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Tax Reporting as Regulation of Digital Financial Markets

Young Ran (Christine) Kim*

Abstract

FTX's recent collapse highlights the overall instability that blockchain assets and digital financial markets face. While the use of blockchain technology and crypto assets is widely prevalent, the associated market is still largely unregulated, and the future of digital asset regulation is also unclear. The lack of clarity and regulation has led to public distrust and has called for more dedicated regulation of digital assets. Among those regulatory efforts, tax policy plays an important role. This Essay introduces comprehensive regulatory frameworks for blockchain-based assets that have been introduced globally and domestically, and it shows that tax reporting is the key element of those regulatory frameworks.

Furthermore, this Essay argues that tax reporting and transparency requirements can significantly stabilize the digital financial market and provide additional funding for much-needed regulatory programs through increased tax compliance. Tax reporting requirements have been effective tools in traditional financial markets. By replicating such policies in the digital financial market, the market would significantly improve. These requirements would help combat money laundering and tax evasion. Also, reporting requirements that target both financial institutions and taxpayers would increase tax compliance and lower administrative burdens. The

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requirements also have the potential to generate revenue, which can fund additional regulatory developments. For these reasons, tax reporting requirements could be an important tool whose utilization would bring much needed stability to digital assets and the market.

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INTRODUCTION

Enforcing information reporting and transparency requirements in the digital financial market via tax policy can be an effective regulatory tool to combat the market's current instability and provide funding for additional regulations. Much of my recent work focuses on the intersection between tax and new technology, including the taxation of the platform

economy,¹ the taxation of the Metaverse,² and the potential application of blockchain technology in tax administration.³ Given the prevalent use of blockchain assets in the largely unregulated digital financial market, it only made sense that I now address traditional tax reporting requirements as a regulatory method.

Blockchain assets, or Digital Ledger Technology-based (“DLT-based”) assets, are relatively recent innovations that have quickly garnered substantial attention from the public.⁴ Popular examples include cryptocurrencies such as Bitcoin and Ether,⁵ or non-fungible token (“NFT”) collections such as CryptoPunks or the Bored Ape Yacht Club.⁶ The initial purpose of the digital ledger technology underlying all blockchain assets is to record and manage data.⁷ The value of such an application is evident and frequently discussed in situations like keeping personal records, tracking ownership of property, managing supply chains, or government compliance and reporting.⁸

1. See generally Young Ran (Christine) Kim & Darien Shanske, *State Digital Services Taxes: A Good and Permissible Idea (Despite What You Might Have Heard)*, 98 NOTRE DAME L. REV. 741 (2022).

2. See generally Young Ran (Christine) Kim, *Taxing the Metaverse*, 112 GEO. L.J. (forthcoming 2024).

3. See generally Young Ran (Christine) Kim, *Blockchain Initiatives for Tax Administration*, 69 UCLA L. REV. 240 (2022).

4. See Susannah Hammond & Todd Ehret, *Special Report: Cryptos on the Rise 2022*, THOMSON REUTERS, <https://perma.cc/3J TZ-K9 TC> (last visited June 25, 2023) (“Crypto-assets and the vast universe of associated products and services have grown rapidly in recent years and are becoming increasingly interlinked with the regulated financial system.”).

5. See Kat Tretina, *Top 10 Cryptocurrencies Of 2023*, FORBES ADVISOR, <https://perma.cc/NH2S-6YPB> (last updated May 23, 2023, 11:57 AM) (listing Bitcoin and Ether as the top two cryptocurrencies of 2023).

6. See Andrew Hayward, *The Biggest NFT Collections of 2022*, DECRYPT (Dec. 21, 2022), <https://perma.cc/G8HU-E4AW> (listing CryptoPunks and the Bored Ape Yacht Club as the seventh and first biggest NFT collections respectively).

7. See David Rodeck & Benjamin Curry, *Understanding Blockchain Technology*, FORBES ADVISOR (May 23, 2023, 4:46 PM), <https://perma.cc/R4BB-5HYA> (“At its core, blockchain is a distributed digital ledger that stores data of any kind. A blockchain can record information about cryptocurrency transactions, NFT ownership or DeFi smart contracts.”).

8. See Adam Levy, *15 Applications for Blockchain Technology*, THE MOTLEY FOOL (July 13, 2022, 10:13 AM), <https://perma.cc/9SJS-H8ZF> (listing

However, the current application of DLT-based assets in the e-commerce, banking, financial services, and currency sectors is more akin to a consumer good or speculative asset⁹ and thus makes up the digital financial market.¹⁰

Unfortunately, much of the recent attention on the digital financial market is negative. Many investors view blockchain assets and the associated markets as overly risky and unstable.¹¹ The resulting “crypto winter” is characterized by a drop in prices and market capitalization.¹² The recent collapse of FTX is illustrative of the overall poor state of the market. Before November 2022, FTX seemed to be doing quite well in an unfriendly marketplace.¹³ It was the fourth-largest crypto exchange in the world, valued at \$32 billion,¹⁴ high-profile celebrities, such as Larry David and Tom Brady, were

secure storage of personal information, voting, logistics and supply chain tracking, or gambling as other applications of blockchain technology).

9. See Peyman Pardis, *NFTs—Just a Speculative Asset? Think Again*, LINKEDIN (Jan. 19, 2022), <https://perma.cc/HU9P-9K55> (observing that NFTs are examples of “speculative asset[s]” that are valued “based on the belief that somebody will want it more in the future”).

10. See *What Is Digital Finance?*, EUROPEAN COMM’N, <https://perma.cc/4RHZ-7KDC> (last visited June 25, 2023) (describing digital finance in terms of the “variety of products, applications, processes and business models” it facilitates).

11. See Simon Chandler, *How to Invest in Blockchain, the High-Risk but High-Potential Technology Behind Bitcoin and Other Digital Transactions*, PERS. FIN., <https://perma.cc/5YHW-W9X4> (last updated July 29, 2022, 2:26 PM) (“[B]lockchain stocks represent a high-growth sector that exposes investors to plenty of risk.”); Naveen Joshi, *7 Risks Investors Need to Know Before Jumping Headfirst into the NFT Bandwagon*, FORBES (Apr. 24, 2022, 8:30 PM), <https://perma.cc/7SD6-SYGM> (listing potential risks involved in purchasing NFTs); Maurie Backman, *Why Is Crypto Riskier Than Stocks?*, THE ASCENT (Oct. 12, 2021), <https://perma.cc/KKZ8-3SM9> (“Even stocks aren’t as risky as an investment that’s grown increasingly popular this past year—cryptocurrency.”).

12. See Joanna England, *What Is a Crypto Winter and Are We Still Experiencing One?*, FINTECH (Jan. 30, 2023), <https://perma.cc/XS9X-8AL6> (“‘Crypto winter’ refers to a prolonged bear market in the cryptocurrency industry . . . It is a period during which investor sentiment towards the cryptocurrency market is negative, and few people are interested in buying digital currencies.”).

13. See *infra* notes 14–15 and accompanying text.

14. Farran Powell, *FTX Declares Bankruptcy*, FORBES ADVISOR, <https://perma.cc/HST6-Z2TQ> (last updated Dec. 13, 2022, 9:49 AM).

promoting it,¹⁵ and it had a liquidity provider that frequently acted as a lender of last resort to other struggling Crypto companies.¹⁶ The rapid downfall of FTX was the result of a liquidity run on FTX's native coin after a single article raised concerns about the exchange's solvency,¹⁷ thus exemplifying the general distrust in the digital financial market.¹⁸ In only a few short days, FTX had filed for bankruptcy, lost over \$1 billion in customer funds, and was under investigation for potential criminal and security violations.¹⁹ The sketchy actions of FTX management only further reinforce the air of distrust.²⁰

15. See Minyvonne Burke, *Tom Brady, Larry David and Other Celebrities Named in FTX Lawsuit*, NBC NEWS (Nov. 16, 2022, 12:04 PM), <https://perma.cc/4N68-QGQK>.

16. See Powell, *supra* note 14 (“Bankman-Fried’s Alameda [Research] stepped in as a lender of last resort to crypto firms such as Voyager Digital and Celsius, went down the drain[,] and threatened to take huge parts of the crypto market along with them.”).

17. See Phil Rosen, *The Lehman Brothers of Crypto: Here’s How the Fall of Sam Bankman-Fried’s FTX Compares to the Collapse that Sparked the Great Financial Crisis*, INSIDER (Nov. 14, 2022, 6:05 AM), <https://perma.cc/5S28-EAA5> (describing how the FTX empire collapsed after the value of its native FTT token “saw its value virtually hit zero overnight,” resulting in a domino effect leading to the company’s eventual bankruptcy); Powell, *supra* note 14 (describing how the downfall of FTX began with an article questioning its FTT token’s solvency); see also Ian Allison, *Divisions in Sam Bankman-Fried’s Crypto Empire Blur on His Trading Titan Alameda’s Balance Sheet*, COINDESK (Nov. 2, 2022, 10:44 AM), <https://perma.cc/J5WJ-4PXW> (last updated May 9, 2023, 12:01 AM) (describing the murky association between Alameda Research and FTX).

18. Cf. *supra* notes 11–12 and accompanying text.

19. See Powell, *supra* note 14 (“Within only a few days, the multibillion-dollar crypto exchange went from crypto leader to bankrupt.”); Angus Berwick, *At Least \$1 Billion of Client Funds Missing at Failed Crypto Firm FTX*, REUTERS (Nov. 13, 2022, 5:00 PM), <https://perma.cc/T3WX-6TMP> (“Spreadsheets indicated between \$1 billion and \$2 billion in client money is unaccounted for.”).

20. See, e.g., Berwick, *supra* note 19 (describing how Bankman-Fried secretly transferred billions in customer funds to his trading company before losing a large portion of customer funds); see also Powell, *supra* note 14 (listing the myriad of ways FTX associates were suspected of fraudulent behaviors, such as an SEC complaint claiming that Bankman-Fried defrauded FTX customers and investors, and a statement from the Bahamian prime minister stating that individuals associated with FTX “may have betrayed public trust and broken the law”).

The aftermath of FTX and the ongoing “crypto winter” has many calling for more regulation in the digital financial market.²¹ Currently, the United States lacks a dedicated regulatory framework for the digital financial market.²² Although various types of blockchain assets fall under the legal jurisdiction of agencies like the Securities and Exchange Commission (“SEC”) or the Commodities Futures Trading Commission (“CFTC”), the application and enforcement of these laws are irregular.²³ The practical result is that a large portion of the digital financial market is unregulated.²⁴ The future of digital asset regulation is similarly unclear, although there have been some efforts towards implementing a more dedicated regulatory framework.²⁵

Amidst the chaos that is the present and future regulation of blockchain assets, one rarely hears calls for tax policy as a regulatory method. This Essay proposes that, although agencies like the SEC and CFTC will likely play a crucial role,²⁶ using tax policy to enforce information reporting and transparency requirements will most effectively regulate and stabilize the digital financial market while providing additional funding for worthwhile efforts.²⁷

21. See Hammond & Ehret, *supra* note 4 (discussing rising national and international efforts to regulate cryptocurrencies in response to growing concerns of instability and potential for risk); see also Kathryn White et al., *Cryptocurrency Regulation: Where Are We Now, and Where Are We Going?*, WORLD ECON. F. (Mar. 28, 2022), <https://perma.cc/XHM2-6VAJ> (outlining efforts of banks and regulators across the world to regulate cryptocurrencies in order to stabilize monetary systems and improve economic growth).

22. Cf. White et al., *supra* note 21 (pointing to the Biden Administration’s “long-awaited Executive Order” as the United States’ first foray into digital finance regulation).

23. See Cheryl L. Isaac et al., *CFTC and SEC Perspectives on Cryptocurrency and Digital Assets—Volume I: A Jurisdictional Overview*, K&L GATES (May 6, 2022), <https://perma.cc/9ZYD-3XV4> (examining various enforcement actions by the CFTC and SEC against cryptocurrency companies with disparate results).

24. See Hammond & Ehret, *supra* note 4 (“Policymakers appear to be struggling to keep track of risks posed by a sector where most activities are unregulated, or at best lightly regulated.”).

25. See Responsible Financial Innovation Act, S. 4356, 117th Cong. (2022) (“To provide for responsible financial innovation and to bring digital assets within the regulatory perimeter.”).

26. See *infra* Section II.B.

27. See *infra* Part III.

Part I discusses the ways in which tax reporting requirements have proven to be an effective regulatory tool in traditional financial markets with similar challenges.²⁸ Part II discusses how, having recognized tax reporting's effectiveness and the unique tax challenges accompanying blockchain assets, multiple regulators, both domestic and foreign, are looking to implement comprehensive digital asset frameworks wherein *tax* reporting and transparency requirements are critical.²⁹ Finally, Part III posits that tax reporting requirements are particularly beneficial in the digital financial market because these policies successfully combat parallel challenges in the traditional financial market, such as money laundering and various forms of tax evasion.³⁰ Moreover, it targets taxpayers and financial intermediaries, resulting in higher tax compliance and a lower administrative burden, two problems that are rampant in the digital financial market.³¹ Finally, such a policy has the potential to significantly boost tax revenue and fund additional regulations in the market.³²

I. TAX REPORTING IN TRADITIONAL FINANCIAL MARKETS

Tax reporting and transparency requirements have proven to be efficient regulatory tools in traditional financial markets. A good example is tax reporting's success in combatting money laundering and various forms of tax evasion.

Money laundering, or the process of disguising criminal proceeds through various schemes, is an inevitable result of profitable activity³³ and has a host of negative consequences. Perhaps the most apparent impact is promoting criminal activity, inside and outside the market, by effectively allowing

28. *See infra* Part I.

29. *See infra* Part II.B–C.

30. *See infra* Section III.

31. *See infra* Section III.B.

32. *See infra* Section III.C.

33. *Cf.* IRM 9.5.5.1 (Feb. 15, 2008) (“Money laundering is a necessary consequence of almost all profit generating crimes and can occur almost anywhere in the world.”).

criminals to deploy illegal funds.³⁴ It also distorts financial markets by creating an unstable demand for money, turning “once-productive businesses into sterile ones,” and harming the reputation of financial intermediaries.³⁵ Finally, money laundering results in a significant loss of government revenue, diminished government control over the economy, and undermined public confidence.³⁶

The United States National Money Laundering Strategy, in which the Treasury Department and the Internal Revenue Service (“IRS”) play a significant role, effectively combats these negative impacts through various statutes.³⁷ Consider the Anti-Money Laundering Act of 2020³⁸ (“AML”), which “represents the most significant change to the American bank secrecy, and anti-money laundering/counter-terrorist financing (‘AML’/‘CFT’) regime since the USA PATRIOT Act of 2001.”³⁹ The AMLA solidifies the United States Department of the Treasury Financial Crimes Enforcement Network (“FinCEN”)

34. See Ansia Storm, *Establishing the Link Between Money Laundering and Tax Evasion*, 12 INT’L BUS. & ECON. RES. J. 1437, 1441 (2013) (“[Money laundering] promotes crime because it enables criminals to use and deploy illegal funds effectively.”).

35. *The Economic Consequences of Money Laundering*, Q5ID (Aug. 15, 2022), <https://perma.cc/LVR6-8HMY>; see also John McDowell & Gary Novis, *Consequences of Money Laundering and Financial Crime*, 6 ECON. PERSP. 6 (2001) (examining the economic and social effects of money laundering).

36. See *The Economic Consequences of Money Laundering*, *supra* note 35 (listing “loss of government revenue” as a consequence of money laundering); Storm, *supra* note 34, at 1441 (“[Money laundering’s] most important consequence is that [it] reduces revenue and control by weakening government control over the economy, causing ‘injury’ to the public.”); see also IRM 9.5.5.1 (Feb. 15, 2008) (explaining that money laundering “erodes public confidence in the tax system.”).

37. See IRM 9.5.5.1 (Feb. 15, 2008) (“The National Money Laundering Strategy, established by the Secretary of the Treasury and the Attorney General, describes the goals, objectives and priorities for combating money laundering, terrorism and related financial crimes.”); see also *Bank Secrecy Act*, INTERNAL REVENUE SERV., <https://perma.cc/G5CX-HUDN> (last updated Apr. 12, 2023) [hereinafter BSA IRS] (“The Internal Revenue Service is a partner in the U.S. National Money Laundering Strategy.”).

38. Pub. L. No. 116-283, §§ 6001–6511, 134 Stat. 3388, 3415–16 (2021) (codified as part of National Defense Authorization Act of 2021 in scattered sections of 12 and 31 U.S.C.).

39. Jules W. Carter, *Fact Sheet: AML Act of 2020*, WESTLAW TODAY (Apr. 7, 2021), <https://perma.cc/C9A8-PU5P>.

“as the center of financial intelligence in the United States.”⁴⁰ Its primary purpose is to “improve cooperation, coordination, and information-sharing among regulators, financial institutions, law enforcement and intelligence agencies.”⁴¹ One of the ways it does this is by “requiring certain companies doing business in the U.S. to disclose the identities of their beneficial owners” to discourage money laundering through shell corporations.⁴² This provision, in particular, “has garnered the most attention,” presumably because it is likely to have “far-reaching consequences.”⁴³

Another important statute is the Bank Secrecy Act⁴⁴ (“BSA”) and its various expansions. Under the BSA, businesses must file a Form 8300 with the IRS upon receiving more than \$10,000 in cash from a single buyer in a single transaction or two or more related transactions.⁴⁵ Moreover, the IRS has the ability to identify money laundering violations within their jurisdiction by observing “tax and information returns and other tax information secured from IRS sources/files or developed by the IRS in determining a person’s tax liability.”⁴⁶ After the 2008 financial crisis, the United States expanded the BSA to require a Report of Foreign Bank and Financial Accounts (“FBAR”).⁴⁷ To comply with the FBAR, U.S. taxpayers must keep certain records and annually report to the IRS any “foreign bank account, brokerage account, mutual fund, unit trust, or other financial account.”⁴⁸ Failure to comply with FBAR reporting

40. *Id.*

41. *Id.*

42. *Id.*

43. *Id.*

44. Pub. L. No. 91-508, 84 Stat. 1114 (1970) (codified as amended in scattered sections of 12 and 31 U.S.C.).

45. BSA IRS, *supra* note 37; *see also* IRM 9.5.5.3.6.2 (Aug. 27, 2007) (listing Form 8300 filing requirements).

46. IRM 9.5.5.4.4(1)–(2) (Aug. 27, 2007).

47. *See Report of Foreign Bank and Financial Accounts (FBAR)*, INTERNAL REVENUE SERV. [hereinafter FBAR IRS], <https://perma.cc/XM5Q-2FW8> (last updated July 12, 2022) (“Per the Bank Secrecy Act, every year you must report certain foreign financial accounts . . . by filing a Report of Foreign Bank and Financial Accounts (FBAR) . . .”).

48. BSA IRS, *supra* note 37; *see also* IRM 9.5.5.3.3.1.3(1) (Aug. 27, 2007) (“[E]ach United States person who has a financial interest in, or signature

requirements results in a penalty, which will be discussed later on in this Essay.⁴⁹

Also consider the Foreign Account Tax Compliance Act⁵⁰ (“FATCA”) in conjunction with the Swiss Bank Program and various Intergovernmental Agreements (“IGAs”). Like FBAR, FATCA requires United States persons, including individuals, companies, and trusts, to report their financial accounts outside the United States to the Treasury Department and the IRS.⁵¹ To promote global compliance with FATCA, the United States signed Intergovernmental Agreements with foreign countries, including Switzerland.⁵² Under the IGA with Switzerland, Swiss financial institutions must automatically report to the Swiss Federal Tax Administration (“FTA”) any accounts held by U.S. taxpayers.⁵³ In return, the Swiss FTA will pass this

authority over, any financial accounts in a foreign country including bank, securities or other types of accounts, must report that relationship by filing an FBAR . . .”).

49. See *infra* Part III.C.

50. 26 U.S.C. §§ 1471–74.

51. Compare *Summary of Key FATCA Provisions*, INTERNAL REVENUE SERV., <https://perma.cc/Z8T4-QGD2> (last updated Nov. 9, 2022) [hereinafter FATCA IRS] (requiring U.S. taxpayers, foreign entities in which U.S. taxpayers hold a substantial interest, and foreign financial institutions to report certain information directly to the IRS), with FBAR IRS, *supra* note 47 (requiring U.S. citizens, residents, corporations, partnerships, limited liability companies, trusts, and estates to file an FBAR when holding certain foreign accounts).

52. See *FACTA Information for Governments*, INTERNAL REVENUE SERV. (Feb. 8, 2023), <https://perma.cc/R3WZ-79SB> (discussing general use of IGAs with foreign countries to implement FACTA); see also *Justice Department Reaches Final Resolutions Under Swiss Bank Program*, DEP’T OF JUST. (Dec. 29, 2016), <https://perma.cc/65UB-RREB> (announcing a cooperative agreement between the Department of Justice, the Swiss government, and certain Swiss banks); Marnin J. Michaels et al., *The DOJ’s Swiss Bank Program: Lessons Learned and the Road Ahead*, THOMSON REUTERS (Aug. 2016), <https://perma.cc/L8YB-ZYKM> (detailing the compliance requirements of the DOJ’s Swiss Bank Program agreement).

53. See *Switzerland: Issued FACTA Notifications*, KPMG (Mar. 26, 2021), <https://perma.cc/D5PP-FXUV> (summarizing the key features of the FATCA agreement between the United States IRS and twenty-nine Swiss financial institutions). *But see* Michaels et al., *supra* note 52 (discussing challenges to robust implementation of the older Swiss Bank Program under the Swiss Federal Data Privacy Act).

information to the IRS.⁵⁴ The result was essentially the end of Swiss bank secrecy.⁵⁵

In short, the reporting requirements under the AMLA, BSA, FBAR, and FATCA effectively combat offshore tax evasion and money laundering, and these provisions greatly enhance global transparency in the traditional financial market.⁵⁶ In addition, they are notable examples of using tax policy to regulate the financial market. First, the reporting requirements are imposed not only on taxpayers/customers but also on financial intermediaries.⁵⁷ Second, tax policymakers improved the existing system for exchanging tax information by developing common reporting standards and making the automatic exchange among countries a new status quo.⁵⁸ As a result, the tax reporting policy greatly enhances global transparency in the traditional financial market.

54. See *Switzerland: Issued FACTA Notifications*, *supra* note 53 (noting the Swiss FTA would make reports to the IRS per the FATCA Agreement between the two countries); Michael Shields, *Era of Bank Secrecy Ends as Swiss Start Sharing Account Data*, REUTERS (Oct. 5, 2018, 6:03 AM), <https://perma.cc/W4MJ-KPMA> (reporting the first automatic exchange of financial account data from Switzerland to partner states).

55. See Shields, *supra* note 54 (noting how the automatic exchange of financial account information from Switzerland to eighty partner States follows a years-long trend of weakening Swiss banking secrecy laws).

56. See *id.* (noting that Switzerland adopted Organisation for Economic Co-operation and Development global standards designed to enhance tax transparency and discourage “tax cheats”); see also Omri Marian, *Blockchain Havens and the Need for Their Internationally-Coordinated Regulation*, 20 N.C. J.L. & TECH. 529, 532, 545–46 (2019) (describing the success of developed economies in enacting laws and international agreements to combat tax havens).

57. See, e.g., FATCA IRS, *supra* note 51 (requiring FATCA reporting directly to the IRS by financial intermediaries).

58. See Young Ran (Christine) Kim, *Engineering Pass-Throughs in International Tax: The Case of Private Equity Funds*, 56 SAN DIEGO L. REV. 707, 763–69 (2019) (positing that the 2007 global financial crisis was the catalyst for a more transparent international tax information regime); Young Ran (Christine) Kim, *Considering “Citizenship Taxation”*: In Defense of FATCA, 20 FLA. TAX REV. 335, 359–62 (2017) (discussing the policies and conditions that resulted in the change from an upon request tax information sharing status quo to an automatic tax information sharing status quo).

II. FUTURE FRAMEWORKS IN DIGITAL FINANCIAL MARKETS

Built upon the tax reporting framework developed for traditional financial markets, a host of regulatory bodies are turning to comprehensive frameworks to regulate the digital finance sphere.⁵⁹ Such an approach is not surprising given the success of regulatory tax reporting, such as FBAR and FATCA, in the past. This Part will briefly introduce and explain proposed frameworks from the Organisation for Economic Co-operation and Development (“OECD”), the United States, and the European Union.⁶⁰

A. OECD Framework: CARF

The OECD recently developed the Crypto-Asset Reporting Framework (“CARF”) to combat the unique risks that Crypto-Assets pose to global tax transparency.⁶¹ Namely, Crypto-Assets are transferred and held without going through traditional financial intermediaries, making it difficult for tax administrations to verify whether taxes are appropriately reported and assessed.⁶² CARF attempts to resolve this issue by ensuring an annual standardized and automatic exchange of tax information for Crypto-Asset transactions with the taxpayers’ resident jurisdiction.⁶³ The OECD has already published the reporting rules (and commentary) and will release the framework for how this information is to be exchanged sometime in 2023.⁶⁴

59. See *infra* Part II.A–D.

60. See *infra* Part II.A–D.

61. See OECD, CRYPTO-ASSET REPORTING FRAMEWORK AND AMENDMENTS TO THE COMMON REPORTING STANDARD 9–10 (2022), <https://perma.cc/WG4W-3P9B> (PDF) (advancing CARF in response to the “novel challenges” posed by Crypto-Assets).

62. See *id.* at 9 (noting that Crypto-Assets use largely new, non-traditional financial intermediaries that are subject to limited regulatory oversight and limited tax reporting requirements).

63. *Id.* at 6.

64. See Talking Tax, *Global Crypto Tax Standards near with G20 Support*, BLOOMBERG TAX, at 02:30 (Nov. 17, 2022), <https://perma.cc/F7KF-9QVH> (interviewing Artur Olszewski on the publication timeline of the CARP framework). For a critical perspective on CARF, see Noam Noked, Presentation at the 5th Annual UCI Law—Taylor Nelson Amitrano LLP Tax

CARF applies to all Crypto-Assets held or transferred via a secured distributed ledger or similar technology (i.e., a blockchain).⁶⁵ However, there are three exclusions that do not pose the same tax risks: (1) any Crypto-Asset that cannot be used for payment or investment purposes;⁶⁶ (2) Central Bank Digital Currencies that function similarly to money held in a traditional bank;⁶⁷ and (3) “Specified Electronic Money Products that represent a single Fiat Currency and are redeemable at any time in the same Fiat Currency at par value.”⁶⁸ On the other hand, CARF has identified three types of Crypto-Asset transactions subject to the reporting requirements, namely: (1) exchanges between Crypto-Assets and Fiat Currencies; (2) exchanges between Crypto-Assets and other Crypto-Assets; and (3) the transfer of a Crypto-Asset.⁶⁹

Reporting Crypto-Asset Service Providers (“Service Providers”) are subject to the reporting rules and due diligence requirements under the CARF because they are in the best position to have all the necessary information.⁷⁰ An entity or individual qualifies as a Service Provider if they provide services facilitating exchanges in Crypto-Assets for, or on behalf of, customers—which includes not only traditional exchanges, but also brokers, dealers, and operators of Crypto-Asset ATMs.⁷¹ Service Providers are subject to the rules when they are (1) a tax resident in, (2) a legal personality and are incorporated in or organized under the laws of, (3) subject to tax reporting requirements in, (4) managed from, (5) having a regular place of business in, or (6) facilitating relevant Crypto-Asset

Symposium: Tax Transparency for Crypto Assets (Apr. 17, 2023) (on file with author).

65. See OECD, *supra* note 61, at 11 (defining the scope of Crypto-Assets to be covered by CARF).

66. *Id.*

67. *Id.*

68. *Id.*

69. See *id.* at 12 (listing these three types of Crypto-Asset transactions as “[r]elevant [t]ransactions that are reportable under the CARF”).

70. See *id.* at 11 (“Such . . . service providers are expected to have the best and most comprehensive access to the value of the Relevant Crypto-Assets and the Exchange Transactions carried out.”).

71. See *id.* at 11–12 (explaining the scope of intermediaries and other service providers).

transactions from a branch based in, a jurisdiction that adopts the rules.⁷²

Service Providers are subject to annual reporting requirements wherein they must report their name, address, and identifying number, as well as the name(s), address(es), jurisdiction(s) of residence, Tax ID Number(s) (“TIN”), and date/place of birth for each reportable individual user.⁷³ If the user is an entity, it must report the same for each controlling person that qualifies as a reportable user and their role in the entity.⁷⁴ The Service Providers must report the aggregate amount, the number of units, and the number of transactions for each transaction by type (e.g., Crypto-to-Currency exchanges, Crypto-to-Crypto exchanges, and Transfers) and separated into inward and outward transactions (e.g., bought and sold).⁷⁵ Any Transfers must also be separated into sub-categories if possible (e.g., airdrops).⁷⁶ The amount for each transaction is measured in fiat currency.⁷⁷ For Crypto-to-Crypto transactions or Crypto transfers, the reportable amount is equal to the asset’s fair market value at the time it was disposed of or acquired.⁷⁸ If a Service Provider processes a payment for a merchant accepting Crypto-Assets as payment for goods or services, the Service Provider must also treat the merchant’s customer as a user subject to all the reporting requirements.⁷⁹ Additionally, a Service Provider must report the number of units

72. *Id.* at 12.

73. *See id.* at 14–15 (detailing reporting requirements for qualifying “Service Provider[s]”).

74. *See id.* at 15 (detailing requirements “in the case of any Entity that . . . is identified as having one or more [c]ontrolling [p]ersons that is a [r]eportable [p]erson”).

75. *See id.* at 12, 15 (defining these transactions as “Relevant Transactions” that must be reported under CARF and specifying the requirements).

76. *See id.* at 12 (“Reporting Crypto-Asset Service Providers will also categorise Transfers by Transfer type (e.g., airdrops, income derived from staking, or a loan), in instances where they have such knowledge.”).

77. *See id.* at 12, 15 (requiring measurement in fiat currency for both Crypto-Asset-to-Crypto-Asset and Crypto-Asset-to-Fiat Currency transactions).

78. *See id.* at 12, 15–16 (defining reportable amount as the gross proceeds or acquisition value based on the fair market value at the time of disposal or acquisition of the Crypto-Asset).

79. *Id.* at 12–13.

and the total value of Transfers facilitated by the Service Provider on behalf of users to wallets not associated with a virtual asset service provider.⁸⁰

Service Providers are also subject to due diligence procedures.⁸¹ These procedures require Service Providers to identify whether each user is reportable and adjust if circumstances change.⁸² Such procedures typically require a self-certification with the user's information, including names, addresses, jurisdictions, TINs, date of birth, and any controlling persons (if an entity).⁸³ All documentation must be held for at least five years.⁸⁴ The Service Provider can hire a third party to satisfy these requirements but ultimately remains liable for any mistakes.⁸⁵

B. U.S. Framework: IIJA

The United States has also taken steps to develop and implement a comprehensive framework of tax reporting for the digital financial market.

In the past, the IRS issued ad hoc guidance on cryptocurrency reporting imposed on *taxpayers* only. For example, in 2014, the IRS clarified that taxpayers must report any gain or loss from the sale of cryptocurrency with the basis equaling the fair market value of the cryptocurrency upon receipt.⁸⁶ The notice also explained that taxpayers must report the fair market value (upon receipt) of any cryptocurrency received as payment for goods or services as gross income, including mining efforts.⁸⁷ In 2018, the IRS further advised that hard forks in cryptocurrency would not result in gross

80. *Id.* at 12.

81. *See id.* at 14 (providing four conditions that could subject Service Providers to due diligence procedures).

82. *See id.* at 16–17 (establishing procedures for determining whether an individual or entity is a “Reportable User”).

83. *See id.* (listing self-certification requirements for both individuals and entities).

84. *Id.* at 18.

85. *Id.*

86. I.R.S. Notice 2014-21, 2014-16 I.R.B. 938.

87. *Id.*

income if the taxpayer did not receive any new cryptocurrency units.⁸⁸ Later, in 2020, the IRS amended Form 1040 to ask taxpayers whether, at any time during 2020, the taxpayer received, sold, sent, exchanged, or otherwise acquired any financial interest in any virtual currency.⁸⁹

Despite these efforts, studies showed that U.S. taxpayers still were not paying appropriate taxes on cryptocurrency transactions.⁹⁰ In response, the Infrastructure Investment and Jobs Act⁹¹ (“IIJA”) was signed into law in 2021, containing new tax reporting requirements for *digital-asset brokers or intermediaries* to bring greater “transparency to the market while also giving taxpayers greater certainty as to their taxable gains and losses related to the transaction of digital assets.”⁹² The Act defines digital assets as “any digital representation of value recorded on a cryptographically secured distributed ledger or any similar technology.”⁹³ It also defines digital-asset brokers as “any person who (for consideration) is responsible for regularly providing any service effectuating transfers of digital assets on behalf of another person.”⁹⁴ Some believe that the definition of digital-asset brokers is too broad and will hinder innovation by including miners, validators, and software developers.⁹⁵

Starting in 2023, the IIJA requires that digital-asset brokers report to the IRS and investors all transactions

88. See Rev. Rul. 2019-24, 2019-44 I.R.B. 1004 (mapping the different situations when an individual in possession of cryptocurrency is taxed based on their accession to wealth and gross income).

89. *Frequently Asked Questions on Virtual Currency Transactions*, INTERNAL REVENUE SERV., <https://perma.cc/EPD4-D43D> (last updated May 2, 2023).

90. See Adam Goldberg et al., *What the US Infrastructure Bill Means for Cryptocurrency Brokers and Owners: Part II*, S&P GLOB. MARKET INTEL. (Dec. 20, 2021), <https://perma.cc/F679-TU4W> (noting that taxpayers have underpaid because the “IRS has historically treated cryptocurrency and other digital assets as property, applying general property-tax-transaction principle”).

91. Pub. L. No. 117-58, 135 Stat. 429.

92. Goldberg et al., *supra* note 90.

93. *2023 IRS Cryptocurrency Reporting Requirements*, STRAUSS TROY (Mar. 10, 2022), <https://perma.cc/GX4A-NV79>.

94. Goldberg et al., *supra* note 90.

95. See *id.* (highlighting how an intense cryptocurrency lobbying effort sought to amend the relevant provision to exempt these classes but ultimately failed to make it into the bill prior to passage by the Senate and House).

involving digital assets in an annual tax report, such as Form 1099-B or another form the IRS designs.⁹⁶ This report will require digital-asset brokers to collect “customer’s name, address, and phone number, the gross proceeds from the sale of digital assets, and capital gains or losses and whether these were short-term (held for one year or less) or long-term (held for more than one year).”⁹⁷ Additionally, the Act requires any trade or business that receives more than \$10,000 in cash in exchange for a digital asset to file a Form 8300 within fifteen days.⁹⁸ The trade or business selling the digital asset must gather information, including the buyer’s name, TIN, occupation, birth date, and address.⁹⁹ The Act also requires that “transfer statements be furnished between digital-asset brokers when digital assets are transferred, and it attempts to close gaps by extending transfer reporting to include transfers to non-brokers.”¹⁰⁰

C. *EU Framework: DAC8*

The European Union (“EU”) is also taking steps to regulate the digital financial market through tax policy.

In 2021, the EU made its commitment to a digital future clear by announcing a new EU funding program, Digital Europe, with a plan to spend €7.5 billion in “bringing digital technology to businesses, citizens and public administrations.”¹⁰¹ As part of

96. *Id.*; see also *2023 IRS Cryptocurrency Reporting Requirements*, *supra* note 93 (emphasizing that 2021 legislation extended the broker information reporting rules to cryptocurrency exchanges, custodians, or platforms and digital assets).

97. *Id.*

98. See Kevin Ainsworth et al., *Infrastructure Investment and Jobs Act Contains New Cryptocurrency Reporting Requirements*, BDO U.S. (Jan. 5, 2022), <https://perma.cc/NYR9-X2MU> (illustrating through a hypothetical how an individual selling a single nonfungible token directly for over \$10,000 in bitcoin would be required to file a Form 8300 within fifteen days reporting cryptocurrency receipt).

99. *Id.*

100. Denise Hintzke et al., *Tax Reporting in the Age of Cryptocurrency*, DELOITTE, <https://perma.cc/B4UH-QJ73> (last visited July 6, 2023).

101. *The Digital Europe Programme*, EUROPEAN COMM’N, <https://perma.cc/7KZV-9YA2> (last updated Nov. 14, 2022); see also Nana Ama Sarfo, *The EU’s Cryptoasset Tax Strategy Needs Coordination*, FORBES (Aug.

this digital renaissance, the EU has approved new legislation governing digital assets known as the Markets in Crypto Assets Regulation (“MiCA”).¹⁰² MiCA is a comprehensive regulatory framework for Crypto-Assets governing the transparency, disclosure, authorization, and supervision of Crypto transactions.¹⁰³

As a subsequent measure, in December 2022, the EU proposed a taxation framework for Crypto-Assets called the Directive on Administrative Cooperations 8 (“DAC8”).¹⁰⁴ DAC8 seeks to improve the monitoring and reporting of Crypto-Assets transactions to prevent tax evasion and fraud.¹⁰⁵ DAC8 also “aims to ensure consistent application of crypto-asset reporting rules across the EU.”¹⁰⁶ Similar to the OECD’s CARF and the United States’ IJA, DAC8 requires Crypto-Asset Service Providers to collect, verify, and report relevant user information to the proper authority.¹⁰⁷ It also requires the automatic exchange of such information between member states.¹⁰⁸ DAC8

2, 2021), <https://perma.cc/R5Z4-Z3M8> (framing the Digital Europe project in light of EU’s concern that decentralized, partially anonymous Crypto-Assets could “provide a conduit to the shadow economy and undercut the market for traditional financial instruments, especially if cryptoasset-based income” is underreported or not reported at all).

102. *Proposal for a Regulation of the European Parliament and of the Council on Markets in Crypto-Assets, and Amending Directive*, COM (2020) 593 final (Sept. 9, 2020).

103. *MiCA Set to be Voted into Law in 2023*, SCORECHAIN (Jan. 12, 2023), <https://perma.cc/5GLV-25S3>.

104. *Tax Transparency Rules for Crypto-Asset Transactions*, at 1, European Parliamentary Research Service (Jan. 27, 2023), <https://perma.cc/7UWL-PQG9> (PDF).

105. See Rodrigo Calleja, *DAC8 is Coming—What Crypto Stakeholders Need to Know and Do*, BLOOMBERG TAX (Mar. 24, 2022), <https://perma.cc/2N5U-U93M> (“DAC8 . . . [is] much broader in scope than current EU regulations, giving financial authorities new options for taking action against tax evasion or fraud . . .”).

106. *DAC8: Reporting Rules on Crypto-Asset Transactions*, SIMMONS & SIMMONS (Dec. 14, 2022), <https://perma.cc/P7LZ-PD4D>.

107. See *European Union: DAC 8—Implementation of Crypto-Asset Reporting Framework Published*, BAKER MCKENZIE (Dec. 15, 2022), <https://perma.cc/H3K7-RUDC> (listing required disclosures for Reportable Users, including: legal name, legal address, member state of residency, tax identification number, and, for individuals, place of birth).

108. See *id.* (“[DAC8 requires] the exchange of information from the reported information by the respective member state’s competent authority that is receiving the information from the Reporting Crypto-Asset Service

further extends to financial institutions, requiring them to “report on e-money and central bank digital currencies.”¹⁰⁹ Beyond these requirements, the proposal establishes additional rules for wealthy individuals and imposes minimum penalties for non-compliant behavior.¹¹⁰

D. *Analysis*

In sum, the fact that every major prospective framework for regulating blockchain assets and digital financial markets relies on tax reporting requirements is a testament to their past effectiveness and future potential. Although not identical, the reporting requirements under the FBAR and FATCA are similar to the framework proposals for the digital financial market from the OECD, United States, and European Union.

Indeed, some early discussions have been about whether FBAR and FATCA, which were developed for the traditional financial markets, apply to blockchain assets in the digital financial market.¹¹¹ However, the digital nature of these assets creates complications. Blockchain assets, such as cryptocurrencies and NFTs, exist solely on the internet, which is simultaneously everywhere and nowhere.¹¹² The lack of physical location makes determining which tax authority has

Provider, to the competent authority of another relevant member state where the Reportable User is tax resident.”).

109. *DAC8: Reporting Rules on Crypto-Asset Transactions*, *supra* note 106.

110. *Id.*

111. *See e.g.*, Omri Marian, *Are Cryptocurrencies Super Tax Havens?*, 112 MICH. L. REV. FIRST IMPRESSIONS 38, 44–46 (2013) (noting virtual currencies were not considered in developing FATCA but a similar regulation for cryptocurrencies may help with tax evasion in digital markets); Evgenia Belyavskaya, *Foreign Cryptocurrency: U.S. FBAR and FATCA Reporting Requirements*, PKF O’CONNOR DAVIES (Feb. 22, 2023), <https://perma.cc/W96A-4KBP> (“Cryptocurrency has been excluded from FBAR requirements to date. However, with the recent proposed regulations, FinCEN . . . is looking to include foreign cryptocurrency accounts in FBAR reporting.”).

112. *Cf.* Marian, *supra* note 111, at 41 (“Bitcoins, unlike government-backed currencies and unlike virtual currencies used in computer games, are not really ‘issued’ by anyone. They come into existence when they are ‘mined’ by users.”).

jurisdiction difficult.¹¹³ For example, should authority be based on the taxpayer's physical location or the physical location of the server containing the digital asset? Interestingly, the OECD's CARF proposal attempts to resolve this issue by subjecting service providers to the tax authority in which they reside and then requiring that any collected information be exchanged between countries under the automatic tax exchange of information system.¹¹⁴

Deep analysis regarding the novel tax issue of source taxation versus residence taxation in the digital financial market is beyond the scope of this Essay. However, given such uncertainty and the vast size and complexity of the digital financial market, it is perhaps unsurprising that regulatory agencies have opted for more dedicated frameworks rather than relying upon FBAR and FATCA, despite the latter's proven effectiveness in traditional financial markets.¹¹⁵

III. BENEFITS OF USING TAX REPORTING

The past success and the future application of tax reporting requirements suggest they can be effective tools. In particular, this Essay argues that this policy is especially effective in the digital financial market for three reasons. First, tax reporting requirements are effective at combating money laundering and tax evasion in traditional financial markets, and thus will likely be effective at resolving parallel issues in the digital financial market.¹¹⁶ Second, tax reporting requirements simultaneously target financial institutions and taxpayers, which will likely increase tax compliance and lower the administrative burden, two common issues within the digital financial market.¹¹⁷ Lastly, such requirements have the potential to generate

113. *See id.* at 42 (“[B]ecause there is no jurisdiction in which [cryptocurrencies] operate (they are ‘held’ in cyberspace accounts known as online ‘wallets’), they are not subject to taxation at source.”).

114. OECD, *supra* note 61, at 10 (stating the purpose of the CARF is to provide “a framework of bilateral or multilateral competent authority agreements or arrangements for the automatic exchange of information collected under the CARF with jurisdiction(s) of residence of the Crypto-Asset Users”).

115. *See supra* Part I.

116. *See infra* Part III.A.

117. *See infra* Part III.B.

significant revenue through improved compliance and civil penalties, which can fund much-needed additional regulatory developments in the digital financial market.¹¹⁸ The remainder of this Part will address each of these points in turn.

A. *Proven Efficiency*

Many challenges in the digital financial market, such as money laundering, tax havens, and other forms of tax evasion, overlap with those of traditional financial markets.¹¹⁹ As mentioned in Part I, the tax reporting requirements under FBAR, FATCA, and the like, successfully combat these issues by enhancing overall transparency in the traditional financial market.¹²⁰ Given the overlap of challenges and past success, it is logical to expect similar results in the digital financial market.

One can make a strong argument that secrecy, or an overall lack of transparency, is the defining characteristic of money laundering, tax havens, and other forms of tax evasion.¹²¹ Unfortunately, secrecy is also a key characteristic of the current state of blockchain assets and lies at the heart of the digital financial market.¹²² However, blockchain technology is inherently transparent due to its nature as a public ledger.¹²³ Nevertheless, a key tenet of such technology is the ability of participants to interact without providing any identifying

118. See *infra* Part III.C.

119. See Marian, *supra* note 111, at 44 (“Governments have identified the regulatory challenges of virtual currencies, including the potential of Bitcoin to facilitate tax evasion.”).

120. See *supra* Part I.

121. Cf. Storm, *supra* note 34, at 1443 (using four factors in determining whether a jurisdiction is a tax haven: “the existence of no or nominal taxes, the lack of transparency, the prevention of the effective exchange of information for tax purposes and an absence of a requirement that the activity must be substantial”).

122. See David Yaffe-Bellany, *Millions for Crypto Start-Ups, No Real Names Necessary*, N.Y. TIMES (Mar. 2, 2022), <https://perma.cc/4AJG-3ZMJ> (“The ability to operate anonymously is a central tenet of crypto technology.”).

123. See Telis Demos, *Crypto’s Transparency May Be Part of the Problem Right Now*, WALL ST. J. (Nov. 17, 2022, 8:43 AM), <https://perma.cc/822K-6ZYL> (emphasizing that blockchains’ digital ledger, unlike traditional bank ledgers which are only visible to account owners, are public allowing anyone to track movements of currency from place to place).

information or bank account.¹²⁴ Such pseudonymity arguably undermines the intrinsic transparency of the blockchain and promotes an overall air of secrecy.¹²⁵ Even if policymakers identify suspicious behavior or illegal acts, it may be impossible to identify the criminal unless they make a mistake that allows regulators to connect their identity with the specific digital wallet.¹²⁶ Additionally, pseudonymity promotes various fraudulent activities, the proceeds of which are unlikely to be reported for tax purposes.¹²⁷

A big concern with the digital financial market is the threat of money laundering.¹²⁸ To reiterate, money laundering is the process of disguising criminal proceeds through various schemes.¹²⁹ It traditionally involves moving currency through various financial institutions and assets to disguise illicit funds.¹³⁰ The advent of cryptocurrencies significantly enhances

124. See Yaffe-Bellany, *supra* note 122 (“All cryptocurrency transactions are recorded on decentralized ledger systems . . . which let users transact namelessly, without registering a bank account or interacting with traditional financial gatekeepers.”).

125. See *Money Laundering, Bitcoin and Blockchain: Anonymity, Transparency and Privacy Are Not Incompatible*, FINEXTRA (May 27, 2016), <https://perma.cc/5TPC-X753> (“The identification of beneficial owners lies at the heart of the fight against money laundering, and without it, any legal or technical measure would become ineffective.”).

126. See *How Private Is the Blockchain?*, BITSTAMP LEARN (Aug. 10, 2022), <https://perma.cc/858Y-RXX4> (“[E]ven though it is easy to figure out what transactions someone has made, it is impossible to say who that someone is The only way to expose a blockchain user’s identity is to establish an indisputable connection between them and their public key.”).

127. See Yaffe-Bellany, *supra* note 122 (highlighting the dangers of pseudonymity within the crypto industry by detailing several high-profile fraudulent schemes within the industry).

128. See, e.g., MacKenzie Sigalos, *Crypto Criminals Laundered \$540 Million by Using a Service Called RenBridge, New Report Shows*, CNBC, <https://perma.cc/3GRY-ELU6> (last updated Aug. 10, 2022, 11:04 AM) (describing a money laundering scheme involving RenBridge, a crypto cross-chain bridge); *Money Laundering in Digital Currencies*, NAT’L DRUG INTEL. AGENCY (June 2008), <https://perma.cc/K6RA-Q2TL> (“Digital currencies provide an ideal money laundering instrument because they facilitate international payments without the transmittal services of traditional financial institutions.”).

129. IRM 9.5.5.1 (Feb. 15, 2008).

130. See Katherine A. Lemire, *Cryptocurrency and Anti-Money Laundering Enforcement*, REUTERS (Sept. 26, 2022, 11:06 AM), <https://perma.cc/ZF99-PS2V> (“[Anti-money laundering] laws seek to prevent

this process by eliminating various practical limitations. Criminal proceeds can originate in or be converted into cryptocurrency, then move through thousands of pseudonymous digital wallets within seconds.¹³¹ It also allows criminals to bypass centralized services that trace or freeze suspicious transactions by transferring digital assets across blockchains and circumventing international borders and laws.¹³² NFTs also pose a serious money laundering threat, given their pseudonymous nature and subjective price.¹³³ One method involves self-laundering whereby “criminals purchase an NFT with illicit funds and then resell to a purchaser who pays for it with clean funds unconnected to a prior crime.”¹³⁴

Another concern with the digital financial market is the threat of tax evasion, particularly in the form of tax havens.¹³⁵

‘layering,’ Traditionally, money launderers engaging in layering repeatedly move fiat currency, such as U.S. dollars, into different financial institutions and assets to blur the origins of the criminal proceeds.”)

131. See *id.* (emphasizing that money launderers can use crypto to “move the illicit funds through hundreds of wallets” before cashing out and, unlike bank accounts, “thousands of wallets may be opened without proof of identity, within seconds”).

132. See Sigalos, *supra* note 128 (discussing how launderers use “cross-chain bridges” to create “a loophole in the regulatory regime that has been painstakingly established by governments around the world, to combat crypto laundering”); see also Jonathan T. Marks, *Cryptocurrency and Money Laundering: Why Understanding Fraud Is Critical*, BAKERTILLY (Nov. 15, 2021), <https://perma.cc/2S7X-7GCH> (observing that cryptocurrencies are becoming the preferred currency of money launderers “because cryptocurrency offers a combination of anonymity, ease of use and the ability to circumvent international borders and regulations”).

133. See *What You Need to Know About NFT Money Laundering*, FINTECH GLOB. (Feb. 16, 2023), <https://perma.cc/S7W3-QEUF> (explaining that NFTs have become attractive to money launderers due to “pseudonymous trading, open access, being highly mobile and subjective pricing”); see also David Jolly, *NFTs Should Fall Under Anti-Money Laundering Law, DOJ Says*, BLOOMBERG TAX (Sept. 26, 2022, 4:27 PM), <https://perma.cc/96XB-KUG7> (noting that the market for NFTs “creates conditions under which bad actors like drug traffickers can launder money”).

134. Jolly, *supra* note 133.

135. See Marian, *supra* note 111, at 39 (“To the extent that cryptocurrencies continue to gain momentum, we could reasonably expect tax-evaders—who traditionally executed their tax-evasion techniques through the use of offshore bank accounts in tax-haven jurisdictions—to opt out of traditional tax havens in favor of cryptocurrencies.”); Sarah Gruber, *Trust*,

Scholars and policymakers have long recognized the close nexus between money laundering and tax evasion.¹³⁶ Indeed, tax evasion itself is an inherent form of money laundering because it “[1] produces criminal tax savings; and [2] launders those criminal proceeds by concealing or disguising their unlawful origin.”¹³⁷ Parking funds in tax havens, which are “the most common place to hide money or to launder money,” is also a form of tax evasion.¹³⁸ Although an exact definition of a tax haven is elusive, various factors and characteristics have been identified.¹³⁹ Consistent among them all is a lack of

Identity and Disclosure: Are Bitcoin Exchanges the Next Virtual Havens for Money Laundering and Tax Evasion?, 32 QUINNIAC L. REV. 135, 196–204 (2013) (discussing the threat of Bitcoin exchanges being used as modern tax havens); see also Jeff Kauflin, *IRS and Foreign Tax Enforcers Warn NFTs Pose Growing Money Laundering Risks*, FORBES (Apr. 28, 2022, 5:16 PM), <https://perma.cc/7JPK-QCEU> (summarizing warnings released by foreign regulators and private analysts on the risk of tax crime using digital assets).

136. See, e.g., Patricia Torres Serpel & Amir Shachmurove, *Appropriate Measures to Use Money Laundering Prevention as an Antidote to Tax Evasion*, 10 PEPP. J. ENTREPRENEURIAL FIN. & BUS. VENTURES 57, 57 (2005) (“Money laundering . . . is closely linked with tax evasion and informal trade . . .”); see also Deen Kemsley et al., *Tax Evasion and Money Laundering: A Complete Framework*, 29 J. FIN. CRIME 589, 590 (2022) (hypothesizing that “the actual link between tax evasion and money laundering goes deeper than a simple predicate relationship; . . . all tax evasion is itself necessarily a form of money laundering”); Jesus Becerra, *What is the Relationship Between Money Laundering and Tax Havens?*, JESUS BECERRA (Apr. 27, 2022), <https://perma.cc/MS5F-Y99S> (“[T]he relationship between [tax havens] and the crime of money laundering is close, since they are ideal places for tax avoidance and evasion: bank secrecy and little or no cooperation offer legal protection to the perpetrators of subsequent money laundering.”).

137. Kemsley et al., *supra* note 136, at 591.

138. Storm, *supra* note 34, at 1443; see also Kemsley et al., *supra* note 136, at 596 (“Using a tax haven or other means to simply hide undeclared taxable income also is central to the tax evasion process.”); Richieson Gyeni-Boateng, *The Role of Tax Haven in Money Laundering Activities*, LINKEDIN (Sept. 8, 2020), <https://perma.cc/A5J7-GWHC> (“Simply put, tax haven countries are vulnerable to money laundering activities.”).

139. See Storm, *supra* note 34, at 1443 (“[Tax] haven[s] can be described as being autonomous or semi-autonomous jurisdictions offering a combination of lax legislation, low or zero taxation on income and capital of non-residents, secrecy facilities for banking or corporate ownership, and absence of effective information exchange with the authorities of third party countries.” (internal quotation omitted)); see also OECD CTR. FOR TAX POLY AND ADMIN., COUNTERING OFFSHORE TAX EVASION 11 (Sept. 28, 2009), <https://perma.cc/23MD-XEX8> (relying on four factors to identify tax havens, namely the existence of “[n]o or nominal tax[es],” the “[l]ack of transparency,”

transparency and taxes.¹⁴⁰ Unfortunately, blockchain technology may represent the next generation of tax havens, as it allows participants to remain pseudonymous and operate in a decentralized manner, such that no centralized government can impose a tax.¹⁴¹

In the past, secrecy and a lack of transparency in the traditional financial market led to rampant money laundering, tax havens, and tax evasion.¹⁴² Fortunately, reporting requirements such as the AMLA, FBAR, FATCA, and the Swiss Bank Program, in all of which tax reporting is a significant part, were effective in mitigating these problems.¹⁴³ Given that the digital financial market suffers from similar ailments, it is fair to anticipate an equally efficient result if using tax reporting. In fact, tax reporting requirements may be even more effective in the digital financial market. Because blockchain ledger technology is particularly effective at obscuring identity, tax reporting requirements will ultimately have a proportionally larger positive effect as compared to traditional financial markets.¹⁴⁴

the prevention of the “effective exchange of information” for tax purposes, and an absence of a requirement that the activity must be “substantial”); Marian, *supra* note 56, at 541 (characterizing tax havens as jurisdictions with “very low (or no) taxes on foreign residents, and robust financial secrecy laws”); Gyeni-Boateng, *supra* note 138 (“Tax haven countries are characterized by their developed financial institutions and markets, low record of corruption, limitation on sharing and reporting financial information of beneficiaries to foreign tax authorities and lack of transparency obligations.”).

140. See *supra* note 139.

141. See Marian, *supra* note 56, at 533 (“[T]he rise of blockchain technology is a godsend for tax cheats and tax havens. Blockchain, in its very essence, is a decentralized ledger that documents ownership and transfers, but does not require transacting parties to identify themselves to one another.”).

142. Cf. Storm, *supra* note 34, at 1443 (identifying “lack of transparency” as a key factor in determining whether a jurisdiction is a tax haven); Kemsley et al., *supra* note 136, at 595 (positing that a “basic step” of money laundering is “using layers of complex or secretive transactions to obscure the funds’ true origin”).

143. See Marian, *supra* note 56, at 529, 544–46 (summarizing the success of global regulatory efforts in combatting traditional tax havens); see also Shields, *supra* note 54 (pronouncing that new OECD regulatory proposals have brought an end to “the days when well-paid European professionals could stash wealth across the border and beyond the prying eyes of their tax man”).

144. Cf. *supra* note 124 and accompanying text.

B. *Reporting Requirements Target Both Financial Institutions and Taxpayers*

Another reason tax reporting requirements will be effective tools in the digital financial market is that they will target both individual taxpayers and financial institutions through third-party reporting. Evidence suggests that using third-party reporting agents or withholding tax systems dramatically increases tax compliance and reduces administrative burdens.¹⁴⁵ Given that both tax compliance and administrative burdens are sizeable problems in the digital financial market, it is unsurprising that digital asset frameworks such as CARF, the IIJA, and DAC8 place the burden on financial intermediaries to collect, verify, and report individual taxpayer information to the proper authority, as they are in the best position to obtain all the necessary information.¹⁴⁶

One of the most significant advantages of relying on third-party reporting is its ability to drastically increase tax compliance.¹⁴⁷ Statistics on the compliance rates for reporting wage income with and without third-party withholding or reporting illustrate this advantage.¹⁴⁸ Reports show that when a third-party is responsible for withholding taxes or reporting information, “99 percent of the income tax on wages is reported and paid to the government on time.”¹⁴⁹ Absent third-party responsibility, less than 40 percent is reported.¹⁵⁰ Thus, tax authorities saw a shocking 59 percent increase in tax compliance by simply initiating third-party reporting or withholding. Such results are likely the product of expanding the tax base to include taxpayers that would otherwise go

145. See *infra* notes 147–150 and accompanying text.

146. See *supra* note 70 and accompanying text.

147. See Kathleen DeLaney Thomas, *The Modern Case for Withholding*, 53 U.C. DAVIS L. REV. 81, 90 (2019) (“There is an obvious benefit to the government from tax withholding, which is that tax compliance is demonstrably higher when it is present.”).

148. See *id.* (highlighting compliance outcomes when third-party withholding or information reporting requirements are/are not present); see generally IRS, FEDERAL TAX COMPLIANCE RESEARCH: TAX GAP ESTIMATES FOR TAX YEARS 2008–2010 (May 2016), <https://perma.cc/GA2D-LKRR> (PDF).

149. Thomas, *supra* note 147, at 90.

150. *Id.* at 90; see also IRS, *supra* note 148, at 14 (estimating the self-employment tax non-filing tax gap to be \$4 billion).

undetected,¹⁵¹ ensuring that known taxpayers report accurate information and reducing taxpayers' administrative burdens.¹⁵²

Increased tax compliance is of particular worth in the digital financial market. It is difficult for authorities to verify the accurate reporting and assessment of tax liability because blockchain transactions occur without traditional financial intermediaries or centralized authority.¹⁵³ Indeed, such difficulty prompted the OECD to develop the CARF, which relies on third-party reporting.¹⁵⁴ As further evidence, consider the United States' experience with crypto reporting regulations before 2021. The United States had imposed various reporting requirements on individual taxpayers but found they were largely unsuccessful, prompting the passage of the IIJA, which also utilizes third-party reporting via service providers.¹⁵⁵

Another related advantage of third-party reporting is its capacity to significantly reduce the administrative tax burden on the IRS and the taxpayer.¹⁵⁶ Targeting third-party financial intermediaries simplifies the process for tax authorities, as they can focus their audits on the relatively small number of intermediaries, and these intermediaries are more likely to be

151. See Thomas, *supra* note 147, at 90–91 (“[W]ithholding ensures taxpayers pay some tax, even if they fail to file returns, and brings taxpayers into the tax system (and onto the government’s radar) who may otherwise go completely undetected.”); see also Piroška Soos, *Self-Employed Evasion and Tax Withholding: A Comparative Study and Analysis of the Issues*, 24 U.C. DAVIS L. REV. 107, 127–30 (1990) (explaining how withholding provides a “convenient payment method to taxpayers and enables the government to collect small amounts of tax efficiently”).

152. See Thomas, *supra* note 147, at 84 (“[I]ncome tax withholding has proven to be one of the government’s most powerful and effective enforcement mechanisms to ensure compliance with the tax law.”).

153. See OECD, *supra* note 61, at 6 (“[Crypto-Assets] can be transferred and held without interacting with traditional financial intermediaries and without any central administrator having full visibility on either the transactions carried out, or the location of Crypto-Asset holdings.”).

154. See *id.* (describing CARF as a “dedicated global tax transparency framework which provides for the automatic exchange of tax information on transactions in Crypto-Assets in a standardized manner with the jurisdictions of residence of taxpayers on an annual basis”).

155. See *supra* Part II.B.

156. See Thomas, *supra* note 147, at 90–91 (“[W]ithholding reduces administrative costs for the IRS and speeds up tax collection for the government.”).

on top of the tax process than each taxpayer.¹⁵⁷ Such an approach also simplifies the taxpayers' obligation, as they do not have to keep complicated records of every transaction or apply what can be complex tax law to their situation.¹⁵⁸

Like increasing tax compliance, relieving the administrative burden on the tax authority and the taxpayer is particularly valuable in the digital financial market. As an illustration, consider the crypto-reporting requirements in the United States before the passage of the IIJA. Until the 2023 tax year, cryptocurrency exchanges did not provide taxpayers with a Form 1099-B (i.e., reporting summaries), thus forcing taxpayers to bear the burden of keeping meticulous records of all crypto transactions across various wallets, exchanges, and currencies.¹⁵⁹ Multiplying this burden is the large array and relative incompatibility of available wallets, exchanges, and cryptocurrencies, as well as the frequency with which digital transactions occur.¹⁶⁰ Furthermore, the volatility of blockchain

157. See *id.* at 104 (discussing how “a withholding system allows the IRS to monitor a smaller pool of people,” reducing the number of entities which must be audited and the costs associated with conducting those audits).

158. See *id.* (illustrating through a hypothetical how corporate intermediaries are more likely to have “well-kept books and records as compared to the individual[s]”).

159. See *Yes, Taxpayers Must Report Their Cryptocurrency Trading to the IRS. Here's How*, CBS NEWS: MONEY WATCH (Jan. 26, 2022, 10:40 AM), <https://perma.cc/G6KQ-QQC5> (“Cryptocurrency exchanges won't be required to send taxpayers 1099-B forms, also known as tax-reporting summaries, until the 2023 tax year. So the onus is on traders to keep accurate records of their transactions.”); Kelly Phillips Erb, *More Changes Are on the Way for Cryptocurrency Tax Reporting*, BLOOMBERG TAX (Aug. 12, 2022, 4:45 AM), <https://perma.cc/YP9Z-ADH5> (advising taxpayers to keep “excellent records” because they may need to report information which is not contained in the forms provided by brokers); see also Riley Adams, *Your Crypto Tax Guide*, INTUIT TURBOTAX (May 18, 2023, 1:55 PM), <https://perma.cc/R9HW-3GET> (explaining that the “IRS treats cryptocurrency as property, meaning that when you buy, sell or exchange it, this counts as a taxable event and typically results in either a capital gain or loss”).

160. See *Yes, Taxpayers Must Report Their Cryptocurrency Trading to the IRS. Here's How*, *supra* note 159 (“Reporting a single trade on one exchange likely won't be difficult. But a typical taxpayer has three to five wallets and exchanges . . . This makes it harder to reconcile cost basis across varying platforms.” (internal quotation omitted)).

assets makes it difficult to keep track of details, such as the cost basis, fair market value, and holding period for each asset.¹⁶¹

To make matters worse, the unique nature of digital assets often defies clear-cut rules, requiring individual taxpayers to learn the various nuances or pay for professional help. For example, taxpayers must know the differing tax treatment of cryptocurrency received as an airdrop versus a hard fork versus payment for goods and services.¹⁶² Moreover, the rapid development of digital assets has created various uncertainties in how the current tax laws apply, such as whether NFTs qualify as a collectible or whether staking rewards are taxed similarly to mining rewards.¹⁶³

Requiring taxpayers to keep meticulous records of, and apply uncertain and complex tax laws to, blockchain assets imposes a significant burden and likely necessitates hiring professional help.¹⁶⁴ Indeed, it is likely that these burdens are partly to blame for the lack of U.S. taxpayer compliance before the passage of IIJA.¹⁶⁵ Moreover, it also burdens tax authorities as they try to audit and ensure compliance.¹⁶⁶

161. *See id.* (emphasizing the importance of tracking cost basis across various platforms to pay the accurate amount of capital gains tax); *see also* Nicole Lapin, *Explaining Crypto’s Volatility*, FORBES (Dec. 23, 2021, 6:00 AM), <https://perma.cc/ZL4F-6KEB> (discussing how cryptocurrency’s volatility is at least in part due to it not being backed by any commodity).

162. *See* Adams, *supra* note 159 (defining an airdrop as “when a new crypto project launches and sends out several free tokens to early adopters and their communities,” whereas a “hard fork is a wholesale change in a blockchain network protocol that invalidates previously-verified transaction history blocks or vice versa”).

163. *Cf. IRS Issues Guidance, Seeks Comments on Nonfungible Tokens*, INTERNAL REVENUE SERV., <https://perma.cc/3KQL-PC5B> (last updated Mar. 21, 2023) (seeking feedback on upcoming guidance which clarifies the tax treatment of NFTs as a collectible); *Jarrett v. United States*, No. 3:21-cv-00419, 2022 WL 4793235, at *2–3 (M.D. Tenn. Sept. 30, 2022) (dismissing as moot plaintiff’s action seeking a refund for income taxes paid on cryptocurrency created by plaintiff because government issued a refund check after the lawsuit was filed).

164. *See supra* notes 159–161 and accompanying text.

165. *See supra* notes 90–92 and accompanying text.

166. *Cf. Joel Slemrod, Does It Matter Who Writes the Check to the Government? The Economics of Tax Remittance*, 61 NAT’L TAX J. 251, 263 (2008) (“The principal justification for withholding is that it economizes on the

In short, the relatively recent development of a decentralized digital financial market and the unique nature of digital assets make it especially difficult for taxpayers to report their income accurately and allows opportunists to evade taxes. Implementing third-party reporting requirements resolves both issues by significantly increasing taxpayer compliance and delegating the burden to those more capable. Thus, it is a reasonable path for the CARF, IIJA, and DAC8 to require service providers to gather and report taxpayer information to the proper authority, as they are in the best position to obtain and keep track of all the necessary information effectively.¹⁶⁷

C. *Potential to Generate Significant Revenue*

The final strength of using tax reporting requirements to regulate the digital financial market is its potential to generate considerable revenue via increased tax compliance. As discussed extensively, tax reporting requirements will likely increase tax compliance.¹⁶⁸ Tax authorities can further boost revenue by imposing significant pecuniary penalties for non-compliance.¹⁶⁹ The additional revenue is particularly valuable in the digital financial market, as it can provide funding for much-needed regulatory programs.

At the risk of stating the obvious, increasing tax compliance will inevitably lead to increased tax revenue. Intriguingly, penalties for failing to comply with tax reporting requirements can also provide a significant revenue source. For example, consider the penalties imposed on taxpayers under FATCA, where a failure to report results in “a \$10,000 failure to file penalty, an additional penalty of up to \$50,000 for continued failure to file after IRS notification, and a 40 percent penalty on an understatement of tax attributable to non-disclosed

administrative and compliance costs of collecting a given amount of tax revenue . . .”).

167. See OECD, *supra* note 61, at 11 (“[Service Providers] are expected to have the best and most comprehensive access to the value of the Relevant Crypto-Assets and the Exchange Transactions carried out. . . . As such, they are in a position to collect and review the required documentation of their customers . . .”).

168. See *supra* notes 147–152 and accompanying text.

169. See *infra* notes 170–172 and accompanying text.

assets.”¹⁷⁰ While such penalties might seem relatively small in the grand scheme of things, it has the potential to add up. Additionally, consider the penalties under the BSA and FBAR, which delineate between willful and non-willful violations.¹⁷¹ Willful violations result in a per-account penalty equal to the greater of \$100,000 or 50 percent of each account’s balance,¹⁷² thus opening the door for substantial returns. In contrast, non-willful violations result in a maximum penalty of \$10,000 per report,¹⁷³ representing a smaller, but not insignificant, revenue source.

Interestingly, the United States Supreme Court recently addressed whether a non-willful penalty under FBAR accrues on a per-report or per-account basis in the case of *Bittner v. United States*.¹⁷⁴ Bittner was a dual citizen unaware of his responsibility to file a report under FBAR and BSA from 2007 through 2011.¹⁷⁵ Bittner failed to report 272 accounts in those five years—“61 accounts in 2007, 51 in 2008, 53 in 2009 and 2010, and 54 in 2011.”¹⁷⁶ The government interpreted the language of the non-willful penalty as per-account and imposed a fine of \$2.72 million.¹⁷⁷ Bittner challenged this interpretation, arguing that the penalty applies per each annual report, and thus the fine should only equal \$50,000 for the five missing

170. *Summary of FATCA Reporting for U.S. Taxpayers*, INTERNAL REVENUE SERV., <https://perma.cc/6HAD-QSC2> (last updated Sept. 29, 2022).

171. See Steven L. Walker, *IRS Provides Guidance on FBAR Penalties*, TAX ADVISER (Nov. 5, 2015), <https://perma.cc/RD39-DFVC> (explaining that a “nonwillfulness penalty . . . may be imposed on any person who violates or causes any violation of the FBAR filing and recordkeeping requirements” whereas a “willfulness penalty” is imposed on anyone who commits such a violation “willfully”).

172. *Id.*

173. *Id.*; see also *Bittner v. United States*, 598 U.S. 85, 93–94 (2023) (holding that non-willful FBAR violations accrue on a per-report, not a per-account, basis).

174. 598 U.S. 85 (2023).

175. See *id.* at 90–91 (“Like many dual citizens, he did not appreciate that U.S. law required him to keep the government apprised of his overseas financial accounts even while he lived abroad.”).

176. *Id.* at 91.

177. *Id.*

years.¹⁷⁸ A 5-4 Court held that the penalty accrues on a per-report, not per-account, basis.¹⁷⁹ The majority reasoned that since the statutory language for willful violations was clearly per-account, the absence of the same type of language for non-willful breaches demonstrates Congress's intent to make it a more uniform penalty.¹⁸⁰ As further support, the majority also discussed various "contextual clues" such as IRS fact sheets and form instructions repeating that the maximum penalty was \$10,000 and the unfair results between non-willful and willful violations if a per-account rule was adopted.¹⁸¹

The holding in *Bittner* has various consequences. First, and most obviously, it substantially limits the revenue potential of non-willful penalties under FBAR. As a result of the potentially large discrepancy in penalties, the question of whether an individual acted willfully or not becomes imperative. Hence, it will be interesting to monitor whether the Supreme Court eventually chooses to address the question recently presented in *Bedrosian v. United States*¹⁸²—whether "willfulness under 31 U.S.C. § 5321(a)(5)(C) should be determined according to a subjective, rather than objective, standard that focuses on an individual's knowledge and intent in failing to disclose a foreign account."¹⁸³ Lastly, the *Bittner* holding raises the question of

178. See *id.* at 92 ("As [Bittner] put it, an individual's failure to file five reports in a timely manner might invite a penalty of \$50,000, but it cannot support a penalty running into the millions.")

179. See *id.* at 93–94.

180. See *id.* at 95 ("[T]he one thing Congress did not say is that the government may impose nonwillful penalties on a per-account basis. Conspicuously, the one place in the statute where the government needs per-account language to appear is the one place it does not."); see also Robert Goulder, *The Bittner Decision: FBAR Penalties Made Simple*, 109 TAX NOTES INT'L 1745, 1747 (2023) (discussing Justice Gorsuch's examination of the statutory language); George K. Yin, *Of Blind Men, Elephant, and the Supreme Court's Misinterpretation of the FBAR Statute*, in UNIV. VA. PUB. L. & LEGAL THEORY RSCH. PAPER SERIES 1, 2–3 (University of Virginia, Research Paper No. 2023-56, 2023), <https://perma.cc/3G5A-ECNZ> (PDF) (criticizing Justice Gorsuch's interpretation of the statute).

181. *Bittner*, 598 U.S. at 96–97; see also Goulder, *supra* note 180, at 1747 ("These [contextual] factors aren't controlling, but they add to the case for reversal.")

182. *Bedrosian v. United States*, 42 F.4th 174 (3d Cir. 2022), *cert. denied* 143 S. Ct. 2636 (2023) (mem.).

183. Petition for Writ of Certiorari, *Bedrosian v. United States*, 143 S. Ct. 2636 (2023) (No. 22-598).

whether taxpayers who overpaid non-willful penalties but signed a closing agreement with the IRS are able to seek a refund.¹⁸⁴

Taking a step back, it seems relatively clear from the examples above that monetary penalties for violating tax reporting requirements can positively impact revenue. Therefore, a similar approach to tax reporting requirements in the digital financial market makes sense. Although *Bittner*'s holding cuts against the profitability of non-willful penalty provisions under FBAR, it is essential to note that FATCA and willful FBAR violations are still per-account and represent high revenue potential.¹⁸⁵ Moreover, the disagreement in *Bittner* was based entirely on statutory interpretation and whether Congress intended to maximize revenue or merely put the IRS on notice of potential violations for future investigation.¹⁸⁶ The court ultimately found Congress's intent to align with the latter.¹⁸⁷

Understanding the outcome in *Bittner* provides policymakers with an outline for avoiding similar results and for maintaining the revenue potential of non-compliant penalties. Specifically, policymakers should use explicit language and identify a purpose that is furthered by per-account penalties. A strong argument can be made that the dual purpose of tax reporting requirements in the digital financial market should be

184. See Aysha Bagchi, *IRS Penalty Refund Options for Foreign Account Holders Uncertain*, BLOOMBERG TAX (Mar. 20, 2023, 4:46 AM), <https://perma.cc/Q4T7-HJV6> ("Many account holders who overpaid non-willful penalties would have signed a closing agreement with the IRS that likely blocks their ability to seek refunds, according to practitioners. But even for those who didn't agree not to seek a refund, getting the refund may still be hard.").

185. See *Comparison of Form 8938 and FBAR Requirements*, INTERNAL REVENUE SERV., <https://perma.cc/QBP2-U86Z> (last updated Sept. 28, 2022) (specifying penalties per each account under FACTA's required Form 8938 and for willful violations under FBAR).

186. See *Bittner v. United States*, 598 U.S. 85, 100 (2023) (determining that BSA's regulatory scheme suggests that "the law aims to provide the government with a report sufficient to tip it to the need for further investigation, *not* to ensure the presentation of every detail or maximize revenue for each mistake").

187. See *id.* at 99 ("[W]hat we do not see is any indication that Congress sought to maximize penalties for every nonwillful mistake . . .").

to generate revenue and increase tax compliance, given the significant amount of money in the market, the need to fund further regulation, and a history of low taxpayer compliance.¹⁸⁸ Implementing a per-account penalty for non-compliance would generate revenue and act as a “stick” to ensure tax compliance. Additionally, imposing per-account penalties may increase whistleblower activity due to higher rewards and incentives, resulting in higher revenue and tax compliance.¹⁸⁹

More revenue provides governments with the ability to finance worthwhile projects and efforts. It may be particularly beneficial in funding the various regulations required to combat the historically risky digital financial market.¹⁹⁰ The rapid development and popularity of digital assets, combined with a lack of regulation and the ability to participate pseudonymously, creates significant cyber security and fraud concerns.¹⁹¹ Additionally, online wallets lack the same protections as bank accounts, and digital assets are highly volatile and not backed by the government or a central bank.¹⁹² Reflect on the recent collapse of FTX, where at least \$1 billion of customer funds are missing in the aftermath, prompting investigations by the DOJ, SEC, and CFTC.¹⁹³ Although many agree on the need for more regulation,¹⁹⁴ it is not free. The additional revenue gained from tax reporting requirements can help fund regulatory efforts, which are likely to be a massive undertaking.

In sum, tax authorities implementing third-party reporting requirements are likely to experience an increase in revenue from higher tax compliance and penalties for non-compliance.

188. See *supra* note 90 and accompanying text.

189. Cf. Goulder, *supra* note 180, at 1745–46 (discussing the whistleblower advocates’ amicus brief in *Bittner*).

190. See *supra* note 11 and accompanying text.

191. See *Challenges and Risks Associated with Non-Fungible Tokens (NFT)*, SHARDEUM (Oct. 26, 2022), <https://perma.cc/3CUU-CWUF> (“There are significant cybersecurity and fraud threats as a result of the development of the digital world and the astounding increase in the popularity of NFTs.”).

192. See Lapin, *supra* note 161 (“[W]ithout anything intrinsically valuable backing up the currency, crypto’s market value is based entirely on speculation . . . Investing in something that is speculative is a guaranteed way to introduce volatility in your portfolio.”).

193. See Berwick, *supra* note 19 (summarizing the aftermath of FTX’s collapse, including ongoing investigations).

194. See *supra* note 21 and accompanying text.

That revenue can then fund additional regulatory measures in the digital financial market.

CONCLUSION

The digital financial market is likely struggling due to a lack of consistent regulation. Although the recent collapse of high-profile crypto exchanges and the ongoing “crypto winter” have led many to push for more stringent regulations,¹⁹⁵ not much has been said about the strengths of using tax reporting requirements as a regulatory tool. Such a lapse is a mistake, as tax policy can play an essential role in regulating the blockchain assets that make up the digital financial market.

First, implementing a tax policy enforcing transparency and reporting requirements is likely efficient in the digital financial market, as it has successfully combatted similar issues, namely money laundering and tax evasion, in traditional financial markets. Second, tax transparency and reporting requirements are likely effective, as many regulators across the globe are utilizing them in upcoming digital asset frameworks. Lastly, these reporting requirements are particularly important in the digital financial market, as they have effectively resolved similar issues in the past, target both taxpayers and financial intermediaries, and will likely boost revenue.

195. See *supra* note 21 and accompanying text.