

UNITED STATES DISTRICT COURT
FOR THE
DISTRICT OF CONNECTICUT

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TOWN OF WESTPORT)	CASE NO. <u>3:23-cv-1205</u>
)	
Plaintiff,)	
)	
vs.)	September 13, 2023
)	
UNITED STATES OF AMERICA,)	
)	
Defendant.)	
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Complaint

The Town of Westport, Connecticut (“Plaintiff”) brings this action against Defendant, the United States of America (“Defendant”) and for its claims respectfully alleges as follows:

I. PARTIES

1. Plaintiff is a municipal corporations and a political subdivision of the State of Connecticut, created pursuant to the laws of the State of Connecticut.
2. Defendant is the United States of America, by its agency, the Internal Revenue Service (“IRS”).
3. For purposes of reporting to the IRS, Plaintiff’s Employer Identification Number is 06-6002128, which is reflected on all returns and claims described below.
4. The actions complained of herein were taken by representatives of the Commissioner of Internal Revenue.

II. JURISDICTION AND VENUE

5. This is an action under the Internal Revenue Code (“IRC”) for the recovery and refund of federal employment taxes, accrued interest, and penalties erroneously and illegally assessed against and collected from Plaintiff, including, but not limited to, tax refunds which have been

assessed and withheld by the IRS, pursuant to the Claims for Refunds filed in accordance with the law and regulations thereof, for taxable quarters ended March 31, 2020 (“Q1 2020”) and December 31, 2020 (“Q4 2020”) (collectively the “Refund Claims”).

6. This Court has jurisdiction over the subject matter of this complaint pursuant to the following statutory provisions:

- a. 28 U.S.C. 1331 (Judicial Code, federal question jurisdiction);
 - b. 28 U.S.C. 1340 (Judicial Code jurisdiction concerning internal revenue laws);
 - c. 28 U.S.C. 1346(a)(1) (Judicial Code jurisdiction concerning the recovery of erroneously or illegally assessed or collected internal revenue taxes); and
 - d. 26 U.S.C. 7422 (Internal Revenue Code jurisdiction for civil action for refund).
7. Venue is proper in the United States District Court for the District of Connecticut pursuant to 28 U.S.C. § 1402(a)(2) because the Plaintiff is located in Connecticut and the conduct occurred in Connecticut.

III. FACTUAL BACKGROUND

A. The Q1 2020 Claim for Refund

8. The Town’s assessed payroll tax liability for Q1 2020 was \$4,519,904.16.
9. During Q1 2020, the Town deposited \$4,519,607.91 in normal payroll tax deposits for that respective quarter.
10. The Town timely filed its Q1 2020 Form 941 on May 7, 2020.
11. On April 1, 2020, the Town made its first payroll tax deposits for the taxable quarter ended June 30, 2020 (“Q2 2020”) in the amounts of \$354,302.28 and \$88,440.90.
12. The IRS initially incorrectly credited the \$354,302.28 and \$88,440.90 deposits to Q1 2020 instead of Q2 2020.

13. The IRS then removed from Q1 2020 and transferred to Q2 2020 the \$354,302.28 and \$88,440.90 deposits.
14. Although the Town had timely filed its Q1 2020 Form 941 and paid in full substantially all Q1 2020 payroll taxes,¹ the IRS subsequently lost and failed to process the Town's timely filed Q1 2020 Form 941.
15. As a result, the IRS erroneously treated the \$4,519,607.91 balance of the Town's Q1 2020 payroll deposits as a "credit," presumably because it could not attribute such deposits to a Form 941 on file.
16. Without notifying the Town, the IRS initiated a series of transfers totaling \$385,158.65 from the Town's Q1 2020 payroll deposit balance to other taxable periods, creating an artificial deficit.
17. On April 30, 2020, the IRS erroneously transferred \$113,300 from Q1 2020 to the taxable period ended December 31, 2018 ("Q4 2018") to pay a civil penalty purportedly attributable to Q4 2018 (the "Q4 2018 Civil Penalty").
18. The IRS did not send the Town a Notice of Proposed Penalty for the Q4 2018 Civil Penalty until September 21, 2020, which was nearly five months *after* it had transferred the \$113,300 credit out of Q1 2020 to pay for it.
19. A Notice of Penalty Charge for the Q4 2018 Civil Penalty was not sent to the Town until on or about January 18, 2021, meaning that the Q4 2018 Civil Penalty was not formally assessed against the Town until approximately 9 months *after* the \$113,300 credit had been transferred from Q1 2020 to pay for it.

¹ At the end of Q1 2020, there was a \$296.25 shortfall between the Town's assessed payroll tax liability of \$4,519,904.16 and its payroll deposit balance for Q1 2020 of \$4,519,607.91.

20. By failing to provide the Town with notice before transferring \$113,300 from Q1 2020 to pay for the Q4 2018 Civil Penalty, the IRS deprived the Town of its right and opportunity to appeal or seek a waiver of the penalty and/or request further information surrounding the Q4 2018 Civil Penalty.
21. Thus, the IRS' transfer of \$113,300 from Q1 2020 to Q4 2018 was unjustified, improper, and erroneous.
22. On April 30, 2020, the IRS also transferred \$73,503.34 from Q1 2020 to the taxable period ended December 31, 2019 ("Q4 2019").
23. The Town's assessed tax liability for Q4 2019 was \$5,247,023.95.
24. The Town deposited \$5,251,944.38 through normal payroll tax deposits during Q4 2019.
25. This resulted in an overpayment by the Town of \$4,920.43 for its Q4 2019 payroll tax liability.
26. In light of the Town's overpayment of its payroll tax liability during the quarter, there was no deficit at the end of Q4 2019.
27. Since there was no deficit at the end of Q4 2019, the IRS should not have transferred \$73,503.34 from Q1 2020 to Q4 2019.
28. Thus, the IRS' transfer of \$73,503.34 from Q1 2020 to Q4 2019 was unjustified, improper, and erroneous.
29. On April 30, 2020, the IRS also transferred \$198,355.31 from Q1 2020 to Q3 2020.
30. Q3 2020 had not begun at the time the IRS made this transfer.
31. No payroll tax deposits were due for Q3 2020 at the time the IRS made this transfer.
32. The Town had not made any payroll tax deposits for Q3 2020 at the time the IRS made this transfer.

33. The Town's Q3 2020 Form 941 was not yet due and had not yet been filed by the Town at the time the IRS made this transfer.
34. Thus, the IRS' transfer of \$198,355.31 from Q1 2020 to Q3 2020 was unjustified, improper, and erroneous.
35. In sum, the IRS erroneously transferred \$113,300, \$73,503.32, and \$198,355.31 to other taxable periods instead of applying such amounts towards the Town's Q1 2020 \$4,519,904.16 payroll tax liability.
36. Since the IRS failed to provide the Town with notice in advance, these transfers were improper under law. See Ahmed v. Comm'r of IRS, 3d Cir., No. 22-1091, April 7, 2023.
37. As a result of the IRS' improper transfers, the balance of the Town's Q1 2020 payroll tax deposit account was reduced to \$4,134,449.26.
38. By making the improper transfers, the IRS created an artificial deficit for Q1 2020 of \$385,158.65.
39. Since all payroll taxes due had been timely deposited during the quarter for Q1 2020, the Town reasonably operated on a good faith basis that its subsequent payments were satisfying the principal balance owed for each respective quarter and avoiding the accrual of additional penalties, interest, and fees.
40. The IRS subsequently transferred three interest credits totaling \$10,235.03 from other quarters to the Town's Q1 2020 payroll tax balance, which reduced the artificial deficit to \$374,923.62.
41. The IRS then assessed that the Town had failed to pay \$375,219.87 in payroll taxes for Q1 2020, which was comprised of the \$374,923.62 erroneous deficit and the legitimate \$296.25 shortfall previously acknowledged by the Town.

42. The IRS subsequently assessed \$13,132 in penalties and \$10,051.96 in interest against the Town on the \$375,219.87, increasing the Town's assessed liability for Q1 2020 to \$398,404.53.
43. An additional \$20,681.49 in penalties and \$382.19 in interest were then assessed by the IRS, bringing the Town's total purported unpaid payroll tax liability for Q1 2020 to \$419,468.21.
44. Notwithstanding the fact that the Town had timely deposited all payroll taxes due for Q1 2020, with the exception of the legitimate \$296.25 shortfall, the Town continued to receive inaccurate notices reflecting a balance of unpaid taxes, penalties, and interest for Q1 2020.
45. The information provided by the IRS in conjunction with the assessed penalties, interest, and fees was untimely, incomplete, inaccurate, and inconsistent, which made it impossible for the Town to ascertain how or why such amounts were being assessed when all tax due had been timely paid.
46. The Town attempted to contact the IRS on numerous occasions to determine why it was continuing to receive inaccurate notices reflecting a balance of unpaid taxes, penalties, and interest for Q1 2020 when it had accurately and timely deposited substantially all tax due, but did not receive a response.
47. On September 30, 2022, the Town spoke with IRS agent badge #1003959721 who confirmed that there was a balance due for Q1 2020 of \$423,186.97.
48. To avoid being assessed additional penalties and interest, the Town immediately remitted payment in full the same day through the RS' Electronic Federal Tax Payment System.

49. On November 30, 2022 the Town filed a Request for Refund seeking a refund of the \$423,186.97 it paid on September 30, 2022, less the \$296.25 shortfall, and any penalties and interest attributable thereto (the “Q1 2020 Request for Refund”).
50. To date, the Town has not received a response from the IRS regarding its Request for Refund.

B. The Q4 2020 Claim for Refund

51. The Town of Westport’s assessed payroll tax liability for Q4 2020 was \$4,760,473.51.
52. During Q4 2020, the Town paid \$4,761,489.70 through normal payroll tax deposits for that respective quarter.
53. The Town timely filed its Q4 2020 Form 941 on February 1, 2021.
54. Due to an administrative error by its then-payroll clerk, the incorrect amounts were entered into the spreadsheet that was used to compile the Q4 2020 Form 941 information.
55. As a result, the Town’s Q4 2020 Form 941 incorrectly reflected that the Town’s payroll tax liability for Q4 2020 was \$4,551,512.59 instead of the correct amount of \$4,760,473.51.
56. The Town self-identified this error during a review of its accounting reports on March 22, 2021.
57. In response, the Town immediately filed a corrective Form 941x on March 29, 2021 to correct the self-identified errors on its original Q4 2020 Form 941.
58. The Q4 2020 Form 941x reflected that the Town had inadvertently understated its tax liability on the original Q4 2020 Form 941 by approximately \$209,582.31.
59. Notwithstanding that the original Q4 2020 Form 941 inadvertently understated the Town’s Q4 2020 payroll tax liability by approximately \$209,582.31, the Town made its payroll

deposits for Q4 2020 based on the correct amount (\$4,760,473.51), resulting in payroll deposits during Q4 2020 being made in the amount of \$4,761,489.70.

60. While the Town owed \$4,760,473.51, it paid \$4,761,489.70 during Q4 2020, resulting in an *overpayment* of approximately \$1,016.19.
61. Notwithstanding the fact that the Town had timely and accurately deposited all payroll taxes due during Q4 2020, on December 3, 2021, the Town received a Notice CP210 reflecting a \$209,323.97 overpayment on its payroll deposit account and erroneously assessing a \$105,699.97 penalty for failure to make a proper tax deposit.
62. On December 29, 2021, the Town responded to the IRS' Notice CP210 by letter, explaining the errors described above and directing the IRS to review the original Form 941 and the amended Form 941x.
63. At this point in time, the Town had an overpayment of \$1,016.19 on its payroll deposit account for Q4 2020 and no penalties or interest should have been assessed.
64. Since all taxes due for Q4 2020 had been timely paid through regular payroll deposits during the quarter, the Town requested that the IRS waive the erroneously assessed \$105,699.07 penalty.
65. The IRS did not respond to this request.
66. Since the Town had timely paid all payroll taxes due during Q4 2020, it reasonably operated on a good faith basis that its subsequent payments were satisfying the principal balance owed for each respective quarter and avoiding the accrual of additional penalties and interest.
67. On June 10, 2022, the Town received Notice CP128 reflecting that the erroneous \$105,699.07 penalty was still showing as due per IRS records.

68. The Notice CP128 also showed that the IRS had inexplicably transferred in and applied a \$59,790.13 “overpayment” from the taxable period ended December 31, 2019 (“Q4 2019”) to the \$105,699.07 penalty, reducing the amount purportedly due by the Town for Q4 2020 to \$42,505.73.
69. The Town does not know where the Q4 2019 overpayment credit came from since the Town did not have such a substantial overpayment at the end of Q4 2019.
70. The Town does not believe that it was entitled to such an overpayment credit.
71. This uncertainty was further obfuscated by numerous interest and other credits attributable to other tax periods that were periodically added and subtracted from the Town’s Q4 2020 payroll tax deposit balance by the IRS.
72. The Town attempted to contact the IRS numerous times to determine why it was continuing to receive inaccurate notices reflecting an outstanding balance for Q4 2020 when it had timely paid all taxes due through normal payroll deposits during that quarter but did not receive a response.
73. On September 30, 2022, the Town spoke with IRS agent badge #1003959721 who confirmed that there was a balance due for Q4 2020 of \$43,748.27.
74. To avoid being assessed additional penalties and interest, the Town immediately remitted payment in full the same day through the IRS’ Electronic Federal Tax Payment System.
75. On December 23, 2022, the Town filed a Request for Refund seeking a refund of the \$43,748.27 overpayment it made on September 30, 2022 and any penalties and interest attributable thereto (the “Q4 2020 Request for Refund”).
76. To date, the Town has not received a response from the IRS regarding its Request for Refund.

IV. PRAYER FOR RELIEF

WHEREFORE, the Plaintiff prays for a judgment in its favor and demands all refunds amounting to \$466,638.99 in overpaid taxes, penalties, and accrued assessed interest, or such greater amount as the Court may determine, plus accrued statutory interest according to law.

Respectfully Submitted,

THE PLAINTIFF,
TOWN OF WESTPORT

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