A Guide to Understanding Proposed Treasury/IRS Reporting Requirements for Qualifying Digital Asset Brokers

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Introduction to Proposed IRS/Treasury Digital Asset Broker Regulations

A. Background on Digital Assets

A digital asset is a representation of value that uses cryptography for transaction verification and record maintenance through a distributed ledger, as opposed to a centralized authority. In recent years, digital assets have gained popularity due to their potential for low transaction fees, decentralization, and the privacy granted by the distributed ledger technology (DLT) which does not reveal the identities of the parties involved in a transaction. Blockchain, a form of DLT, is a digital ledger where transactions are recorded in "blocks" and added to a "chain" representing the entire transaction history. Each transaction on the blockchain is associated with unique codes called "public keys" that identify the digital asset addresses involved, preserving a degree of confidentiality for digital asset owners.

According to the IRS and Treasury's proposed regulation report, the anonymity associated with digital assets poses challenges for tax compliance, as the distributed ledger technology only identifies digital asset owners by their public keys, making compliance largely reliant on self-reported information.

B. The Necessity for Proposed Regulations

The IRS and Treasury maintain that information reporting is crucial for the integrity of the tax system. According to the IRS's 2019 tax gap analysis, net misreporting as a percentage of income stands at 55 percent for income categories with little to no third-party information reporting. In contrast, misreporting for income with substantial information reporting, such as dividend and interest income, is only 5 percent.

Before the introduction of these proposed regulations, many transactions involving digital assets were outside the scope of information reporting rules. Despite being treated as property for Federal income tax purposes, digital assets were not specified in the existing regulations under section 6045 of the Internal Revenue Code (Code), which requires brokers to file information returns for customers that sell certain types of property. Similarly, section 6050W of the Code, which mandates information reporting by payment settlement entities, does not clarify whether certain exchanges involving digital assets are reportable payments.

C. Overview of Proposed Regulations

The proposed regulations aim to include digital assets in the list of properties for which brokers must file information returns under section 6045. Essentially, brokers would be required to report sales of digital assets in exchange for cash, stored-value cards, other digital assets, services, or other properties subject to reporting under section 6045. Additionally, real estate transactions involving digital assets would also require information returns. These regulations also provide tax rules for determining a taxpayer's amount realized on the disposition of digital assets and basis in purchased digital assets, addressing exchanges of digital assets for services or other properties, and providing rules for allocating transaction costs when one digital asset is exchanged for another.

This guide is intended to provide readers with an examination of the IRS/Treasury's proposed digital asset broker regulations including the impact these proposed rules may have on the U.S. cryptocurrency sector. The full text of these proposed rules can be found at https://public-inspection.federalregister.gov/2023-17565.pdf?1692967516. Readers should be sure to consult the IRS/Treasury's final approved form of these proposed regulations for guidance on how these rules will impact qualifying digital asset brokers.

Background: Proposed Reporting Requirements

Just prior to Congress passing the 2021 Infrastructure and Jobs Act, a report was prepared by the Joint Committee on Taxation that provided Congress with a technical explanation of the proposed Digital Asset Reporting Act provisions. The JCT report noted that the proposed Act provision revises section 26 C.F.R. § 6045(c)(1) to explicitly include any individual who, for a fee, regularly provides services that facilitate the transfers of digital assets on behalf of another person, within the definition of a broker. The JCT noted that this amendment clarifies existing law to eliminate ambiguity regarding the classification of certain market participants as brokers. It's noteworthy that this amendment does not intend to restrict the Secretary's authority to interpret the broker definition. Moreover, the provision elaborated that the term 'specified security' would encompass a digital asset, defined as any digital representation of value recorded on a cryptographically secured distributed ledger or any similar technology as specified by the Secretary unless otherwise provided.

Furthermore, the JCT report noted that proposed section 6045A(a) omits the phrase "a security which is," clarifying that broker-to-broker reporting is applicable to all transfers of covered securities as defined in section 6045(g)(3), including digital assets. It also introduces a new section, 6045A(d), which primarily pertains to transfers by a broker to a non-broker entity. According to section 6045A(d), brokers are mandated to file a return with the IRS for a calendar year concerning any transfer, not part of a sale or exchange executed by the broker, of a digital asset as a covered security from an account managed by the broker to an account or address not associated with an individual the broker knows or has reason to believe is also a broker. The return, whose format is to be determined by the Secretary, will display the information typically required for transfers under section 6045A(a).

Additionally, solely for section 6050I, the proposed legislative provision would broaden the definition of cash to encompass any digital asset as described under the amended section 6045(g)(3). The report noted, however, that it was not implied that digital assets are regarded as cash for any other purposes. Lastly, nothing in the provision of the amendments carried out by the provision intends to suggest, for any period preceding the effective date of the amendments, whether any individual is a broker under section 6045(c)(1) or if any digital asset is property categorized as a specified security under section 6045(g)(3)(B).

On November 15, 2021, President Joe Biden signed the 2021 Infrastructure and Jobs Act into law. According to the Jobs Act, digital asset transfers over $10,000 will be subject to KYC ("know your customer") and IRS reporting requirements. The Jobs Act essentially amended the "cash reporting" requirements of 26 U.S.C. § 6050I to encompass transactions in "digital assets." This provision of the Act is intended to address anti-money laundering ("AML") gaps in the realm of convertible

virtual currencies (CVCs) and digital assets. Under U.S. federal law, the Financial Crimes Enforcement Network (FinCEN), is tasked with preventing and combating money laundering by enforcing anti-money laundering regulations and laws. FinCEN administers the nation's primary anti-money laundering law, the Bank Secrecy Act (BSA).

The BSA requires financial institutions to assist U.S. government agencies in detecting and preventing money laundering. FinCEN also mandates financial institutions to file Suspicious Activity Reports (SARs) for any suspicious transactions that may signify money laundering, tax evasion, or other financial crimes. The BSA also requires banks to file Currency Transaction Reports (CTRs) for cash transactions exceeding $10,000 in one business day. FinCEN shares the information it collects with law enforcement agencies to investigate and prosecute money laundering and other related financial crimes.

FinCEN also enforces the requirement that financial institutions establish an AML compliance program. These programs should include a system of internal controls to assure ongoing compliance, independent testing of BSA compliance, specifically designated individuals responsible for managing BSA compliance, and training for appropriate personnel. FinCEN has also started regulating virtual currencies to prevent their misuse in money laundering. Under the Jobs Act, the U.S. Treasury must pass a set of rules for how FinCEN will handle the filing of KYC and records for transactions involving certain digital assets.

But as the deadline loomed for implementation of this provision of the Jobs Act, there was still no clarity on how the United States Treasury and IRS would enforce the digital asset provisions relating to brokers. In December 2022, Senator Patrick McHenry wrote a letter to Treasury Secretary Janet Yellen requesting that the United States Department of Treasury "prioritize rulemaking for Section 80603 of the Infrastructure Investment and Jobs Act (IIJA) and delay any related compliance requirements." The concern was that if no changes or amendments are made to Section 80603 by December 31, 2023, then effective January 1, 2024, digital asset brokers will need to come into compliance with the IRS return requirements as well as implement and comply with KYC and AML standards under FinCEN's.

On August 29, 2023, the U.S. Department of the Treasury and the Internal Revenue Service (IRS) unveiled proposed regulations on the sale and exchange of digital assets by brokers. This move is a component of the Biden-Harris Administration's rollout of the Infrastructure Investment and Jobs Act (IIJA) and aims to mitigate tax evasion through digital assets and narrow the tax gap.

Key Points in the Treasury/IRS Proposed Regulations:

The proposed Treasury/IRS regulations are intended to establish a fair tax playground for all, ensuring that everyone follows the same set of rules.

1. Reporting: Brokers dealing in digital assets will be obligated to report certain sales and exchanges, equating them with brokers for securities and other financial tools in terms of information reporting requirements.

2. Ease for Taxpayers:

- Current law mandates taxpayers to pay taxes on digital assets' gains and allows deductions on losses. However, calculating these gains and losses is arduous for many.

- The proposed regulations intend to simplify this process by introducing Form 1099-DA, which will provide the necessary information to determine taxes owed.

- The introduction of this form intends to negate the need for taxpayers to resort to complicated calculations or spend money on digital asset tax preparation services. It ensures that tax reporting on digital assets is in line with other types of assets.

3. Implementation Timeline: The first year for which brokers will have to report on the sale and exchange of digital assets is set for 2026, concerning sales and exchanges in 2025.

4. Projected Impact: The nonpartisan Joint Committee on Taxation estimates that the IIJA provisions will yield close to $28 billion over a decade. The committee emphasizes the importance of third-party income verification in ensuring accurate tax reporting.

5. Public Participation:

- The proposed regulations are open for public comments until October 30, 2023.

- Public hearings are scheduled for November 7 and possibly November 8, 2023, depending on the volume of responses.

6. Legal Specifics from the Infrastructure Investment and Jobs Act:

- Definition of Broker: It now includes anyone offering services that facilitate the transfer of digital assets.

- Specified Securities: The definition has been expanded to comprise digital assets, especially if acquired after January 1, 2023.

- Definition of Digital Asset: It refers to any digital value representation stored on a secured distributed ledger or similar technology.

- Transfer Statement Reporting: This applies to covered securities that are digital assets, primarily if the transfer is not a sale or if the broker is not aware that the receiving account is also managed by a broker.

- Effective Date: The stipulated amendments are applicable to returns filed and statements provided after December 31, 2023.

- Rule of Construction: The statutory amendments should not be interpreted to infer any definition or classification before the effective amendment date.

So who is subject to the digital asset broker reporting requirements?

The IRS/Treasury's proposed regulations extend the information reporting rules under 26 C.F.R. § 1.6045-1 to brokers who, in the ordinary course of a trade or business, act as:

(1) agents,

(2) principals, or

(3) digital asset middlemen

for others to affect sales or exchanges of digital assets for:

(1) cash,

(2) broker services, or

(3) property of a type that is subject to reporting by the brokers (including different digital assets, securities, and real estate) under section 6045 of the Internal Revenue Code (Code) or

(4) effect on behalf of customers payments of digital assets associated with payment card and third-party network transactions subject to reporting under section 6050W of the Code.

26 C.F.R. § 1.6045-1 currently defines a "broker" as follows:

> (1) The term broker means any person (other than a person who is required to report a transaction under section 6043), U.S. or foreign, that, in the ordinary course of a trade or business during the calendar year, stands ready to effect sales to be made by others. A broker includes an obligor that regularly issues and retires its own debt obligations or a corporation that regularly redeems its own stock. However, with respect to a sale (including a redemption or retirement) effected at an office outside the United States, a broker includes only a person described as a U.S. payor or U.S. middleman in § 1.6049-5(c)(5). In addition, a broker does not include an international organization described in § 1.6049-4(c)(1)(ii)(G) that redeems or retires an obligation of which it is the issuer.

26 C.F.R. § 1.6045-1 (2023).

These IRS proposed regulations would also clarify that the definition of broker for purposes of section 6045 includes:

(1) Digital asset trading platforms: A person who operates a trading platform or website that allows users to exchange digital assets in return for different digital assets or cash (meaning the U.S. dollar or foreign currency) is referred to in this preamble as a digital asset trading platform.

(2) digital asset payment processors,

(3) Certain digital asset hosted wallet providers, and

(4) persons who regularly offer to redeem digital assets that were created or issued by that person.

In addition, these proposed regulations would require real estate reporting persons to report on real estate purchasers who use digital assets to acquire real estate in a reportable real estate transaction and extend the information that must be reported under §1.6045-4 with respect to sellers of real estate to include the fair market value of digital assets received by sellers in exchange for real estate.

Virtual currency: defined for Federal income tax purposes as a digital representation of value that functions as a medium of exchange, a unit of account, or a store of value other than the U.S. dollar or a foreign currency (fiat currency). See https://www.irs.gov/pub/irs-irbs/irb14-16.pdf.

In these proposed rules, when digital assets are traded for goods (excluding other digital assets or services), the goods part is reported under section 6050W, while the digital assets part is reported under proposed §1.6045-1, not under section 6050W.

What are existing information reporting rules for virtual currency or other digital assets?

Notice 2014-21: Notice 2014-21 explains how the current reporting rules apply when virtual currency is used for paying wages, making miscellaneous payments, and handling third-party network transactions, requiring the filing of specific forms like W-2, 1099-MISC, and 1099-K respectively. See https://www.irs.gov/pub/irs-drop/n-14-21.pdf However, this notice only covers reporting for virtual currency payments received, not for income from selling virtual currency or other digital assets. Although there are some existing rules in the Code that might apply to selling virtual currency, these rules aren't clear or comprehensive enough for consistent reporting of such transactions.

26 U.S.C. § 1001: Outlines how to calculate the gain or loss when selling or exchanging something. It says that the gain is what you get from the sale minus your original cost, and the loss is how much your original cost exceeds what you get from the sale. Section 1.1001-1(a) explains that the money you make or lose from turning property into cash or exchanging it for different property is counted as income or loss. However, these rules don't specifically talk about digital assets.

26 U.S.C. § 1012: Explains that the original cost of an item is its basis for calculating gains or losses. Although there are special rules for calculating the basis for certain items, these rules don't clearly cover digital assets.

26 U.S.C. § 6041: States that if someone in their business dealings pays $600 or more, they need to file certain forms and give the payee a statement showing the amount and details of the payment. However, if the payment is for a capital asset and the payer can't determine the payee's cost basis in the asset, this rule doesn't apply. For example, if a payment is made for digital assets, and the payer can figure out the payee's cost basis, and the gain is $600 or more, it needs to be reported

under this section. However, this reporting doesn't apply to brokers paying customers. If a payment falls under this section and another section (6050W), it should be reported under section 6050W instead.

26 U.S.C. § 6045: Requires brokers to file certain forms and provide statements to customers they've sold specific assets for, like stocks or options, showing details like the customer's name, address, and the amount made from the sale. The 2021 Infrastructure Investment and Jobs Act, updates Section 6045 to clarify how brokers should report digital asset transactions and expands the rule to include all digital assets.

26 U.S.C. § 6045(c)(1): Under § 6045(c)(1), a broker includes dealers, barter exchanges, and anyone who regularly acts as a middleman for property or services, for a fee. The existing regulations under section 6045 further explain what a broker is, stating anyone, whether in the U.S. or abroad, who in their regular business helps make sales for others. This term covers not just traditional brokers, but also some securities custodians, escrow agents, stock transfer agents, and others who might not usually be considered brokers. For instance, a company that often issues and then retires its own debt, or a mutual fund that frequently buys back its own stock, are also treated as brokers under these rules.

26 U.S.C. § 1.6045-1(a)(5): The term 'commodity' is defined as any kind of personal property approved for trading by the Commodities Futures Trading Commission (CFTC) according to certain regulations. Initially, CFTC approval was needed to list new regulated futures contracts on a commodities exchange. However, with the Commodity Futures Modernization Act, the process changed, allowing new contracts to be listed if the market self-certifies that they comply with relevant laws and CFTC's rules. The regulations don't clearly say whether digital assets, allowed for trading through CFTC's self-certification, are considered commodities for reporting purposes.

26 U.S.C. 6045(g): Brokers, when filing a return on the sale of a covered security, are required by section 6045(g) to include the security's adjusted basis and whether the gain or loss is long-term or short-term. Covered securities, apart from stocks, are defined as specified securities acquired on or after January 1, 2013, or a later date set by the Secretary. Stocks are considered covered securities if acquired on or after January 1, 2011, or January 1, 2012, based on certain conditions under section 1012. Section 6045(g)(3)(B) lists what qualifies as specified securities, like shares of corporate stock, bonds, certain commodities contracts, and other financial instruments deemed appropriate by the Secretary for adjusted basis reporting. However, the existing rules under section 6045 don't specifically list digital assets as a specified security.

26 U.S.C. § 6045A: The current version of § 6045A mandates that when certain individuals transfer covered securities to a broker, they must provide a written statement with specific information as required by the Secretary. This statement should include the names of the person transferring and the receiving broker, the customer's name and account number, and details about the security such as the transfer date, adjusted basis, and original acquisition date. Before the Infrastructure Act amendments, section 6045A didn't specify whether these requirements applied to digital asset transfers.

26 U.S.C. § 6045B: Mandates that some securities issuers report to the IRS and shareholders about how certain corporate actions like stock splits or mergers affect the basis of issued securities. However, these rules don't clearly state the reporting requirements concerning digital assets.

26 U.S.C. § 1.6045-1(a)(4): Under existing regulations, a barter exchange is defined as an organization where members or clients make agreements to trade or barter goods or services with each other or with the organization. Barter exchanges are required to file information returns and provide statements to payees regarding the trading of goods or services by its members or clients. A trade is considered to have occurred through a barter exchange if it's facilitated by credits on the exchange's books, scrip issued by the exchange, or if the exchange arranges a direct trade between members.

26 U.S.C. § 6045(e): Mandates that individuals involved in certain real estate transactions file information returns and provide payee statements, which include details like the seller's name, address, and the total money paid to the seller, along with other information as needed by the Secretary. The person responsible for closing the transaction, or in the absence, of others like the mortgage lender or brokers, are defined as real estate reporting persons and are considered brokers for reporting purposes under this section. An exception exists for those relying on seller certifications proving the sale involves the seller's main home, and the gain from the sale is excludable from gross income under section 121 of the Code, up to certain limits. The rules only require reporting cash payments received or to be received by the seller, so payments made using digital assets are not required to be reported unless the digital asset is considered cash under these rules.

The existing rules generally exclude a person defined as a non-U.S. payor or non-U.S. middleman from the definition of a broker when a sale is made on behalf of a customer at an office outside the U.S. Also, brokers, whether based in the U.S. or not, are not required to file an information return under section 6045 for sales for customers who can be considered exempt foreign persons, with the exemption based on certain documentation and whether the sale was made at a broker's office inside or outside the U.S. Essentially, these rules mean that non-U.S. securities brokers, except for certain ones with U.S. activities, don't have to report customer information to the IRS, and neither U.S. nor non-U.S. brokers need to report on non-U.S. customers under section 6045.

26 U.S.C. § 6050W: Mandates that payment settlement entities file information returns and provide payee statements for each payee they've made payments to, regarding certain transactions. These entities include merchant acquiring entities, like banks or organizations contractually bound to pay participating payees for payment card transactions, and third-party settlement organizations (TPSOs). TPSOs are central organizations required to make payments to participating payees for transactions of goods or services sold through a third-party payment network.

Third-Party Settlement Organizations: TPSOs are required to report payments for third-party network transactions only if they surpass a certain minimum amount. The American Rescue Plan Act of 2021 changed this amount for years starting after December 31, 2021. Previously, reporting was necessary only if a payee had over 200 transactions and the total amount exceeded $20,000 in a year. Now, TPSOs must report transactions if the total payments to any payee go beyond $600,

regardless of the number of transactions. However, section 6050W does not mention if exchanges of digital assets through TPSOs should be reported under this section or under section 6045.

How does the 2021 Infrastructure Investment and Jobs Act modify the above IRS provisions?

The Infrastructure Investment and Jobs Act updates rules on how brokers should report digital asset transactions, aiming to enhance IRS and taxpayer access to information on gross proceeds and adjusted basis when selling digital assets through brokers. Key points include:

1. It expands the broker definition to include anyone regularly facilitating digital asset transfers for others, for a fee.

2. It updates the definition of specified securities to include digital assets, treating them as covered securities for basis reporting if acquired on or after January 1, 2023.

3. It broadly defines a digital asset as any digital value representation recorded on a secured, cryptographic ledger or similar technology, as specified by the Secretary.

4. It confirms that transfer statement reporting applies to digital assets as covered securities, and introduces a new reporting provision for brokers on transfers of digital assets, provided they are not sales and not to another known broker account.

5. These amendments apply to returns and statements after December 31, 2023.

6. It states that these amendments do no imply any interpretations for periods before the effective date regarding who is considered a broker or whether any digital asset is deemed a specified security.

Reasons for New Information Reporting Rules for Digital Assets:

The growing popularity of digital assets as a means of payment and investment necessitates new information reporting rules to ensure tax compliance. The current allure of digital assets stems from potential benefits like lower transaction costs and faster speeds. However, the pseudonymity of transactions, due to the lack of identity recording on distributed ledgers, poses a significant risk to tax administration.

Digital assets are now common in ordinary transactions which, if done using traditional currency, would be subject to information reporting. For instance, some payment processors and credit card issuers now facilitate digital asset payments. Taxpayers can directly buy, sell, or invest in digital assets, trade derivatives on them, or even own tokenized stock and security interests that trade on digital asset platforms. These transactions can occur on U.S. or foreign platforms and financial intermediaries.

The lack of third-party information reporting to the IRS has been identified as a contributor to the tax gap, which is the difference between taxes owed and paid. Accurate third-party reporting leads to higher taxpayer compliance as it makes income transparent to both the IRS and taxpayers.

Specific reporting on digital asset transactions would help the IRS identify hard-to-discover transactions, aiding in closing the information gap concerning digital assets.

The benefits of expanding information reporting for digital assets extend to taxpayers as well. It helps taxpayers accurately track and report gains or losses from digital asset dispositions, something that some digital asset platforms and tax service providers are trying to address voluntarily. This reporting also allows the IRS to focus audit efforts on taxpayers more likely to have underreported digital asset transaction income.

To improve tax compliance, it's proposed that brokers, including digital asset trading platforms and payment processors, should be required to file information returns and provide payee statements concerning digital asset dispositions. For instance, a platform facilitating a digital asset sale should report the gross proceeds realized by the customer from that sale. Likewise, payment processors aiding digital asset payments should report on these transactions.

Lastly, substantive rules are needed to help taxpayers file accurate information returns concerning digital asset dispositions, including rules for determining gain or loss in a digital asset sale or exchange transaction and for calculating the basis of digital assets. This comprehensive approach to reporting and regulation would help address the challenges posed by the evolving digital asset landscape in terms of tax compliance.

Explanation of Provisions

The Treasury Department and the IRS plan to implement new reporting rules for digital assets handled by brokers in several stages. Initially, the focus is on modifying current regulations to mandate brokers to report digital asset sales. Future stages will aim at incorporating reporting for specific types of security transfers that aren't sales or transfers to known brokers.

1. The first phase aims to amend existing rules to ensure brokers report sales of digital assets.

2. Subsequent phases will address reporting for certain security transfers, with details on these phases coming later.

The proposed changes generally align with the existing framework but have been tailored to accommodate the unique nature of digital assets, as highlighted by the Infrastructure Act. However, not all transactions involving digital assets are covered in these proposals; for instance, income from digital assets received in hard forks will be addressed under different tax code provisions.

Proposed §1.6045-1: The proposed regulations in section § 1.6045-1 largely adhere to existing broker reporting rules, but have been adjusted to account for the unique characteristics of digital assets and the amendments introduced by the Infrastructure Act to section 6045. As stated above, they don't cover all digital asset transactions that could generate income, like receiving digital assets in hard forks, as such transactions are better handled under other sections of the tax code.

Expansion of the types of property subject to reporting: Currently, under section § 1.6045-1(a)(9), brokers must file a report for each sale made on a customer's behalf, but only if the sold item is a

specific type of asset like a security or commodity, and the sale is for cash. The new proposals extend this reporting requirement to certain sales of digital assets, not just for cash, but also when exchanged for other digital assets, stored-value cards, broker services, or other properties already covered under existing reporting rules in section 6045.

Definition of Digital Assets: Proposed regulation § 1.6045-1(a)(19)(i) defines digital assets similarly to the Infrastructure Act's definition, referring to them as value representations recorded on a secured digital ledger. This definition doesn't include digital cash like funds in online bank accounts. It's broad to cover digital asset transactions whether or not they are individually recorded on a secured ledger. For instance, brokers might hold digital assets and execute internal transactions before updating the distributed ledger, or record transactions on non-public ledgers.

The definition also encompasses newer digital assets like stablecoins and Non-Fungible Tokens (NFTs), as they also can result in taxable gains or losses when traded. This broad approach aims to ensure clarity as digital assets evolve. However, the definition excludes virtual assets restricted to closed systems like in-game tokens, and applications of digital ledger technology that don't create new transferable assets, like inventory tracking. The regulation aims to focus on assets whose sales could be reportable, asking for feedback on whether the proposed definition aptly identifies the assets it should cover.

Coordination with Reporting Rules for Securities, Commodities, and Real Estate: The Treasury Department and IRS recognize that digital assets might be seen as securities or commodities under certain laws. They aim to clarify the reporting requirements for brokers in this aspect through these proposed regulations, but they don't provide a complete answer to the classification of digital assets.

The existing rules under section 6045 require reporting on sales of securities, some commodities, and real estate transactions. To avoid confusion or double reporting, coordination rules have been introduced. These specify that the classification of an asset for reporting purposes under these proposed regulations doesn't apply to any other legal determination regarding its nature.

Despite the overlapping characteristics of digital assets with securities and commodities, these regulations suggest that digital assets should be reported under their own category to ensure clarity. This stance also considers the fact that digital asset transactions may pose different tax compliance concerns compared to traditional asset transactions, due to their transfer methods and the platforms used for trading.

Moreover, the proposal acknowledges that there might be temporary digital representations of securities during transactions, created using blockchain or similar technologies. While these might technically fall under the digital asset definition, they may not be the primary focus of these regulations. Feedback is requested to understand if an exception is needed for such transactions.

Furthermore, the proposal mentions a delay in certain reporting requirements for assets that fall under both specified securities and digital assets, to allow time for more comprehensive rules to be developed.

According to IRS and Treasury, these proposed regulations aim to define a clear reporting pathway for digital assets, while remaining open to feedback for refining the definitions and rules, ensuring they align with the evolving nature of digital assets and the technology behind them.

Definition of Commodities: The initial definition of a commodity was established in 1983, covering personal property or interests approved for futures trading by the CFTC (Commodity Futures Trading Commission). Later, the CFTC introduced a self-certification mechanism for new contracts, which brought some digital assets under its jurisdiction. However, some digital asset platforms argue that these assets are not commodities as the CFTC didn't officially approve them. To align with the CFTC's current practice, the Treasury Department and IRS propose updating the rule to include assets under the CFTC's self-certification as commodities for reporting purposes under section 6045.

This change, effective from January 1, 2025, applies to all commodities under CFTC's jurisdiction, covering sales of such assets regardless of when they were self-certified. This updated definition doesn't affect the reporting obligations on regulated futures contracts.

Now, a digital asset approved for regulated futures trading or self-certified by the CFTC will be treated as a commodity for reporting purposes, in addition to being a digital asset. This dual classification could cause confusion on whether to report sales as commodities or digital assets, potentially leading to double reporting. To avoid this, a coordination rule is proposed: a broker must report the sale of an asset qualifying as both a commodity and a digital asset only as a sale of a digital asset.

Lastly, recognizing that digital technology may represent real estate in transactions, a coordination rule is suggested to avoid double reporting. If a digital asset also represents reportable real estate, the sale should only be reported as a sale of reportable real estate, ensuring clarity and consistency in reporting standards.

Definition of brokers required to report: Before the Infrastructure Act, a broker was defined as a dealer, barter exchange, or any middleman involved in transactions of goods or services. Post the Act, this definition extends to individuals or entities facilitating digital asset transfers for others, in light of evolving digital markets. Now, anyone involved in digital asset sales as part of their regular business, and has knowledge about the parties and transactions, will be classified as a broker. This aims to ensure tax compliance.

The Act also brings certain digital asset platforms under scrutiny, which despite their decentralized nature, have operators with enough control to access transaction information. Even those platforms that operate through smart contracts, connecting buyers and sellers directly, are under this purview if they have a level of control or influence over transactions. The idea is to have these platforms, depending on their control level, report sales information for tax purposes.

Additionally, the Act seeks to address scenarios where platforms might try to dodge these reporting obligations or where individuals may seek non-reporting platforms to evade taxes. According to the IRS and Treasury, the updated definition is meant to ensure that the tax laws are adhered to, regardless of how a business operates.

Moreover, the Act proposes that facilitative services, which aid in executing digital asset sales, fall under the broker category, ensuring broader coverage. However, those engaged only in validating transactions on the blockchain or selling hardware/software for accessing digital assets, without other services, are exempt from this definition.

The new proposed rules clarify that anyone acting as a middleman in digital asset transactions as part of their regular business is considered a broker, aimed at ensuring tax compliance. This includes a wide range of digital asset platforms and services, with certain exemptions to avoid undue burdens. The aim is to obtain necessary information for tax reporting while inviting feedback on potential privacy or technical challenges these changes might pose.

The new definition of "brokers" as outlined in the Infrastructure Act emphasizes their role in digital asset transactions. Initially, brokers were conceived as intermediaries in property or service transactions. However, the new guidelines extend this definition to include those facilitating digital asset transfers. This expansion aims to encompass digital trading platforms and requires such brokers to gather and report sale information for tax compliance. The definition also encapsulates those offering certain facilitative services, while excluding solely hardware sellers and ledger validators from it. Furthermore, the text mentions a "for consideration" clause, stressing a broker's engagement in a trade or business for gain or profit. Examples illustrating who falls or doesn't fall under the broker definition are provided in the proposed regulations for better clarity.

The proposed IRS/Treasury regulations delve into the updated broker definition as per the Infrastructure Act, extending it to cover individuals or entities facilitating digital asset transfers. Initially, a broker was perceived as a middleman in property or service transactions, as per section 6045(c)(1). The new framework under section 80603(a) of the Infrastructure Act now includes those effectuating digital asset transfers on others' behalf. This amendment aims to clarify the broker status of various market participants, not limiting the Secretary's interpretative authority over the term "broker."

The revised broker definition is reflected in proposed §1.6045-1(a)(1), maintaining the original broker notion but expanding the term "effect" under §1.6045-1(a)(10)(i) and (ii) to include any person offering facilitative services that help execute digital asset sales by customers. This alteration considers whether a person is "in a position to know" customer identities and transaction details, essential for tax compliance. The amendment expects to bring some decentralized exchanges under this definition, requiring them to collect and report sales information if they qualify as brokers.

The proposed regulation also addresses potential privacy concerns associated with personal identity information collection, requesting public comments on alternative approaches to meet tax compliance objectives while mitigating privacy issues. Furthermore, it explores technical challenges that might affect a non-custodial digital asset trading platform's ability to gather and transmit necessary information under these proposed regulations.

The term "person" in these proposed regulations is generally defined per section 7701(a)(1) to include individuals, legal entities, or unincorporated groups engaged in business, financial operations, or ventures like partnerships. See 26 U.S.C. § 7701. This definition covers groups

providing facilitative services, knowledgeable about customer identities and transaction natures, and treats them as brokers for tax purposes.

The document further delves into scenarios where platform operators might maintain control or influence over facilitative services, discussing governance tokens and administration keys in decentralized exchanges. It examines how these elements might affect an operator's control over a platform and its facilitative services, inviting comments on circumstances under which an operator retains sufficient control or influence over a digital asset trading platform's facilitative services.

The "for a consideration" clause in the broker definition emphasizes a broker's regular engagement in a trade or business for gain or profit. The document also provides examples of who would typically be considered brokers under this new definition, including digital asset trading platforms, digital asset payment processors, and digital asset kiosk operators, among others. It clarifies that certain individuals or entities, like merchants selling goods or services for digital assets or those solely engaged in validating distributed ledger transactions, are excluded from the broker definition.

In summary, this section elaborates on the expanded broker definition, encompassing those facilitating digital asset transfers, and outlines the implications of this broadened definition on tax compliance and digital asset trading platforms.

Digital Asset Broker: In the proposed section § 1.6045-1(a)(1), a broker is defined as someone ready to facilitate sales for others as part of their regular business activities. When it comes to digital assets, this definition, termed a "Digital Asset Broker", extends to both physical businesses like digital asset kiosks and online platforms managing digital asset trades. For online platforms, this includes those that hold their customers' digital assets and those with enough control over platforms that don't hold assets but facilitate sales using automated contracts or software.

IRS/Treasury maintains that these online platform operators, especially those of non-custodial trading platforms, can access or request customer identity and sales information due to their control over transaction protocols. The term "person" in this context includes individuals, legal entities, or groups conducting business, meaning an operator of a digital asset trading platform can be considered a broker, regardless of its organizational structure, including decentralized organizations (DAOs).

Merchants accepting digital assets for goods or services are not considered brokers under these guidelines. The broker designation applies only when facilitating digital asset sales for customers. For instance, if a merchant's digital asset transactions are managed through a digital asset payment processor, that processor might be categorized as a broker.

Under current law, a broker is someone who, in their regular business activities, facilitates sales and usually knows the total amount made from the sale. This includes some agents who handle securities like stocks. The law has a special rule for cases where multiple brokers are involved, saying only the broker closest to the customer needs to report the sale details.

In the digital asset world, there are providers known as digital asset-hosted wallet providers. They safeguard the digital keys of assets for others, similar to how a bank safeguards your money. Some

of these providers go beyond just safeguarding; they also facilitate sales of digital assets or have information about the sales, much like a traditional securities custodian.

The proposed legal definition of a broker is expanded to include these digital asset-hosted wallet providers, but only if they also play a part in the sale of digital assets, acting either as the main party in the sale, an agent who knows the sale amount or as a middleman with knowledge of who made the sale and the total sale amount. However, if a hosted wallet provider only stores and transfers digital assets without any knowledge of the sale details, they won't be considered a broker.

Digital Asset Payment Processors: These are services that help facilitate transactions using digital assets like cryptocurrencies. Digital Asset Payment Processors are increasingly becoming a conduit for transactions using digital assets. Many of these processors allow customers to pay with digital assets, a trend reflecting the growing acceptance of cryptocurrencies. Typically, a scenario plays out where a customer pays with digital assets, and the payment processor then exchanges these digital assets for U.S. dollars to settle with the merchant or another involved entity. There are also instances where the digital assets are directly transferred to the merchant, bypassing any currency conversion. In both scenarios, the overarching reality is that the customer has traded their digital assets, a move that could manifest in a financial gain or loss for them.

On the regulatory front, there is a wave of proposed regulations aiming to bring more transparency to these transactions. IRS/Treasury proposed regulations aim towards having these processors provide detailed information on such transactions. This reporting ambit extends to the exchange of goods for digital assets and the financial gain or loss resulting from such transactions. The clarity in transaction trails is seen as a step towards a more regulated digital asset environment.

Digging into the specifics, a Digital Asset Payment Processor is defined as a service that stands in the gap to facilitate digital sales. They receive digital assets from one party, which they then exchange for other assets or cash to settle with another party, such as a merchant. A notable feature in their operation is the provision of a temporary fixed exchange rate for transactions. This feature is more than a convenience; it aids in determining the fair market value received by the customer, a critical aspect of financial and tax accounting.

With these proposed reporting requirements comes the necessity for customer information. For the sake of reporting, payment processors are mandated to collect personal information from the customer making the payment in digital assets. IRS/Treasury maintains that this level of reporting is not just for regulatory compliance, but is also a tool that helps customers determine the financial gains or losses from their transactions.

Broadening the scope, the definition of digital asset payment processors also envelops certain payment settlement entities and payment card issuers engaging in digital asset transactions. In this scenario, the customer is identified as the individual transferring the digital assets for payment, a definition that holds regardless of the contractual arrangements in place.

However, these proposed regulations also raise concerns surrounding the privacy of personal customer information associated with these digital asset transactions. IRS/Treasury has therefore

opened up a comment period seeking feedback on alternative approaches that can strike a balance between meeting tax compliance objectives and addressing privacy concerns.

Lastly, the proposed regulations don't provide a minimum threshold for reporting. The absence of a small transaction exemption is grounded on the understanding that small transactions can accumulate to significant amounts over time. Although these proposed reporting requirements are seen as cumbersome by critics, the IRS/Treasury maintains they are also intended to assist customers in determining their financial position accurately, fostering a culture of financial responsibility and compliance in the digital asset landscape.

Initial Coin Offerings and Stablecoins: The IRS/Treasury proposed changes to the definition of a broker under section §1.6045-1(a)(1) seeks to cover individuals or entities that frequently offer to buy back digital assets they initially issued, like in the case of initial coin offerings or stablecoin redemptions. A stablecoin is a type of digital asset designed to maintain a steady value by pegging it to another asset, usually a fiat currency. Some stablecoin issuers buy back the coins from certain or all customers and are aware of the total amount paid to these customers. According to IRS/Treasury, they are included in the broker definition as, despite the name "stablecoin," their value can fluctuate, potentially leading to financial gain or loss.

This proposed rule is aimed at those who offer to buy back digital assets rather than those who frequently do so, to ensure that even occasional redemptions by digital asset issuers are reported. The Treasury Department and the IRS are seeking feedback on how often digital asset creators or issuers buy back these assets. They are also interested in comments on whether the broker reporting rules should extend to initial coin offerings, simple agreements for future tokens, and similar contractual arrangements.

Digital Asset and Real Estate Transactions: The proposed rule § 1.6045-1(a)(1) has been amended to state that in a real estate transaction if digital assets are used as payment, the real estate reporting person is considered a broker. They are required to file an information return for the transaction as per proposed rule §1.6045-4(a), ignoring certain reporting exemptions under section 6045(e)(5) or proposed or existing rules §1.6045-4(c) or (d), like the exemptions for some principal residence sales or exempt real estate sellers. For instance, if a buyer uses digital assets to buy real estate, the reporting person must report this exchange of digital assets, even if they aren't required to report on the seller's side of the transaction, say if the seller is a corporation and thus an exempt seller according to existing rule §1.6045-4(d).

Expansion of the types of sales subject to reporting: The proposed rule § 1.6045-1(a)(9)(ii) expands the definition of a sale subject to reporting, due to the unique nature of digital assets that can be exchanged for various other assets or used as payment methods. It now includes the exchange of digital assets for cash, other digital assets, or stored-value cards (like gift cards). This rule also covers situations where digital assets are used to purchase property or services. For instance, using digital assets to buy stocks or real estate, or to pay for a broker's services, will be considered a sale.

Digital asset payment processors, which facilitate transactions between buyers and sellers, are also covered under this rule. For example, if a customer pays in digital assets to a processor who then

pays a merchant, either in a different digital asset or cash, it's treated as a sale. Similarly, if a customer directly pays a merchant in digital assets at a fixed exchange rate provided by a payment processor, it's treated as a sale. These rules apply even when the payment processor is also a payment card issuer.

Additionally, the proposal includes rules on reporting sales arising from certain contracts involving digital assets. For example, delivering digital assets to settle a forward contract or an option will be treated as a sale. However, some transactions are excluded from the definition of a sale, like receiving new digital assets via a hard fork or airdrop without giving up other assets or receiving digital assets for services like completing a survey.

The proposed rules seek to ensure comprehensive reporting while inviting comments on certain areas, like the frequency of forward contract trading involving digital assets, or whether additional transactions should be covered under these rules. The aim is to gather more information and address any potential reporting gaps in the rapidly evolving digital asset landscape.

Information to be reported for digital asset sales: Much like the information required to be reported for securities on Form 1099-B, brokers will now need to report certain information for each digital asset sale. This information includes the customer's details, the type and amount of digital assets sold, the sale date and time, and the gross proceeds of the sale.

Moreover, brokers are required to report additional details to help the IRS verify the reported gross proceeds and ascertain the basis claimed by taxpayers. This includes the transaction ID, digital asset address(es) used in the sale, and the type of consideration received (cash, other digital assets, property, or services).

If the sale involves a digital asset that's also a security, brokers must provide additional information as required for securities sales. For digital assets held in a broker's hosted wallet that were transferred into that account before the sale, brokers should report the transfer-in transaction details. However, this might change once new rules under section 6045A are established.

The reporting format is set to be standard, with transaction dates and times recorded in Coordinated Universal Time (UTC), though feedback is sought on whether a uniform time standard might be burdensome.

These proposed rules, aiming to improve tax compliance and ease the calculation of gains or losses for taxpayers, are anticipated to be applied to sales and exchanges of digital assets occurring on or after January 1, 2025. The introduction of these reporting systems will require digital asset brokers to invest in developing and implementing the necessary infrastructure, with the ultimate goal of addressing underreporting issues related to digital asset transactions.

The rules for reporting gross proceeds from digital asset transactions largely follow existing procedures for determining gains from sales or other dispositions of digital assets. Here's a simplified explanation of the key points in the provided text:

1. Calculating Gross Proceeds in a Sale:

Gross proceeds from a digital asset sale are calculated as the sum of: (1) The total amount in US dollars received by the customer; or (2) The fair market value of any property or services received; If a debt instrument is issued in exchange for a digital asset, the amount related to the debt instrument is generally its issue price. These amounts are reduced by any digital asset transaction costs.

2. Digital Asset Payment Processor's Role:

If a digital asset payment processor facilitates a sale, the gross proceeds reported include: The amount paid in cash or the fair market value of digital assets paid to the second party. Any transaction costs are reduced by allocable digital asset transaction costs.

3. Determining Fair Market Value in an Exchange:

The fair market value of property or services received in an exchange should be measured at the time the transaction occurred. A reasonable valuation method should be used to determine the fair market value, considering factors like exchange rates, trading volumes, and market capitalization among others. In cases where one digital asset is exchanged for another, brokers can rely on valuations done by digital asset data aggregators using a reasonable method If there's a significant value disparity in the exchange, the focus should be on the fair market value of the received services or property.

4. Calculating Transaction Costs in an Exchange:

Brokers often charge a transaction fee in a digital asset exchange, which might vary based on the type of digital asset involved. Generally, all transaction costs paid by the customer are tied to the disposition of the digital assets. In special cases where different kinds of digital assets are exchanged, half of the transaction cost goes to the sold asset and the other half to the acquired asset. Transaction costs include fees paid to brokers, transfer taxes, and other commissions or costs related to the transaction. These guidelines aim to standardize the reporting of digital asset transactions, making it easier for both brokers and tax authorities to handle digital asset sales and exchanges.

1. Mandatory Broker Reporting:

Brokers, already required to report on covered securities, are also to report the adjusted basis of those securities. The Infrastructure Act expands the definition of covered securities to include digital assets, with new rules for transferring digital assets between accounts for better basis reporting. Sales of digital assets, facilitated by custodial brokers, should include mandatory basis reporting, but sales through decentralized exchanges are not subject to these rules. Financial contracts on digital assets, not held in hosted wallets, have different reporting requirements.

2. Digital Assets and Financial Contracts Acquisition:

Brokers should report the adjusted basis for digital assets and certain financial contracts acquired on or after January 1, 2023. However, this reporting requirement for sales will only take effect on January 1, 2026, giving brokers time to prepare.

3. Voluntary Broker Reporting:

Brokers capable of reporting before the mandatory dates are encouraged to do so, with penalty waivers for incorrect reporting on voluntary disclosures.

4. Determining the Adjusted Basis:

The proposed regulations provide guidelines on calculating the initial basis of digital assets, whether acquired for cash or through exchanges. The initial basis includes the total amount paid plus any related transaction costs. Special rules apply for digital assets acquired in exchange for other property.

How brokers should ascertain the sale order of digital assets when a customer possesses multiple units acquired at different instances or at varying prices?

If a customer decides to sell some units, it's crucial for the broker to identify which specific units are being sold. The customer has the option to clarify which units they intend to sell by informing the broker either before or at the exact time of the sale. However, if the customer doesn't provide this specification, the broker is instructed to consider the units that were bought or transferred earliest as the ones being sold. There's a provision for future adjustments; once certain rules are established, brokers might have the ability to use the actual purchase date of transferred-in digital assets to determine which units are sold first. These regulations aim to create a structured approach to ensure brokers report digital asset sales accurately, which is vital for both tax and record-keeping purposes for the broker and the customer.

Existing reporting exceptions for digital asset brokers as per section §1.6045-1(c) concerning exempt recipients and excepted sales.

In essence, no reporting is mandated for sales conducted for certain entities like select corporations, financial institutions, tax-exempt organizations, or government bodies. While there was consideration towards including registered money services businesses (MSBs) in the exempt list, it was not pursued due to the lack of a public method to ascertain an MSB's compliance with the Bank Secrecy Act.

The existing regulations contain a special rule to prevent duplicate reporting when sales are initiated through multiple brokers. However, extending this rule to digital asset brokers presents challenges. It can be difficult for a broker to determine whether a digital asset platform qualifies as a broker under these regulations. Also, the assurance that digital asset brokers will adhere to tax reporting obligations isn't as robust as with traditional financial institutions due to different regulatory frameworks. Therefore, although there was deliberation on including digital asset brokers under this multiple broker rule to prevent duplicate reporting, the decision was to not expand the rule in this manner at this time. However, feedback is welcomed on suggestions to mitigate duplicate reporting while ensuring at least one broker reports the transaction, especially when multiple brokers are involved in a single transaction.

Proposed regulations regarding the reporting of digital asset sales by U.S. and, in some cases, non-U.S. brokers when dealing with customers considered as exempt foreign persons.

Currently, such brokers don't need to report on digital asset sales for these customers, based on existing rules. The Organization for Economic Development and Co-operation has created a framework called the Crypto-Asset Reporting Framework (CARF) for reporting and sharing information on crypto-assets among countries. The U.S. Treasury and IRS are considering adopting CARF, which would require some changes to the proposed regulations. The goal is to ensure U.S. brokers collect necessary information for sharing under CARF, while also possibly exempting some non-U.S. brokers from certain data collection requirements. This implementation might also change reporting requirements for transactions involving exempt foreign persons.

Existing rules under section §1.6045-1(a)(1) define when a broker, be it U.S. or non-U.S., is subject to reporting rules based on where the sale was effected. The location of the sale, whether inside or outside the U.S., plays a crucial role, and brokers may use various documents to ascertain a customer's exempt foreign person status. However, these rules are based on traditional business models where brokers interact with customers in person, which is not the case for digital asset brokers who operate online.

The proposed regulations aim to adapt existing rules to the digital business model of digital asset brokers. Unlike traditional brokers, the determination of a sale's location won't be based on the physical location where the sale was made but on the classification of the broker as per proposed §1.6045-1(g)(4). Here, brokers are classified as U.S. digital asset brokers, CFC digital asset brokers, or non-U.S. digital asset brokers. The rules outline how each type of broker should determine a sale's location and how to ascertain a customer's foreign status to identify if they are an exempt foreign person. In addition, the proposal outlines the backup withholding tax provisions applicable to these brokers, with exceptions based on the level of business conducted within the U.S. or the broker's knowledge of a customer's U.S. status.

The proposed regulation § 1.6045-1(g)(4)(i)(A) defines a U.S. digital asset broker as a U.S. payor or middleman, excluding a controlled foreign corporation, that facilitates digital asset sales for customers. Such brokers include U.S. individuals, certain U.S. branches of foreign entities, and foreign entities with significant U.S. business connections. As per these regulations, U.S. digital asset brokers are treated as brokers for all digital asset sales they facilitate for customers.

The regulations also propose rules under § 1.6045-1(g)(4)(ii) for these brokers to ascertain the location of digital asset sales and the foreign status of customers. Generally, all sales made by U.S. digital asset brokers are considered to occur within the United States. These brokers must report sales for customers unless the customer is identified as an exempt recipient or exempt foreign person. There might be backup withholding under section 3406 if the broker fails to obtain a valid Form W-9 from a customer, with some exceptions.

For a U.S. digital asset broker to classify a customer as an exempt foreign person, they must obtain a valid beneficial owner withholding certificate from the customer, unless there's a presumption rule allowing such treatment. Unlike existing rules for securities brokers, U.S. digital asset brokers cannot rely on documentary evidence like foreign driver's licenses to determine a customer's exempt foreign person status. This difference arises due to the challenge of determining the location of digital asset sales.

The Treasury Department and the IRS are seeking feedback on these proposed regulations, particularly on alternative approaches that might help differentiate between a U.S. digital asset broker's domestic and international business operations, allowing for different documentation in the broker's non-U.S. business. This discussion is part of a broader dialogue on the rules U.S. digital asset brokers should follow to classify their customers as exempt foreign persons.

Controlled Foreign Corporation: Proposed regulation § 1.6045-1(g)(4)(i)(B) outlines the rules for Controlled Foreign Corporation (CFC) digital asset brokers that are not operating as Money Services Businesses (MSBs) regarding digital asset sales. A CFC digital asset broker is defined as a controlled foreign corporation that facilitates digital asset sales for customers. According to the proposed rules, such brokers must follow different guidelines to determine the location of a digital asset sale and the foreign status of its customers, based on whether they are deemed to be operating as MSBs concerning sales of digital assets.

In the scenario where a CFC digital asset broker is not operating as an MSB, a sale facilitated by them is considered to be made at an office outside the United States. Like their U.S. counterparts, these CFC digital asset brokers are required to report all sales unless they are made for an exempt recipient or an exempt foreign person. This requirement for reporting all sales is consistent with existing regulations for securities brokers, which categorize controlled foreign corporations as U.S. payors or middlemen, necessitating them to report sales whether they are made inside or outside the United States unless an exception applies.

These proposed regulations allow CFC digital asset brokers, not operating as MSBs, to rely on documentary evidence instead of a withholding certificate to determine if a customer is an exempt foreign person. This aligns with existing regulations for securities brokers, which permit reliance on documentary evidence for sales made at an office outside the United States to ascertain a customer's exempt foreign person status. While the proposed regulations have a different framework, the fundamental principles generally apply to controlled foreign corporations, both under the proposed and existing regulations, unless the CFC digital asset broker is operating as an MSB.

Unlike U.S. digital asset brokers, CFC digital asset brokers not operating as MSBs are not subject to backup withholding for reportable sales unless they know the customer is a U.S. person. Therefore, if such a broker knows a customer is a U.S. person, and the customer fails to provide a valid Form W-9, the broker must report the sale or exchange of a digital asset by that customer to the IRS and apply backup withholding on the gross proceeds of the transaction.

According to the proposed regulation § 1.6045-1(g)(4)(i)(C), a non-U.S. payor or non-U.S. middleman who facilitates digital asset sales for customers is classified as a non-U.S. digital asset broker. These brokers need to follow different rules to ascertain the location of their digital asset sales and the foreign status of their customers, especially for sales occurring within the United States, based on whether they are acting as Money Services Businesses (MSBs) or not.

When a non-U.S. digital asset broker, not operating as an MSB, facilitates a sale, it is generally considered as happening at an office outside the United States, unless there's documentation or information hinting at the customer's connections to the United States or their status as a U.S.

person. For such outside-the-U.S. sales, these brokers are not considered brokers under proposed § 1.6045-1(a)(1) and hence aren't required to report the sale under proposed § 1.6045-1(c).

These regulations don't necessitate non-U.S. digital asset brokers not acting as MSBs to obtain documentation from customers before processing payments. However, under applicable anti-money laundering or other laws, or according to the broker's policies, they might need to collect certain documentation or information, which might reveal the customer's connections to the U.S. or their U.S. person status. When such information is collected, these regulations require the sale to be treated as occurring inside the U.S., and the non-U.S. digital asset broker must report the sale unless the customer is identified as an exempt foreign person or an exempt recipient, or if the account is closed before the sale occurs.

A digital asset sale by a non-U.S. digital asset broker not operating as an MSB is deemed to occur inside the U.S. if, before the payment, the broker collects documentation or information displaying certain U.S. indicia. These indicia include a customer's communication via a U.S.-located device, U.S. permanent residence or mailing address, cash transactions through U.S. banks, or transactions with a U.S.-based digital asset broker. These U.S. indicia are different from those applicable to traditional brokers due to the digital nature of interactions in the case of digital asset brokers.

If a sale is deemed to occur inside the U.S., the non-U.S. digital asset broker, not acting as an MSB, is not required to report the sale if the customer can be treated as an exempt recipient or an exempt foreign person following certain criteria. The type of documentation required to treat a customer as an exempt foreign person varies depending on the U.S. indicia present. For instance, if there's an unambiguous indication of a U.S. place of birth, the broker can still treat the customer as an exempt foreign person if certain other documentation is provided.

In conclusion, non-U.S. digital asset brokers not acting as MSBs have a set of proposed rules to follow concerning the location of digital asset sales, reporting requirements, and the determination of the foreign status of their customers. The Treasury Department and the IRS are open to receiving comments regarding these proposed rules to ensure they are appropriate and sufficient given the digital nature of these transactions and the evolving technological landscape.

Rules for CFC Digital Asset Brokers and Non-U.S. Digital Asset Brokers

Under the Bank Secrecy Act, both Controlled Foreign Corporation (CFC) digital asset brokers and non-U.S. digital asset brokers might be categorized as Money Services Businesses (MSBs) based on certain criteria defined by the Financial Crimes Enforcement Network (FinCEN) of the Treasury Department. MSBs are required by FinCEN to have an effective Anti-Money Laundering (AML) program to prevent facilitating terrorist financing and money laundering. These MSBs have to obtain necessary customer information, make certain reports to FinCEN, register with the Treasury Department, and maintain records about fund transmittals.

The proposed regulation stipulates that these types of brokers, even without a physical presence in the U.S., may have business dealings with U.S. customers. Hence, they are generally subjected to the same rules as U.S. digital asset brokers regarding sales of digital assets. These brokers must determine the place of sale and the foreign status of their customers following the guidelines for

U.S. digital asset brokers. Except for certain sales at foreign kiosks, digital asset sales are considered to occur inside the U.S., requiring these brokers to report sales information unless the customer is identified as an exempt recipient or an exempt foreign person.

The proposal outlines that a broker is considered to be conducting activities as an MSB with respect to digital asset sales if it's registered as an MSB with the Treasury Department. However, an exception is given for sales at digital asset kiosks located outside the U.S. and owned or operated by the broker, unless the broker is required to comply with the Bank Secrecy Act's requirements for MSBs regarding sales at that kiosk.

The rationale behind this approach is to ensure brokers doing business significantly within the U.S. and subject to FinCEN regulation adhere to the same rules as U.S.-based digital asset brokers, given the difficulty in distinguishing between the U.S. and non-U.S. segments of a broker's business. There's a special rule for foreign kiosk sales acknowledging the possibility of determining such a sale is effected outside the U.S. due to the physical presence of the kiosk and the customer outside the U.S.

The Treasury Department and the IRS are also considering extending similar rules to brokers regulated by other U.S. authorities like the Securities and Exchange Commission, the Commodity Futures Trading Commission, and various banking regulators. This consideration stems from the potential significant contact these brokers may have with the U.S. and its customer base, warranting similar diligence and reporting rules as U.S. digital asset brokers for their U.S. business operations.

The proposal also addresses a concern where creating different rules for foreign brokers could potentially incentivize U.S. customers to shift their digital asset transactions to non-U.S.-based brokers, making it harder for the IRS to verify proper transaction reporting. Hence, it suggests applying the same rules to these brokers as for U.S. digital asset brokers to impose similar obligations regardless of where they are organized. The Treasury Department and the IRS are open to comments on whether different diligence and documentation rules should apply to these brokers concerning the non-U.S. part of their business, and if so, how such determination should be made regarding when these different rules would apply.

Documentation, Reliance, and Presumption Rules Applicable to Digital Asset Brokers

In the context of digital asset sales, U.S. and Controlled Foreign Corporation (CFC) digital asset brokers are required to report sales unless the customer is identified as an exempt foreign person or another exception is applicable. The same rule applies to non-U.S. digital asset brokers for sales deemed to occur within the United States. Brokers can establish a customer as an exempt foreign person either through documentation provided by the customer or, in certain circumstances, by presuming the customer to be a foreign individual based on specific criteria.

If a broker lacks documentation, they must make presumptions regarding the customer's classification (such as an individual or entity), and further presume the customer's nationality (U.S. or foreign) based on this classification. If a customer is presumed to be a foreign person, reporting the sales is generally not required. However, if the customer is presumed to be a U.S. person and

doesn't fall under an exempt recipient category, the broker must report the sales unless they obtain documentation to classify the customer as an exempt foreign person.

The type of documentation a broker can rely on varies depending on whether the broker is a U.S., CFC, or non-U.S. digital asset broker, and whether they are operating as a Money Services Business (MSB) concerning digital asset sales. Typically, U.S. and CFC digital asset brokers, along with non-U.S. digital asset brokers operating as MSBs, may rely on withholding certificates to establish a customer's exempt foreign person status. Conversely, CFC and non-U.S. digital asset brokers not operating as MSBs can rely on either a withholding certificate or other documentary evidence like a foreign government-issued identification document to verify a customer's foreign status. Though the documentation type varies, all brokers must adhere to similar standards to ensure the documentation's reliability.

The proposed regulations elaborate on the specific types of documentation brokers can rely on, veering away from the existing regulations for securities brokers which reference different sections of regulatory provisions. However, for rules concerning reliance, validity, and other related matters, the proposed regulations still reference certain existing regulations with some modifications to accommodate the differences between digital asset brokers and securities brokers. This approach of referencing existing rules under specific sections is beneficial as it provides well-established and comprehensible standards for reliance and validity, which many brokers and U.S. tax advisors are already familiar with.

Valid documentation of foreign status: A broker can rely on documentation to verify the foreign status of a customer if the documentation is valid, can be reliably linked to a payment, and the broker has no knowledge or reason to believe that the documentation is incorrect or unreliable. The proposed regulations reference specific sections of existing regulations for the documentation requirements applicable to digital asset brokers, with certain modifications. These referenced sections also provide guidelines on the duration a broker can rely on a withholding certificate or documentary evidence, and other rules concerning withholding certificates such as who can sign them, when a substitute certificate can be used, and when a taxpayer identification number must be included.

Additionally, the existing regulations contain rules permitting documentation to be obtained electronically or from third-party repositories. Some rules provide more favorable treatment to financial institutions due to the high volume of accounts they handle. Given digital asset brokers may also have a high volume of customer accounts, the proposed regulations allow them to apply certain favorable rules regardless of whether they are financial institutions. The referenced sections also stipulate how long a broker must retain a withholding certificate and the procedures for obtaining, reviewing, and maintaining documentary evidence.

Furthermore, brokers can rely on the documentation without needing to verify the accuracy of the information it contains, unless they have reason to believe it's incorrect. The proposed regulations incorporate this rule but provide specific guidelines for when a broker should suspect that documentation might be incorrect or unreliable.

Lastly, to reliably associate a payment with valid documentation, a broker must hold valid documentation (either directly or through an agent) before the payment, be able to reliably determine the portion of the payment related to the valid documentation, and have no actual knowledge or reason to suspect that any information, certifications, or statements in or associated with the documentation are incorrect.

Presumption rules: If a broker lacks customer documentation, or if the documentation is invalid or can't be linked to a payment, the proposed regulations suggest using presumption rules. These rules also apply if the documentation has expired or the broker knows or has reason to believe it's incorrect or unreliable. The broker can classify a customer (as an individual or entity, for example) using the presumption rules mentioned in specific sections, with certain modifications.

In situations where there's no reliable indication of a customer's classification, the customer might be presumed to be an exempt recipient, provided they can be treated as such without needing to furnish documentation. However, since the exempt recipient categories differ under various sections, the proposed regulations suggest a replacement to align with the correct exempt recipient categories.

The proposed regulations also provide presumption rules to decide if a customer is a U.S. or foreign person in the absence of documentation. The existing regulations for securities brokers generally require a broker to presume an individual to be a U.S. person, but the proposed regulations for digital asset brokers alter this based on the broker's status rather than the location of the customer's obligation or where the payment is made. Specifically, a U.S. digital asset broker or a broker conducting activities as an MSB must treat an undocumented individual customer as a U.S. person, whereas a broker not conducting activities as an MSB only needs to do this when there are certain U.S. indicia for the customer.

For customers presumed to be entities, brokers can generally determine their U.S. or foreign status using the presumption rules in specified sections, except for one rule related to offshore obligations, which is not applicable as digital asset activities are primarily conducted online with no identifiable location. The proposed regulations suggest a similar presumption rule for digital asset brokers as that for securities brokers, disregarding the concept of payments made with respect to offshore obligations due to the online nature of digital asset activities.

Grace period for obtaining documentation: The proposed regulations include a grace period to allow brokers some time to obtain the necessary documentation or additional documentation if the original is found to be incorrect or unreliable. According to Proposed § 1.6045-1(g)(4)(vi)(A)(3), a broker can use the grace period outlined in § 1.6049-5(d)(2)(ii). This grace period allows a payor to treat an account as owned by a foreign person until either 90 days from when the account is first credited (for new accounts) or from when it's first credited after realizing the existing documentation is no longer reliable (for existing accounts), or until the remaining account balance is equal or less than 24 percent of the total credited amounts during the grace period, whichever comes first.

For a payor to use this grace period, at the start of the grace period, the account holder's address in the payor's records must be in a foreign country, the payor must have received the information in

a withholding certificate as described in § 1.1441-1(e)(2), or the payor holds a withholding certificate that is no longer reliable for reasons other than the expiry of the validity period.

By referencing § 1.6049-5(d)(2)(ii), the proposed regulations extend the same grace period to digital asset brokers as is given to payors under section 6049 who hold securities in customer accounts and securities brokers making sales of securities under section 6045. This provides a structured timeframe for digital asset brokers to gather the necessary documentation while aligning with the procedures followed by securities brokers.

Standards of knowledge for reliance on withholding certificates: The proposed regulations stipulate that a broker can rely on documentation only if there's no knowledge or reason to believe that the documentation is incorrect or unreliable. In these regulations, certain provisions are outlined for digital asset brokers to follow regarding the reliance on withholding certificates and beneficial owner withholding certificates. Specifically, a digital asset broker can rely on a beneficial owner withholding certificate to treat a customer as an exempt foreign person, unless there are clear indications in the broker's account files suggesting U.S. status which would raise doubts about the reliability or accuracy of the withholding certificate.

The regulations provide a list of U.S. indicia that would trigger a re-evaluation of the withholding certificate's reliability. In such cases, brokers are required to obtain additional documentation to continue relying on the withholding certificate. This additional documentation should prove the foreign status of the customer and could include identification from a foreign government. Moreover, the customer must provide a reasonable written explanation supporting their claim of foreign status if there are U.S. indicia present.

For digital asset brokers, if a customer has been previously classified as a U.S. person in its account information, then to reclassify them as an exempt foreign person, stringent documentation evidencing citizenship in a country other than the U.S. must be obtained. For entity customers, documentation substantiating that the entity is organized or created under the laws of a foreign country is required.

Moreover, if a broker is a non-U.S. person, they may treat a customer as an exempt foreign person if the payment to the customer is reported to the jurisdiction in which the customer resides, given that the jurisdiction has tax information exchange agreements or income tax treaties with the U.S.

Lastly, if there's unambiguous information showing a U.S. place of birth for the customer, a broker can only treat the customer as an exempt foreign person if they possess certain documentary evidence proving foreign citizenship, along with either a copy of the customer's Certificate of Loss of Nationality of the United States or a reasonable written explanation regarding the customer's renunciation of U.S. citizenship or the reason the customer did not obtain U.S. citizenship at birth.

In summary, these provisions are set to ensure the accuracy and reliability of the documentation digital asset brokers rely on, especially when determining the tax status of their customers, and provide a structured approach to deal with situations where the documentation may be incorrect or unreliable.

Standards of knowledge for reliance on documentary evidence: The proposed section outlines the circumstances under which a broker has reason to suspect that documentary evidence might be incorrect or unreliable. This assessment is triggered when certain U.S. indicators, as outlined in the proposed regulations, are present in the broker's account files for a customer. In such cases, to continue relying on the documentary evidence, the broker is required to collect additional documentation.

The types of additional documentation specified are akin to those outlined in a different section of the regulations concerning withholding certificates, albeit with certain modifications. One notable difference is that in some cases, a broker is allowed to obtain a withholding certificate instead of collecting more documentary evidence.

Essentially, these provisions are designed to ensure the accuracy and reliability of the information on which brokers rely, particularly in the context of identifying the tax status of their customers, while providing a structured recourse should the initial documentary evidence prove to be unreliable or incorrect due to the presence of conflicting U.S. indicia.

Joint owners: The proposed regulations state that if there are amounts paid to customers who hold joint accounts, and if a certificate or documentation is needed for exemption from reporting under certain sections, then these amounts are presumed to be paid to U.S. payees who are not exempt recipients under specified conditions. This rule aligns the treatment of digital asset brokers with securities brokers concerning amounts paid to customers holding joint accounts. By doing so, it provides a uniform approach to handling payments to joint account holders across both digital asset and securities brokers when it comes to reporting requirements.

Foreign intermediaries, foreign flow-through entities, and certain U.S. branches: The section outlines the proposed rules for brokers to ascertain whether a customer is a foreign intermediary, foreign flow-through entity, or a U.S. branch, and if so, whether they can be treated as an exempt foreign person. These proposed regulations are similar to those applicable to securities brokers but provide more detail for digital asset brokers.

A broker can rely on a valid foreign intermediary withholding certificate to determine a customer's classification. There's a modification allowing brokers not to obtain withholding certificates or other documentation for the intermediary's account holders, although this is under consideration for change to avoid regulation circumvention by U.S. persons selling digital assets through foreign intermediaries.

For foreign flow-through entities, brokers may rely on valid foreign flow-through withholding certificates without needing to obtain documentation for the entity's partners. The need for obtaining documentation on partners, beneficiaries, or owners is under consideration to prevent circumvention of these regulations.

If a broker doesn't obtain valid certificates, presumption rules are employed to determine the status of a customer and whether they are U.S. or foreign.

The regulations also cover documentation and presumption rules for payments to a customer that is a U.S. branch. The broker can rely on a valid U.S. branch withholding certificate to determine

the status of a U.S. branch. If a U.S. branch certifies that it agrees to be treated as a U.S. person, the broker can treat it as an exempt foreign person. However, if it doesn't certify, the broker can still treat the U.S. branch as an exempt foreign person unless there is actual knowledge that the person for whom the U.S. branch receives payment is a U.S. person who is not an exempt recipient.

These guidelines provide a detailed structure for brokers to adhere to while dealing with different types of entities and ensuring compliance with the regulatory framework, especially in the complex landscape of digital assets.

Coordination with Rules Applicable to Sales of Securities

The IRS/Treasury proposed rules also discuss the challenges brokers might face when dealing with sales of both securities and digital assets, particularly in identifying whether a sale is conducted inside or outside the US, and if a customer can be treated as an exempt foreign person. The current and proposed regulations under § 1.6045-1(g) are seen as potentially complex for brokers dealing in both asset types.

Although the Treasury Department and the IRS considered a coordination rule to simplify compliance, it wasn't proposed due to the distinct nature of rules needed for digital assets and securities transactions. They are inviting comments to understand if a coordination provision would be beneficial and how it could be structured to ease the brokers' compliance while dealing with both types of assets.

Transition Period: There is a proposed transition period to allow digital asset brokers ample time to gather required documentation from existing customers to ascertain their exempt foreign status under the proposed regulations. For digital asset sales made before January 1, 2026, from accounts set up at a broker before January 1, 2025, brokers can classify a customer as an exempt foreign person, provided they haven't previously labeled the customer as a U.S. person, and the information available, including the residence address from account opening files or other related files, indicates a non-U.S. address.

Special Rules for Barter Exchanges that Effect Certain Digital Asset Exchanges

The section outlines special rules for barter exchanges involved in certain digital asset exchanges. According to existing regulations, a person or organization facilitating trades or barters of property or services among its members or clients is deemed a barter exchange. However, a merchant exchanging goods or services for a customer's digital asset is excluded from this definition. Exchange through a barter system is recognized if payments are made via credits on the exchange's books, scrip issued by the exchange, or if the exchange orchestrates a direct swap of goods or services between members.

The existing regulations don't explicitly cover digital asset exchange transactions for property or services, which creates ambiguity. A single exchange transaction might be seen as a sale executed by a broker and also as an exchange transaction carried out by a barter exchange. It might also be perceived as a reportable payment transaction facilitated by a Third Party Settlement Organization (TPSO) alongside an exchange transaction by a barter exchange.

The proposed rules aim to prevent duplicate reporting by establishing coordination rules for barter exchanges that also act as brokers. Specifically, when one digital asset is exchanged for a different digital asset between customers of the same broker, the transactions are treated as sales, subject to broker reporting rules, and not as exchanges via a barter exchange.

In scenarios where digital assets are swapped for personal property or services, and the digital asset payment is a reportable transaction, different reporting rules are proposed depending on the nature of the asset being disposed of by each member or client. For those disposing of personal property or services, the exchange must be reported as a reportable payment transaction, whereas for those disposing of digital assets, the exchange must be reported as a sale under broker reporting rules.

The aim of these rules is to ensure that brokers report all digital asset exchanges, which are also subject to barter exchange reporting provisions, under the broker reporting rules. The text does not imply whether digital asset exchanges fall under existing barter exchange reporting rules. The Treasury and the IRS seek comments on the extent of broker-facilitated digital asset transactions still under barter exchange reporting rules post the implementation of the proposed regulations, and if there are any broker-mediated transactions not categorized as reportable payment transactions for the client receiving digital assets as payment.

Additional Definitions and Definitional Changes

The section elaborates on additional definitions and changes aimed at clarifying terms related to digital assets and their management. It emphasizes the idea of holding or controlling digital assets through private keys, whether directly or indirectly via a custodian. Digital assets are considered held in a wallet or account if the wallet or account stores the private keys necessary to control or transfer access to the digital assets. The terms such as held at a broker, held by the user of a wallet, etc., are explained to have similar meanings pertaining to the holding or control of digital assets in a wallet or account.

Hosted wallets are defined as custodial services where private keys to digital assets are electronically stored on behalf of others, while unhosted wallets are non-custodial means, either electronic or other, of storing a user's private keys for digital assets held by or for the user. Unhosted wallets can be either connected to the internet (hot wallet) or disconnected (cold wallet).

The definition of cash is updated to include U.S. dollars and convertible foreign currency issued by a government or central bank, in either physical or digital form. Central bank digital currencies are treated as cash and not digital assets under these proposed regulations. Privately-issued digital assets remain excluded from the cash definition.

Stablecoins, digital assets with values generally linked to other assets, are not included in the cash definition as their values may fluctuate, and they may not be fully collateralized. The proposal doesn't exclude stablecoin transactions from sale definitions due to potential inconsistencies in value reflection. Feedback is solicited on whether stablecoins or a subset should be treated differently for these rules, and on the reporting of transactions involving U.S. dollar-related stablecoins with no gain or loss.

Comments are also requested on tokenized deposits or other tokenized assets closely linked to cash held in an account, and how they are structured and used.

The document clarifies the list of governmental exempt recipients by specifying territorial jurisdictions to which the existing exemption for "a possession of the United States" applies. It also republishes definitions for terms like security, barter exchange, and others, with added headings and necessary formatting changes.

Lastly, the proposed regulations specify that certain existing rules, not applicable to digital assets, are limited to securities only, ensuring no change in how the regulations apply to assets currently covered by existing rules.

Proposed 28 C.F.R. §§ 1.1001-7, 1.1012-1(h), and 1.1012-1(j)

The IRS/Treasury discusses new proposed regulations as compared to existing guidance under sections 1001 and 1012 concerning tax rules for digital assets transactions. These rules help in determining the amount realized by a taxpayer on the disposition of digital assets and the basis for purchased digital assets. For instance, transferring digital assets between wallets owned by the same taxpayer is not considered a sale or disposition under section 1001. However, if a transfer fee is paid with digital assets to facilitate this transfer, it's considered a sale or disposition under section 1001, which could result in gain or loss.

The text mentions that there are certain scenarios where taxpayers might benefit from additional clarification. These scenarios include exchanges of digital assets for services or other properties, including different digital assets, and dispositions of a portion of a taxpayer's holdings of a particular digital asset, especially if the holdings were acquired at different times or at different prices. The aim is to provide clear guidance on how these transactions should be treated for tax purposes, ensuring that taxpayers have the necessary information to comply with tax laws when engaging in digital asset transactions.

The amount realized: The text outlines the proposed regulation 28 C.F.R. § 1.1001-7(b)(1)(i) regarding how to determine the amount realized from a sale or disposition of digital assets for cash, other materially different property, or services. It stipulates that the amount realized is the total cash received, the fair market value of property received, and the fair market value of services received, minus the relevant digital asset transaction costs. If digital assets are used to cover transaction costs, this act is considered a disposition of digital assets for services. The text also provides specifics on calculating amounts related to debt instruments exchanged for digital assets, and how digital asset transaction costs should be allocated in various scenarios including the exchange of one digital asset for another.

In exchange of one digital asset for another, a single digital asset transaction cost may be charged, and the proposed rule suggests splitting this cost equally between the disposition of one digital asset and the acquisition of the other. The text also mentions a scenario where a transfer fee incurred during a non-taxable transfer of digital assets is considered a taxable event if digital assets are used to pay the fee.

Lastly, rules for determining the fair market value of digital assets, and the fair market value of services or property received in return for digital assets are provided. The fair market value of a digital asset is to be determined at the time of the exchange or disposition, and if the fair market value of the received property or services can't be determined accurately, it should be referenced to the fair market value of the digital assets transferred at the time of exchange. The authorities are seeking comments on these proposed regulations, especially on the allocation of digital asset transaction costs in digital asset exchanges, to assess the administrability and potential alternatives to the proposed rules.

Basis: This section discusses the proposed guidelines for determining the basis of digital assets, which is the starting point for tax calculations. The basis is generally the cost or value of what is given in exchange for the digital assets acquired. It elaborates on different scenarios like purchasing digital assets for cash, exchanging them for services, other properties, or debt instruments, or acquiring them in a part sale and part gift transaction.

In exchanges, both the amount realized from the assets transferred and the basis of the assets received are usually determined by the fair market value of the received assets. The proposed regulations aim to ensure that the sum of gains or losses from an exchange and a subsequent transaction involving the received assets equals the economic gain on the combined transactions. The basis of digital assets acquired in an exchange should equal the cost of the received assets at the time of the exchange, inclusive of allocable digital asset transaction costs.

Specific rules are provided for different scenarios like when digital assets are purchased for cash, where the basis is the cash paid plus any allocable transaction costs. Similarly, rules are provided for exchanges involving properties other than digital assets and exchanges involving different digital assets. Special rules are also outlined for determining the basis of digital assets received in exchange for services, debt instruments, or in part sale and part gift transfers.

The proposed guidelines also provide rules for allocating digital asset transaction costs to the basis of digital assets acquired, especially in exchanges of digital assets differing materially in kind or extent. In such cases, half of the total transaction costs are allocable to the acquired assets' basis.

Lastly, the rules for determining the cost of digital assets received in certain exchanges are provided. The cost is generally the fair market value of the digital assets at the time of the exchange, with a provision for referencing the transferred property's value when the received digital assets' fair market value cannot be accurately determined. This section of the proposed regulation aims to provide a structured approach to determine the basis of digital assets for tax purposes across varying transaction scenarios.

Identification rules: The section discusses proposed rules for identifying which units of a particular digital asset are sold, disposed of, or transferred when not all units are transacted from a single wallet or account. These rules are categorized based on whether the digital assets are held in unhosted wallets or are in the custody of a broker.

For unhosted wallets, a specific identification of the units being transacted needs to be made. If not specified, the units are determined in order from the earliest purchase date. Adequate records

must be maintained to ensure accurate identification of units for subsequent transactions. The Treasury Department and the IRS are seeking comments on methods to ease the tracking of purchase dates and the basis of digital assets in unhosted wallets, and on whether the ordering rules should be applied on a wallet-by-wallet or address-by-address basis, or alternatively.

For digital assets in the custody of a broker, taxpayers can make an adequate identification by specifying to the broker the particular units to be transacted, by reference to any identifier the broker designates as sufficient. Without such identification, the units are determined based on the order of time from the earliest units purchased or transferred into the account. The Treasury Department and the IRS are seeking comments on whether this rule should apply on an account-by-account basis or if brokers have systems that can better account for transactions. They are also interested in opinions on whether exceptions should be made to allow brokers to use reasonably reliable purchase date information from outside sources.

The proposed regulations also mention that the method of identifying the units of a digital asset transacted is not considered a method of accounting, which means that taxpayers can decide how to identify those units each time a transaction occurs, without being bound to a consistent method. This provision allows for flexibility in identifying the units being transacted, for instance, by the earliest acquired, the latest acquired, or the highest basis, without invoking a change in accounting method under the tax code sections 446 and 481.

Proposed 26 C.F.R. § 1.6045-4: Real Estate Transactions

The proposed regulations under § 1.6045-4 extend the reporting requirements for real estate transactions involving digital assets. Initially, real estate reporting persons are tasked to report the fair market value of digital assets received by sellers (transferors) in real estate transactions. Specific details like the name and number of units of the digital asset used, the date and time of payment, transaction identification, and digital asset address(es) to which the assets are transferred should be reported as per § 1.6045-4(h)(1)(vii). This section also enlarges the definition of gross proceeds to encompass payments made using digital assets received by the real estate transferor under § 1.6045-4(i).

Three notable amendments are made to ensure all payments using digital assets are included in the reported amount. Firstly, § 1.6045-4(i)(1) elucidates that total cash received in a real estate transaction includes cash received from a digital asset payment processor in exchange for digital assets paid by the real estate buyer. Secondly, to maintain consistency, the phrase "cash ... to be received" is replaced with "consideration treated as cash" in § 1.6045-4(i)(1). Lastly, gross proceeds now encompass the value of digital assets received by the transferor, with the value being the fair market value of digital assets actually received or the fair market value of digital assets to be paid as a stated principal under an obligation if the transferor receives such an obligation.

Unrelated to digital asset transactions, § 1.6045-4 is updated to mirror the exception from reporting for gross income up to $250,000 of gain on the sale or exchange of a principal residence under certain conditions as per section 6045(e)(5) and § 1.6045-4(c)(2)(iv). Additionally, it reflects statutory changes in section 6045(e)(3) which discusses the unlawful act of separately charging any customer for compliance with reporting under section 6045, yet allows real estate reporting

persons to factor in their compliance costs when establishing charges for services in real estate transactions as per § 1.6045-4(o). Lastly, the list of governmental exempt transferors is clarified under § 1.6045-4(d)(2)(ii)(A) by listing specific territorial jurisdictions to which the exemption for "a possession of the United States" applies.

Proposed 28 C.F.R. §§ 1.6045A-1 and 1.6045B-1

The mentioned proposed regulations do not encompass or enact the modifications necessitated by the Infrastructure Act regarding transfer statement reporting for digital asset transfers under section 6045A(a) or broker information reporting under section 6045A(d) for digital asset transfers that are neither sales nor transfers to accounts overseen by individuals that the transferring broker is aware, or has grounds to know, are also brokers.

Due to the uncertainty regarding the application of sections 6045A and 6045B to assets characterized both as digital assets and specified securities under existing regulations, the Treasury Department and the IRS have postponed transfer statement reporting under section 6045A(a) and issuer reporting under section 6045B for such dual classification assets until further guidance is provided. Consequently, proposed §1.6045A-1(a)(1)(vi) has been introduced to particularly exclude from transfer statement reporting any specified security also identified as a digital asset. However, transferors who opt to furnish a transfer statement reporting some or all of the information outlined in section 6045A will not incur penalties under section 6722 for incorrect reporting. Analogously, proposed § 1.6045B-1(a)(6) also exempts issuers from reporting on any specified security also recognized as a digital asset. Therefore, under these provisions, the transfer of a specified security as defined in proposed § 1.6045-1(a)(14)(i) through (iv) or an issuer of a specified security as defined in proposed § 1.6045-1(a)(14)(i) through (iv) will not be bound by the reporting rules of section 6045A and section 6045B if the specified security also meets the definition of a digital asset under proposed § 1.6045-1(a)(19). Issuers opting for this reporting will not be penalized under either section 6721 or section 6722 for incorrect reporting or furnishing of this information.

The Treasury Department and the IRS plan to explore guidance for these dual classification assets during the implementation of broader transfer statement reporting under section 6045A(a), broker information reporting under section 6045A(d), and digital asset issuer reporting under section 6045B in a subsequent phase of information reporting guidance. Inputs are invited on whether sections 6045A and 6045B should be enforced for securities also identified as digital assets prior to this later phase of information reporting guidance. Additionally, comments are solicited regarding the identification of the responsible party required to execute the reporting if section 6045B is enforced for securities also recognized as digital assets before the implementation of this later phase of information reporting guidance.

Proposed 26 C.F.R. § 1.6050W-1

The proposed regulations acknowledge that some digital asset brokers categorize payments for digital assets, or exchanges of one digital asset for another, as reportable under section 6050W. However, they don't affirm the correctness of such categorizations under the existing regulations.

In cases where these transactions are reportable under proposed § 1.6045-1 post the applicability date, they must be reported under section 6045 to prevent double reporting.

Proposed § 1.6050W-1(c)(5)(i)(A) outlines a scenario where a payor uses digital assets in a third-party network transaction to exchange for goods or services. If this payment is deemed a sale of digital assets by the payor as per section 6045 broker reporting rules, the amount paid to the payor in settlement will be subject to broker reporting rules, not section 6050W. Similarly, proposed § 1.6050W-1(c)(5)(i)(B) provides that if an exchange constitutes a sale of digital assets by the payee under section 6045, the payment to the payee will be reported under the broker reporting rules, not section 6050W.

To prevent duplication in reporting, rules have been provisioned for certain exchanges involving digital assets for goods or services potentially treated as barter exchanges. Proposed § 1.6050W-1(c)(5)(i)(A) ensures that if a purchaser is subject to reporting under proposed §1.6045-1 due to the use of digital assets for payment, reporting under section 6050W is not required. Proposed § 1.6050W-1(c)(5)(i)(B) extends this to the payee selling goods and services in return for digital assets, specifying that any digital asset paid to a person in a third-party network transaction reportable under proposed § 1.6045-1(e) should be reported under section 6050W, not the barter exchange rules under proposed § 1.6045-1(e). Therefore, reporting is mandated under section 6050W for a payee selling goods or services (excluding digital assets) in exchange for digital assets in third-party network transactions, provided the fair market value of aggregate payments exceeds the de minimis exception outlined in section 6050W(e) for reportable payments post-January 1, 2023.

In particular, instances where a Third Party Settlement Organization (TPSO) operates as a digital asset payment processor as per proposed § 1.6045-1(a)(22)(i)(B), a payment made with digital assets directly to a TPSO's participating payee could be a third-party network transaction subject to reporting. Proposed § 1.6050W-1(a)(2) clarifies that in cases where a TPSO, having a contractual obligation to pay participating payees, receives a payment instruction from a purchaser to transfer funds directly to a participating payee's account for settling a reportable payment transaction, such a payment should be treated as a payment made in settlement of a reportable payment transaction, requiring reporting under section 6050W concerning the participating payee.

Proposed 26 C.F.R. §§ 31.3406(b)(3)-2, 31.3406(g)-2, and 31.3406(g)-1

The proposed regulations under sections 31.3406(b)(3)-2, 31.3406(g)-2, and 31.3406(g)-1 of the Code discuss the requirement for certain payors to deduct and withhold tax at the statutory backup withholding rate of 24% on reportable payments if a payee fails to provide a correct Taxpayer Identification Number (TIN). The existing rules under § 31.3406(b)(3)-2(a) have been broadened to encompass digital asset transactions that are reportable under section 6045, without making any substantive changes. Specifically, § 31.3406(b)(3)-2(b)(2) provides backup withholding rules for brokers reporting on certain types of contracts and transactions, including those involving digital assets. However, since the rules under § 31.3406(b)(3)-2(b)(3) and (4) are limited to securities, they don't apply to most digital assets. Comments are requested on whether amendments are needed to address digital assets treated as securities or short sales of digital assets.

Proposed § 31.3406(g)-2(e) revises existing regulations to clarify that real estate reporting persons must backup withhold on reportable payments related to digital asset dispositions by real estate buyers, under section 3406 and as per the rules in proposed § 31.3406(b)(3)-2. This aims to ensure consistent treatment of customers who exchange digital assets for property in transactions effected by a broker.

Furthermore, an amendment in proposed § 31.3406(g)-1(e) extends an existing exception on backup withholding on gross proceeds for sales effected at an office outside the United States to sales of digital assets by certain foreign brokers. This adjustment applies to Controlled Foreign Corporation (CFC) digital asset brokers and non-U.S. digital asset brokers, provided they are not acting as Money Services Businesses (MSBs) with respect to the sale.

In summary, these proposed regulations extend and clarify the backup withholding requirements to encompass digital asset transactions, ensuring tax compliance and consistent treatment across different types of transactions and assets.

Request for Comments

The IRS and Treasury Request for Comments section is seeking feedback on the proposed regulations concerning digital asset transactions. The inquiries are extensive, covering various facets of digital asset transactions, definitions, reporting requirements, and the applicability of existing tax laws. Here's a concise summary of the primary areas of concern:

1. Definition of Digital Assets: The appropriateness of the proposed definition of digital assets and its application in the regulations.

2. Impact on Non-digital Asset Securities: Whether the definition or reporting requirements inadvertently affect transactions involving non-digital asset securities using distributed ledger technology.

3. Exceptions for Certain Transactions: Suggestions on drafting exceptions for transactions involving non-digital asset securities processed using distributed ledger technology.

4. Reporting Digital Asset Options: The frequency and alternative reporting methods for digital asset options that are also section 1256 contracts.

5. Unique Aspects of Digital Asset Transactions: Differences in undertaking transactions involving digital assets compared to non-digital assets, and any unaddressed reporting issues.

6. Privacy Concerns and Reporting Approaches: Alternative reporting approaches for digital asset trading platforms with limited customer information to balance tax compliance and privacy concerns.

7. Technological Issues for Non-custodial Platforms: Challenges faced by non-custodial digital asset trading platforms in complying with the proposed regulations.

8. Scope of Reporting Obligations: The adequacy of applying reporting rules only to "persons" in control of digital asset trading platforms.

9. Wallet Provider's Role: Whether providing connection software by a wallet provider to a trading platform should be considered a facilitative service.

10. Facilitative Services by Wallet Providers: Additional functions by wallet software that should be considered facilitative services.

11. Determining Control or Influence: Factors relevant to determining control or influence over provided facilitative services.

12. Governance of Digital Asset Trading Platforms: The extent of control or influence maintained by operators or governance token holders over digital asset trading platforms.

13. Treatment of Governance Token Holders: The extent to which governance token holders should be treated as operating a digital asset trading platform business.

14. Alternative Reporting for Digital Asset Payment Processors: Alternative reporting approaches for digital asset payment processors affecting payments to merchants.

15. Frequency of Digital Asset Redemptions: The frequency with which creators or issuers redeem digital assets.

16. Applicability to Initial Coin Offerings (ICOs) and Similar Contracts: Whether broker reporting regulations should apply to ICOs, simple agreements for future tokens, and similar contracts.

17. Consideration for Digital Asset Exchanges: The breadth of consideration types for digital asset exchanges.

18. Logistical Concerns: Concerns about reporting on contracts involving the delivery of digital assets.

19. Forward Contracts Involving Digital Assets: The frequency of trading forward contracts involving digital assets and additional issues for brokers to report on these transactions.

20. Addressing Uncovered Transactions: Revising definitions to cover transactions not addressed in the proposed regulations.

21. Reporting Transaction ID Information: Less burdensome alternatives to reporting transaction ID information and digital asset addresses.

22. Annual Digital Asset Sale Threshold: Proposing an annual digital asset sale threshold for reporting transaction ID information and digital asset addresses.

23. Time Reporting Standard: Whether to report time using a 12-hour or 24-hour clock and the feasibility of a uniform time standard.

24. Uniform Time Standard Concerns: Concerns regarding the burdensomeness of a uniform time standard.

25. Alternative Time Basing: Alternatives to basing the transaction date on UTC for customers in different time zones.

26. Valuation of Services: How the fair market value of services giving rise to digital asset transaction costs should be determined.

27. Avoiding Duplicative Broker Reporting: Suggestions to avoid duplicative multiple broker reporting for sale transactions involving digital asset brokers.

28. Differentiating Between U.S. and Non-U.S. Business: Alternative approaches to differentiate between a U.S. digital asset broker's U.S. business and non-U.S. business for documentation purposes.

29. U.S. Indicia for Digital Asset Brokers: Appropriateness and sufficiency of the U.S. indicia listed in the proposed regulations.

30. Identifying U.S. Organization of Digital Asset Brokers: Defining when a broker has reason to know that a digital asset broker is organized within the United States.

31. Administrable Rules for CFC and Non-U.S. Digital Asset Brokers: Administerable rules that would allow different rules for U.S. and non-U.S. business activities of CFC and non-U.S. digital asset brokers.

32. Diligence and Documentation Rules: Whether different diligence and documentation rules should apply to CFC and non-U.S. digital asset brokers concerning the non-U.S. part of their business.

33. U.S. Regulatory Schemes for CFC and Non-U.S. Digital Asset Brokers: Identifying U.S. regulatory schemes applicable to CFC and non-U.S. digital asset brokers other than registration with FinCEN.

34. Documentation on Account Holders: Whether requiring brokers to obtain documentation on account holders would increase transparency sufficiently to justify the increased burden on brokers.

35. Coordination Provision for Brokers: Whether a coordination provision for brokers affecting transactions involving both non-digital asset securities and digital assets would be helpful.

36. Broker-facilitated Transactions and Barter Exchange Rules: Additional broker-facilitated transactions involving digital assets subject to reporting under the barter exchange rules.

37. Treatment of Stablecoins: Assessing whether stablecoins or a subset of stablecoins, should be treated as digital assets for the purposes of these regulations.

38. Excluding Reporting on Certain Stablecoin Transactions: Whether reporting should be excluded on transactions involving the disposition of U.S. dollar-related stablecoins that give rise to no gain or loss.

39. Adequate Reporting of Stablecoin Transactions: Suggestions for changes to ensure adequate reporting of transactions involving the receipt or disposition of stablecoins.

40. Cascading Digital Asset Transaction Costs: Treatment of cascading digital asset transaction costs.

41. Allocation of Digital Asset Transaction Costs: Administrability of allocating one-half of total digital asset transaction costs to the disposition of digital assets.

42. 100 Percent Allocation of Digital Asset Transaction Costs: Whether a 100 percent allocation of digital asset transaction costs to the disposed-of digital asset would be less burdensome.

43. Unhosted Wallets Tracking: Methods or functionalities that unhosted wallets can provide to assist taxpayers with tracking purchase dates, times, and/or the basis of specific units of a digital asset.

44. Ordering Rules for Unhosted Wallets: Whether the ordering rules for unhosted wallets should be applied on a wallet-by-wallet basis or some other basis.

45. Ordering Rules for Digital Assets in Broker Custody: Alternatives to requiring that the ordering rules for digital assets left in the custody of a broker be followed on an account-by-account basis.

46. Exceptions to Ordering Rule: Should exceptions be made to the ordering rule for digital assets left in the custody of a broker to allow brokers to take into account reasonably reliable?

Additional Questions: The IRS and Treasury also seek feedback on aspects not specifically covered in the proposed regulations. Here's a simplified summary:

1. Data Handling by IRS: Suggestions are sought on how the IRS should plan for the management of information reported under these regulations, covering receipt, storage, retrieval, and usage.

2. Voluntary Engagement Between Brokers: The regulations anticipate that reporting brokers may voluntarily engage with acquiring brokers to obtain basis information on certain transactions. Feedback is requested on what would encourage reporting brokers to voluntarily obtain and provide this information.

Applicability Dates:

• The proposed regulations regarding the computation of gain or loss and the basis of digital assets are to apply from January 1 of the year following their finalization.

• Taxpayers may rely on these proposed regulations for dispositions in taxable years ending on or after the publication date in the Federal Register, provided they follow the regulations consistently.

• The proposed regulations require brokers to report gross proceeds from digital asset sales effected on or after January 1, 2025, and to report the adjusted basis and character of any gain or loss for sales or exchanges effected on or after January 1, 2026.

• For assets classified as commodities, the regulations apply to sales on or after January 1, 2025.

• Changes concerning reporting on real estate transactions apply to transactions with closing dates on or after January 1, 2025.

• Changes concerning transfer statements and organizational actions apply from the date of the publication of the final regulations in the Federal Register.

• Regulations concerning payments made in digital assets apply to payments made on or after January 1, 2025.

• Regulations concerning penalties for failing to file or furnish an information return apply to sales effected on or after January 1, 2025.

• Regulations concerning backup withholding apply to sales of digital assets on or after January 1, 2025.

Special Analyses:

The proposed regulations underwent review under section 6(b) of Executive Order 12866, in line with the Memorandum of Agreement (April 11, 2018) between the Treasury Department and the Office of Management and Budget regarding the review of tax regulations.

Regulatory Planning and Review by the Office of Information and Regulatory Affairs (OIRA): Economic Analysis discusses the directive from Executive Orders 13563 and 12866, which mandates agencies to evaluate the costs and benefits of available regulatory alternatives. Should regulation be required, the directive encourages the selection of regulatory strategies that maximize net benefits, which encompass potential economic, environmental, public health and safety effects, distributive impacts, and equity. Executive Order 13563 particularly emphasizes the importance of quantifying both costs and benefits, reducing costs, harmonizing rules, and promoting flexibility.

The proposed regulations under discussion were subjected to review by the Office of Information and Regulatory Affairs (OIRA) as per Executive Order 12866, following a Memorandum of Agreement (April 11, 2018) between the Treasury Department and the Office of Management and Budget (OMB) concerning the review of tax regulations. These regulations were designated as significant under section 1(c) of the Memorandum of Agreement, and as a result, they were reviewed by the OMB.

Economic Analysis

The IRS/Treasury report further delves into the implications of these proposed regulations on the digital asset sector. Initially, a baseline scenario of no-action is established to gauge the effects of the proposed regulations. The global digital asset market, as per the document, is valued at around $1 trillion as of January 2023, although the share held by U.S. taxpayers remains unclear.

The report discusses the definition of digital assets, which is derived from the Infrastructure Investment and Jobs Act. This definition emphasizes the cryptographic security and distributed ledger technology inherent in digital assets. The regulations aim to extend the realm of information reporting to brokers involved in digital asset transactions, thereby clarifying the role and responsibilities of brokers in this domain.

The report goes on to cover various forms of digital assets including stablecoins and non-fungible tokens (NFTs). The report maintains that transactions involving these types of digital assets should be subject to these proposed regulations, underlining the importance of reporting in maintaining transparency and compliance.

In addressing the allocation of transaction costs in digital asset exchanges, the IRS and Treasury propose an approach that attempts to avoid administrative complexities. This section elaborates on how transaction costs should be allocated, advocating for a simple, unified rule to ease administration and minimize the potential for manipulation.

The effects of the proposed regulations on brokers are analyzed, estimating that between 600 to 9,500 brokers will be impacted. The IRS/Treasury report acknowledges that the initial setup costs for brokers will be significant, but the clarity provided by the regulations is expected to mitigate some of these costs over time. The report notes that:

> Additionally, start-up costs are estimated to be between three and eight times annual costs. Given that we expect per firm annual estimated burden hours to be 425 hours and $27,000 of estimated monetized burden, we estimate per firm start-up aggregate burden hours to range from 1,275 to 3,400 hours and $81,000 to $216,000 of aggregate monetized burden. Using the mid-points, start-up total estimated aggregate burden hours is 11,804,375, and the total estimated monetized burden is $749,925,000.

IRS/Treasury Report at 157.

Furthermore, the document estimates that around 13 to 16 million digital asset owners will be impacted by these proposed regulations. It suggests that a considerable number of digital asset owners will experience reduced costs in monitoring and tracking their digital asset portfolios, which might, in turn, increase the number of digital asset owners and possibly ramp up trading volume. However, it also recognizes a subset of digital asset owners who value the pseudonymity provided by blockchain technology. For these individuals, the requirement for brokers to collect information for tax reporting purposes represents an additional privacy cost, which might deter them from trading digital assets through brokers.

Overall, the economic analysis section provides a structured examination of the potential implications, costs, and benefits associated with the proposed regulations on digital assets, offering

a comprehensive framework for understanding the economic impact on various stakeholders within the digital asset ecosystem.

Proposed Reporting and Compliance Requirements

The report further discusses the implications and considerations of the proposed rule regarding the reporting and compliance requirements for digital asset transactions, particularly focusing on brokers and real estate reporting persons. According to the proposed regulations under Section 1.6045-1(d), brokers are generally required to report to the IRS and the customer the gross proceeds from the sale of digital assets on behalf of the customer, and in certain cases, the customer's adjusted basis and the date of purchase of the digital assets sold. This reporting is essential for both the IRS and the customer to ascertain the amount and nature of the customer's gain or loss from such sales.

Moreover, under Section 1.6045-4(i) of the proposed regulations, real estate reporting persons, who are treated as brokers, are required to report the fair market value of digital assets paid as consideration in real estate transactions to the IRS and the real estate transferor. This information aids in determining the total gross proceeds from digital assets in the transaction and helps ascertain whether, and to what extent, the gross proceeds are taxable income to the real estate transferor.

The document elaborates on the estimated burden on brokers and real estate reporting persons in compliance with these proposed regulations. It mentions an average estimated per-customer burden of between 7.5 to 10.5 minutes for brokers, with startup costs ranging between 1,275 and 3,400 hours to build processes complying with the reporting requirements. However, it is anticipated that the revised Form 1099-S for reporting gross proceeds from digital assets in real estate transactions will not significantly alter the overall costs. Small businesses may opt to engage tax reporting services to fulfill the reporting requirements, although the economic efficiency of such an approach remains uncertain.

In considering the impact on small businesses, alternatives to the proposed regulations were examined, including creating an exception to reporting or a delayed applicability date. However, these alternatives were dismissed as they could diminish the effectiveness of the proposed regulations in bridging the overall tax gap, possibly incentivizing taxpayers to shift their business to exempted small businesses, and undermining the IRS's efforts to track digital asset transactions. Besides, small business brokers providing the same level of useful information as larger competitors and aiding in tax return preparation are seen as beneficial aspects.

Lastly, the section confirms that the proposed rule doesn't conflict or overlap with any existing Federal rules and specifically aims to prevent duplicative reporting. It invites comments on the impact of this rule on small entities and mentions that the notice of proposed rulemaking will be submitted to the Chief Counsel for the Office of Advocacy of the Small Business Administration for further comment on its impact on small entities.

Penalties for Failure to Comply with Information Reporting Requirements

According to a guidance report published by the Joint Committee on Taxation:

A person who is required to file information returns but who fails to do so by the due date for the returns includes on the returns incorrect information or files incomplete returns generally is subject to a penalty of $250 for each return with respect to which such a failure occurs, up to a maximum of $3,000,000 in any calendar year, adjusted for inflation. Similar penalties, also with a $3,000,000 calendar-year maximum, apply to failures to furnish correct written statements to recipients of payments for which information reporting is required. Brokers may be subject to such penalties for failure to file the returns required under section 6045 or for failure to provide statements to others as required by section 6045A.

Cash received in trade or business: Section 6050I requires any person engaged in a trade or business to report any transaction (or two or more related transactions) in which the person receives more than $10,000 in cash. For this purpose, cash includes foreign currency and, to the extent provided by the Secretary, any monetary instrument (whether or not in bearer form) with a face amount of not more than $10,000. Returns required under section 6050I parallel reports required from merchants and service providers under the Bank Secrecy Act. Failure to file such returns and failure to provide customers with copies of such returns are subject to the penalties under sections 6721 and 6722, respectively. See https://www.irs.gov/irm/part20/irm_20-001-007r

Criminal penalties: According to Section 80603 of the Jobs Act, individuals who receive digital assets are obligated to report the sender's name, address, and Social Security number within a 15-day period. In addition to the civil penalties noted above, recipients who deliberately ignore this obligation may be subjected to felony charges, a maximum of five years in prison, and potentially higher civil penalties. Corporations that violate this provision could incur fines of up to $100,000 for each transaction.

IRS Comment Period on Proposed Amendments

Before the proposed amendments are finalized, the IRS will consider all timely submitted comments, with a public hearing scheduled on November 7, 2023, at the IRS Auditorium in Washington, DC. A second hearing will be held on November 8 if needed. Participants can attend in person or by phone, following specific instructions for registration and submission of comments. An outline of topics and comments must be submitted 60 days post-publication in the Federal Register. If no outlines are received, the hearing will be canceled. The hearings are accessible for individuals with disabilities, and requests for special assistance should be made by November 2, 2023. IRS documents cited are available online or from the U.S. Government Publishing Office. Multiple personnel from the Treasury Department and the IRS contributed to the drafting of these regulations.

Disclaimer: This guide was prepared for information purposes only. Nothing in this guide should be considered legal, tax, or financial planning advice. Moreover, the information provided in this guide in no way constitutes the creation of an attorney-client relationship. If you have a specific legal or tax question concerning these proposed regulations, you should consult an attorney and/or tax professional who is licensed to practice in your jurisdiction.