal revenue laws.

29. Lichtig has published articles regarding tax-reduction strategies in insurance and tax journals.

30. Lichtig knew, or had reason to know, that his false statements described in this complaint were false or fraudulent.

Harm to the Government

31. Lichtig and GSL, the organization through which he promoted the tax-fraud schemes discussed above, have at least 250 customers across the United States.

32. Lichtig's schemes harm the United States by fraudulently reducing the amounts of federal income tax that customers report and pay. The IRS estimates that Lichtig's customers have failed to report at least $25 million in income. To reach that estimate, the IRS used customer information that Lichtig provided; the IRS added up the total amount of potentially unreported income for Lichtig's known customers who used his schemes. Audits are ongoing.

33. The United States is further harmed because the IRS must dedicate its scarce resources to the detection and examination of the inaccurate returns filed by Lichtig's customers as a result of his tax-fraud schemes, and in the assessment and collection of unpaid taxes.

34. Lichtig's misconduct is likely to recur unless he is permanently enjoined from promoting these types of schemes.

Count I: Injunction under I.R.C. § 7408 for violations of §§ 6700 and 6701

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

36. Section 7408, I.R.C., authorizes this Court to enjoin persons who have engaged in conduct subject to penalty under I.R.C. §§ 6700 or 6701 from engaging in further such conduct if the Court finds that injunctive relief is appropriate to prevent recurrence of the conduct.

37. Section 6700, I.R.C., imposes a penalty on any person who organizes or participates in the sale of a plan or arrangement and, in so doing, makes a statement with respect to the allowability of any deduction or credit, the excludability of any income, or the securing of any tax benefit by participating in the plan or arrangement which that person knows or has reason to know is false or fraudulent as to any material matter.

38. Section 6701, I.R.C., penalizes a person who aids or assists in, procures, or advises with respect to the preparation or presentation of any portion of a return or other document, knowing or having reason to believe that such document will be used in connection with any material matter under the tax laws, and knowing that such portion, if used, would result in an understatement of another person's tax liability.

39. Lichtig has sold, promoted, and organized tax-fraud schemes that falsely promise tax benefits to customers.

40. In selling, promoting, and organizing these schemes, Lichtig has made false or fraudulent statements to customers regarding the tax benefits of the schemes.

41. Lichtig knew or had reason to know that these statements were false or fraudulent statements within the meaning of 26 U.S.C. § 6700.

42. If he is not enjoined, Lichtig is likely to continue to sell, promote, and organize tax-fraud schemes.

43. In promoting, organizing, and selling the PAT and FROCO tax fraud schemes discussed above, Lichtig knew or had reason to know that his customers would use the schemes to

understate their tax liability on their individual federal income tax returns, within the meaning of 26 U.S.C. § 6701.

44. Injunctive relief is appropriate to prevent recurrence of this conduct.

Count II: Injunction Under I.R.C. § 7402

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

46. Section 7402(a), I.R.C., authorizes a court to issue injunctions as may be necessary or appropriate for the enforcement of the internal revenue laws, even if the United States has other remedies available for enforcing those laws.

47. Lichtig substantially interferes with the enforcement of the internal revenue laws by promoting his tax-fraud schemes.

48. Lichtig's conduct results in irreparable harm to the United States for which the United States has no adequate remedy at law.

49. Unless enjoined by this Court, Lichtig is likely to continue to engage in illegal conduct. The Court should grant injunctive relief under I.R.C. § 7402(a).

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

A. That this Court, under 26 U.S.C. §§ 7402 and 7408, enter a permanent injunction prohibiting Lichtig, individually and doing business under any other name, or using any other entity, and his representatives, agents, servants, employees, attorneys, and anyone in active concert or participation with him, from directly or indirectly:

(1) organizing (or assisting in organizing) or participating, directly or indirectly, in the sale or promotion of the PAT and FROCO plans;

(2) organizing (or assisting in organizing) or participating, directly or indirectly, in the sale of any interest in any other entity, plan, or arrangement, that assists customers to attempt to violate the internal revenue laws or unlawfully evade the assessment or collection of their federal tax liabilities or unlawfully claim improper tax refunds;

(3) engaging in activity subject to penalty under 26 U.S.C. § 6700, including making, in connection with the organization or sale of any plan or arrangement, any statement about the securing of any tax benefit that the defendant knows or has reason to know is false as to any material matter;

(4) engaging in conduct subject to penalty under any provision of the Internal Revenue Code, or engaging in any other conduct that interferes with the administration and enforcement of the internal revenue laws; and

(5) misrepresenting the terms of this injunction.

B. That this Court allow the United States post-judgment discovery to ensure Lichtig's compliance with the permanent injunction;

C. That this Court retain jurisdiction over this action for the purpose of implementing and enforcing this permanent injunction; and

D. That this Court grant the United States such other and further relief as the Court deems just and appropriate.

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