

Office of Chief Counsel  
Internal Revenue Service

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**memorandum**

TL-N-7607-97

date: January 21, 1998

to: Associate District Counsel, Kentucky-Tennessee District  
CC:SER:KTY:LOU

from: Assistant Chief Counsel (Field Service) CC:DOM:FS

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subject: Significant Service Center Advice

This responds to your request for Significant Advice received October 23, 1997, in connection with a question posed by the examination function of the Memphis Service Center.

Disclosure Statement

Unless specifically marked "Acknowledged Significant Advice, May be Disseminated" above, this memorandum is not to be circulated or disseminated except as provided in CCDM (35)2(13)3:(4)(d) and (35)2(13)4:(1)(e). This document may contain confidential information subject to the attorney-client and deliberative process privileges. Therefore, this document shall not be disclosed beyond the office or individual(s) who originated the question discussed herein and are working the matter with the requisite "need to know." In no event shall it be disclosed to taxpayers or their representatives.

**Issue(s)**

Whether information provided in a Form 8300 Currency Transaction Report (CTR) provides an adequate basis for issuing a notice of deficiency for unreported income.

**Conclusion**

For the reasons given below, we think that a Form 8300 Currency Transaction Report is insufficient evidence of unreported income and does not provide an adequate basis for issuing a notice of deficiency without additional investigation.

**Facts**

A Currency Transaction Report, Form 8300, is required to be filed by a party who has received in excess of \$10,000 in cash in the course of his or her trade or business from another party. See section 6050I. The Form 8300 must be filed within 15 days of the transaction and the recipient of the cash must provide the payor of the cash with a statement summarizing all such transactions at the end of the calendar year.

The examination division at your local service center has suggested that if a Form 8300 shows that a taxpayer paid \$50,000 in cash for an automobile, the Form 8300 should be matched to his or her return. If the taxpayer's return does not reflect that

income, the service center would issue a CP 2000 or other proposed adjustment letter requesting that the taxpayer explain the apparent discrepancy. If the taxpayer failed to respond, or the response was unsatisfactory, the service center would issue a statutory notice of deficiency, asserting unreported income in the amount of the cash transaction.

### **Discussion**

Underlying the proposed procedures is the presumption that a cash transaction always represents taxable income in the year of the transaction. In fact, the source of a large amount of cash reported by a payee on a Form 8300 may be nontaxable. A payments reported on an information return (Form W-2 or a Form 1099) is, on its face, usually taxable to the individual and can serve as the basis of a statutory notice of deficiency. If the requirements of section 6201(d) are met, the presumption of correctness would attach to such a notice. In contrast to other information returns, CTRs do not indicate the timing, source or circumstances of the receipt of the cash by the taxpayer.

A taxpayer may have access to a large sum of money from a nontaxable source, such as a legacy or a personal injury award. Such a taxpayer may spend a large sum of cash, thereby generating a Form 8300 report. Although most taxpayers use checks to account for their expenditures, the fact that a taxpayer uses cash rather than some other form of payment is not prima facie evidence of a taxable source for the cash.

Moreover, the fact that the taxpayer was in possession of more than \$10,000 in cash at the time of the reported currency transaction does not mean that all or any part of that amount was accumulated, in whatever fashion, during the year it was spent. Proving the nonexistence of a relatively small cash horde is extremely difficult, particularly if the taxpayer has reported earned income over a number of years.

If the Service were to issue a statutory notice of deficiency based solely on the Form 8300 and the taxpayer's failure to respond to the CP 2000, the Service would still need to produce evidence to refute a taxpayer's claim that the source of the cash was tax free when the taxpayer files a petition in Tax Court. The need for this additional evidence exists without regard to the allocation of the burden of proof. The Tax Court's restrictions on discovery will make additional investigation to develop the record more difficult. With 1099s and W-2s, the payor is available to help establish that the taxpayer received income; with a Form 8300, the preparer of the information return can only testify as to the receipt of cash from the taxpayer, not as to how the taxpayer in turn acquired the cash. Thus, the development required is more extensive than with most other information returns.

Given that larger than average sums of money are involved,

and that, in some cases, criminal activity may be uncovered, we think the wisest course in all cases involving a Form 8300 mismatch would be to refer the form to a district office examination function for further investigation prior to the issuance of any statutory notice. A more complete examination will also allow the Service to consider whether a criminal referral is appropriate.

In addition to the preceding practical problems in defending a notice based almost entirely on a Form 8300, we share your concern that issuing such notices of deficiency is not sound policy. Over the last several years, Congress has shown that it is concerned that the Service fully develop cases before issuing notices of deficiency. Using a summary method to determine unreported income from a Form 8300 without further investigation is similar to Service procedures that led Congress to enact section 6201(d) requiring, under certain circumstances, the Service to produce additional supporting information when a taxpayer contests an adjustment based on an information return. In our view, the Form 8300 information is an invaluable tool that may lead to fruitful targets for examination. It is not a substitute for that examination. Once the field office conducts an examination, the Service should be on firm ground to defend any statutory notice resulting from the investigation.

/s/

DEBORAH A. BUTLER