

# Dealing with the Section 6045 Proposed Regulations on Broker Reporting + OECD Reporting Guidelines

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## Tax Reporting Issues

- The Code already provides that taxable income (including gains and losses on exchanged crypto) must be reported to the government on your tax return as income.
- Various reporting regimes exist and can be applicable in crypto context:
  - 1099-MISC reporting
  - Section 6045 (Form 1099-DA)
  - 6045A Reporting
  - 6050I (Form 8300)

## What is Section 6045?

Section 6045 creates a broker reporting obligation for digital assets.

- Brokers will be required to collect taxpayer information and report information to the IRS and to taxpayers on certain trades that are effected by brokers on a to-be-drafted Form 1099-DA.

IRS and the Treasury Department issued proposed regulations in August 2023 under section 6045. Just under 45,000 comments were received by IRS in November. Final regulations have not been issued.

## Overview of Section 6045

Defines “**broker**” as “any person who (for consideration) is responsible for and regularly provides any service effectuating transfers of digital assets on behalf of another person.”

Defines “**digital assets**” broadly as “any digital representation of value which is recorded on a cryptographically secured distributed ledger or any similar technology as specified by the Secretary.”

- Regulations expand this definition: “any digital representation of value that is recorded on a cryptographically secured distributed ledger (or any similar technology), without regard to whether each individual transaction involving that digital asset is actually recorded on that ledger, and that is not cash.” Reg. § 1.6041-19(a)(19).

Proposed regs: <https://www.govinfo.gov/content/pkg/FR-2023-08-29/pdf/2023-17565.pdf>

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## Overview of Section 6045 – Proposed Regs

- Generally effective for transactions or sales/exchanges effected after 1/1/2025.
- The proposed regulations state that a person can effect the transaction (and thus be a broker) if such person “knows or is in a position to know the identity of the party that makes the sale and the nature of the transaction potentially giving rise to gross proceeds from the sale.”
  - This “in a position to know” standard represents a departure from the usual “knows or has reason to know” standard used in other parts of the Code and regulations relating to reporting.
  - The Preamble provides that: “The ability to modify the operation of a platform to obtain customer information is treated as being in a position to know that information.”

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## Industry Perspective on Broker Reporting

- Proposed Regs would create enormous compliance costs and compliance burdens for centralized exchanges.
- Centralized exchanges (and other taxpayers) requested a longer transitional period to enable taxpayers to prepare for and to adapt to being reporting entities for the industry.
- Many industry participants requested clarity on the scope of the rules and the application of the broker rules to other members of the blockchain industry.

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## Practitioner/Taxpayer Perspective on § 6045

- Practitioners/Taxpayer impact: 1099-DAs with data gaps caused by **transfers**.
- Transfer are very common in the crypto space compared to stocks/TradFi.
  - Blockchain technology enables seamless asset transfers with just a click of a button without any friction.
  - No single exchange can offer access to all cryptocurrency trading pairs in existence at a given time.
  - Privacy and security reasons.

Tax year	Avg. number of transfers per CoinTracker user
2020	10.48
2021	25.16
2022	15.24
2023	6.74

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## Practitioner/Taxpayer Perspective on § 6045

- **Example**
  - Shehan transfers 1 ETH from an unhosted wallet to Coinbase and sells 0.8 ETH for \$2,000. Shehan will get a 1099-DA with missing cost basis.
  - Shehan then transfers 0.2 ETH from Coinbase to Gemini and sells it for \$500. Shehan will again get a 1099-DA with missing cost basis. (§6045A/transfer statements will not fix the gaps)
- **Key point:** Frequent transfers will generate an unprecedented amount of non-covered tax lots in the system compared to traditional securities.
- **Opportunity**
  - Aggregation software maintain non-covered lots. There's an opportunity for brokers to leverage this data in information reporting and in Tax centers.
  - The IRS has an opportunity to leverage this data with user consent.

## Comparing and Contrasting CARF and Broker Reporting

- CARF has four key components:
  - (1) What assets are covered under CARF
  - (2) What service providers are covered under CARF
  - (3) What level of diligence does CARF require
  - (4) What reporting does CARF require
- Thoughts on U.S. implementation of CARF rules
- Comparing the CARF Framework to the 6045 Framework
  - CARF is a governmental reporting regime (rather than a taxpayer reporting tool)

## Applying Broker Reporting Rules to NFTs

Non-fungible tokens (NFTs) present a particular challenge in the context of broker reporting rules

- Application of CARF and section 6045 broker reporting rules apply to non-financial assets
- Application to NFTs specifically
  - NFTs could include an array of things (images, sports tickets, hotel rooms, physical art ownership, etc.)
- Practical challenges for imposing broker rules to unique assets

## Open Questions for Broker Reporting

- Scope of the regulations
  - Who should constitute a broker? Are the regulations too broad?
  - Application of the regulations to stablecoins
  - Application of regulations to tokenized securities (where existing reporting rules already apply)
  - Application of the regulations to DeFi
- How are transactions actually occurring – and are these types of transactions properly accounted for in the broker reporting rules?

## Section 6050I Reporting

- Part of the Infrastructure Investment and Jobs Act, passed into law in 2021.
- Section 6050I now includes “digital assets” within the scope of the cash reporting rules, requiring that any transaction (or series of transactions) over \$10,000 received in the course of a trade or business be reported.
  - Could be millions of forms that are required to be filed annually.
- Taxpayers have already raised privacy challenges – DOJ has argued in Sixth Circuit briefing that the statute is not self-effecting without regulations.
- IRS Announcement 2024-4 indicates that the IRS intends to implement the changes through regulations which have not yet been proposed, and that digital assets need not be included as cash for purposes of section 6050I.