GIBSON&PERKINS
INCOME TAX AND ESTATE TAX UPDATE

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NEWS UPDATES

More on Noncompete Ban

Recently, the FTC published its new ruling (89 FR 38342) which impacts the enforceability of certain covenants not to compete and other such similar covenants.

Basic Application of the Rule

On April 23, 2024, the FTC announced its Final Non-Compete Clause Rule (the "Rule") which bans certain non-compete clauses between employers and their workers. This currently proposed Rule is broad because it bans almost all forms of covenants not to compete between employers and employees. In addition, even though the Rule does not explicitly ban other types of covenants, such as non-disclosure agreements, customer non-solicitation agreements, or employee non-solicit agreements, the Rule will clearly ban such other types of agreements if they have the same operative effect as covenants not to compete. In other words, the FTC would look at whether the agreement effectively prevents an employee from seeking or accepting other work or starting a business after their employment ends. In this respect, the Ruling could be applicable to more than just noncompete agreements/provisions.

Retroactive Application – Except for Senior Employees

In addition to its application past its effective date, the Rule is, to a large extent, retroactive. For almost all existing covenants not to compete, the Rule makes such provisions unenforceable. An exception to the retroactive nature of this Rule is noncompete agreements for "senior executives." Under the Rule, a senior employee is someone earning more than $151,164, AND who is in a "policy-making position" that could affect the entire organization.

The FTC attempts to "isolate the workers who are least likely to have experienced exploitation and coercion and most likely to have bargained for meaningful compensation for their non-compete. Workers for whom exploitation and coercion concerns are likely most relevant and who are unlikely to have bargained for or received meaningful consideration for a non-compete—namely, lower-earning workers, and relatively higher paid or highly skilled workers who lack policy-making authority in an organization—do not fall within this final definition."

For example, many executives in the "C-suite" will likely be senior executives if they are making decisions that have a significant impact on the business, such as important policies that affect most or all of the business. Partners in a business, such as physician partners of an independent physician practice, would also generally qualify as senior executives under the duties prong, assuming the partners have authority to

make policy decisions about the business. The FTC estimates that fewer than 1% of workers are senior executives under the Rule.

That said, non-competes signed with senior executives AFTER the effective date of the Rule will not be enforceable. The exception for senior executives only applies to non-competes already in effect.

§910.3 Exception for Bona Fide Sale of a Business

The FTC made an exception for certain non-competes connected with the bona fide sale of a business. Section 910.3 of the Rule would allow non-competes where the restricted party is "a person who is selling a business entity or otherwise disposing of all of the person's ownership interest in the business entity, or . . . selling all or substantially all of a business entity's operating assets.

A principal reason for this exception to the Rule is the FTC's acknowledgment that non-competes between the sellers and buyers of businesses may implicate unique interests and have unique effects that this rulemaking record does not address. The FTC has left much up to judicial interpretation in this exception.

State Laws

The Rule only preempts state laws to the extent the state law conflicts with the Rule, which is consistent with the Supremacy Clause of the United State Constitution. In other words, a state would not be able to rule non-competes enforceable. However, if a state decides to further restrict this area of law, they may do so. For example, if California law rules that customer non-solicitation agreements are unenforceable, even though the Rule does not provide for this, that California law would be valid.

Effective Date

As alluded to above, currently, the Rule is only a proposed rule. It would become effective 120 days after being published in the Federal Register for public comment. The Rule is set to go into effect on September 4, 2024.

Pending Challenges

There are plenty of pending challenges against the Rule, which focus largely against the lack of the statutory authority for the FTC to enact these kinds of substantive rules. Due to these challenges, it is possible the Rule could be enjoined before it goes into effect.

Action Items for Employers

Even though the Rule is not yet in effect, employers should act as though the Rule will become effective on September 4. Employers should of course follow whether the Rule is in fact enjoined.

It may also be prudent to prepare to send notices should the rule become effective by compiling a list of impacted current and former employees with relevant contact information, and similarly determining whether any impacted employees qualify for the senior executive exception. Along the same lines, employers may consider whether they want current "senior executives" to sign non-competes before the Rule goes into effect.

Income Tax Effects of Rescheduling Marijuana

Under the Controlled Substances Act, drugs are classified based on their medical use and their abuse or dependency potential into one of five schedules. Marijuana is now a Schedule I drug, the highest level. In 2022, President Biden requested a review of whether to reclassify marijuana to a lower schedule or to take it off the list. In 2023, the Dept. of Health and Human Services advised reclassifying the drug to Schedule III. And now the Dept. of Justice has confirmed that the Drug Enforcement Admin. will soon propose approving the rescheduling of marijuana to a Schedule III drug. That proposal will be subject to comments from the public before being finalized.

Under IRC Sec. 280E businesses that traffic in Schedule I or Schedule II drugs that are illegal under federal law are prohibited from claiming business expenses, other than cost of goods sold, on their federal income tax returns. It's irrelevant that weed is legal under the laws of the state in which the marijuana seller is located. If the drug is downgraded to Schedule III, then legal marijuana firms can deduct their business expenses.

Battle Against the Corporate Transparency Act Continues

The National Small Business Association (NSBA) has filed its brief with the Eleventh Circuit urging it to uphold a lower court's finding that the Corporate Transparency Act (CTA) is unconstitutional. Meanwhile bills in both chambers of Congress call for repeal of the law.

Congress passed the CTA in 2021 to combat money-laundering, financing of terrorist activities, and tax evasion. Under the CTA, specified business entities are required to file beneficial ownership information about their owners, officers, and other control persons with Treasury's Financial Crimes Enforcement Network (FinCEN). The initial reporting requirements went into effect this January, and penalties for noncompliance include substantial fines and imprisonment.

However, the NSBA alleges that the CTA's reporting requirements obligate US citizens and residents to report sensitive personal information, in violation of their constitutional rights. An Alabama federal district court agreed this March. (National Small Business United (DC AL 3/1/2024) 133 AFTR 2d 2024-885) That court found that Congress had exceeded its foreign affairs, commerce, and tax powers in enacting the CTA. It enjoined enforcement of the CTA's beneficial ownership information filing requirements for NSBA members — however, all other business entities are still obligated to file the information.

The case is now on appeal before the Eleventh Circuit. In their appellate brief, attorneys for the NSBA contend that the district court correctly found that the CTA exceeds Congress' Article I powers. They also argue that, in the alternate, the Eleventh Circuit should enjoin enforcement of the CTA because it violates the Fourth Amendment's protections against unreasonable searches and seizures. The district court failed to reach that argument in its March decision, finding it sufficient that the CTA did not fall within Congress' "enumerated powers."

Requiring businesses to submit beneficial ownership information for law-enforcement purposes is a "search," says the NSBA in its brief. "The Fourth Amendment reflected the Framers' judgment that any claimed governmental need to make law enforcement easier cannot justify suspicion less searches of the citizenry," the NSBA explains. It alleges that the CTA is being used as "a workaround to the Fourth Amendment's warrant requirement to fight financial crimes more efficiently."

The NSBA draws a parallel to a 1979 US Supreme Court case, *Brown v. Texas (*443 U.S. 47), where the Court struck down a state statute that allowed the police to detain people and require their names and addresses despite lacking a "specific basis" for believing they are involved in a criminal activity. The brief also argues that an exception to the Fourth Amendment for "special needs" is inapplicable because the beneficial ownership information is being gathered for general purposes — not a specific circumstance where obtaining a warrant would be impracticable.

Cases challenging the constitutionality of the CTA have also been filed in Maine and Michigan federal district courts.

Meanwhile, Representative Warren Davidson (R-OH) introduced a bill (HR 8147) to repeal the CTA late last month. And Senator Tommy Tuberville (R-AL) followed with a Senate bill (S 4297) on May 9.

New Offer in Compromise Booklet Released

The IRS recently released the latest version (April 2024) of the Form 656-B, Offer in Compromise Booklet. According to the IRS, tax professionals should always download and use the most current version of the OIC booklet to avoid processing delays.

An offer in compromise is an agreement between a taxpayer and the IRS that settles the taxpayer's tax debt for less than the full amount owed. Generally, a taxpayer must make an offer based on what the IRS considers the taxpayer's ability to pay. In addition, the taxpayer must have exhausted other options for paying their tax debt. The IRS won't accept an offer if the taxpayer can pay their tax debt in full through an installment agreement or equity in assets.

Once the IRS receives an offer it will consider each taxpayer's unique set of facts and circumstances before accepting an OIC.

Before filing an offer, a taxpayer must (1) file all tax returns they are legally required to file; (2) have received a bill for at least one tax debt included in the offer; (3) make all required estimated tax payments for the current year; and (4) for business owners with employees, make all required federal tax deposits for the current quarter and the two preceding quarters.

ESTATE TAX

Estate Not Liable for Gift Tax on Sale of Shares Received from Terminated Marital Trusts

The Tax Court has ruled that Sally J Anenberg's estate was not liable for gift tax upon the termination of the marital trusts because Sally received shares that she was treated as owning and she did not make a gratuitous transfer of those shares as required by Code Sec. 2501.

The court also held that the estate was not liable for gift tax on the sale of those shares for promissory notes because Sally's qualifying income interest in the QTIP property terminated with the marital trusts and, therefore, Code Sec. 2519 didn't apply to the sale. (Estate of Sally J Anenberg, (5/20/2024) 162 TC No. 9)

Facts. After Sally's husband Alvin died in 2008, property held in their family trust, including shares of Sally and Alvin's incorporated business (Al-Sal) passed to marital trusts in which Sally held an income interest for life and Alvin's children held contingent remainder interests. Alvin's estate made a qualified terminable

interest property (QTIP) election for the property passing to the marital trusts and claimed a marital deduction for the QTIP property.

In March 2012, a state court terminated the marital trusts, and ordered all the property (mostly Al-Sal shares) held by the trusts to be distributed to Sally. That same year, Sally made gifts of some shares to Alvin's children, then sold the remaining Al-Sal shares to Alvin's children and grandchildren for interest-bearing promissory notes equal to the purchase price of the shares. Sally filed a gift tax return and paid gift tax for the gifts, but didn't report the sale of Al-Sal shares. Sometime later, Sally passed away.

The IRS examined Sally's 2012 gift tax return and issued a Notice of Deficiency to Sally's estate stating that the termination of the marital trusts and sale of the Al-Sal shares for promissory notes was a disposition of Sally's qualifying income interest and that her estate was liable for gift tax on the value of the QTIP minus the value of Sally's qualifying income interest.

Background. Upon the death of a citizen or resident of the US, a tax is imposed on the "taxable estate" transferred to the decedent's heirs. Generally, when computing the amount of the taxable estate, the value of property passing from the decedent to his or her surviving spouse is deductible. However, the marital deduction generally is not available for a temporary interest (such as a lifetime interest) passed to a surviving spouse unless a QTIP election is made.

The qualified terminable interest property (QTIP) rules permit a decedent who leaves a qualifying lifetime property interest to a surviving spouse to take the marital deduction for the full value of the QTIP, not just the lifetime interest. The rules create a legal fiction under which the surviving spouse is treated as receiving all the QTIP when the surviving spouse has acquired only a lifetime income interest in that property.

Note. These rules are designed to prevent the value of the surviving spouse's interest in the QTIP from escaping tax altogether.

Arguments. The IRS argued that Sally gifted the full value of the QTIP (which was mostly Al-Sal shares) less the value of her qualifying income interest, resulting in a gift tax liability of more than $9 million and related penalties.

The estate argued that Sally converted her qualifying income interest in the QTIP into an equivalent interest in other property. Such conversions, the estate said, are not a disposition under Code Sec. 2519. In the alternative, the estate argued that even if there was a disposition when Sally received the trust's assets and later sold the shares, no gift tax is due because Sally didn't make a gift; Sally received full and adequate consideration for the property she transferred.

Tax Court agreed with the estate. The Tax Court agreed with the estate that even if the termination of the marital trusts and subsequent distribution of the Al-Sal shares was a disposition, it did not result in gift tax liability for Sally.

The court notes that a transfer alone is insufficient to create a gift tax liability. "The gift tax applies on the transfer of property by gift during [the] calendar year," the court said. So, to be liable for any gift tax on the transfer, Sally must have made a gift.

To determine whether Sally made a gift, the court compared what she had before and after the termination of the marital trusts. The court found that after the termination, Sally had full unencumbered ownership of

the Al-Sal shares instead of a life estate in the trust income. As a result, the termination didn't result in any "gratuitous transfers" by Sally because Sally never "parted with dominion and control as to leave in [her] no power to change its disposition." Moreover, after the marital trusts terminated, Sally no longer held a qualifying income interest in the QTIP so her sale of the Al-Sal shares for promissory notes could not trigger Code Sec. 2519.

ENFORCEMENT

From the Kiplinger Tax Letter – 5/9/2024 Issue

IRS Audit Road Map

In 2022, lawmakers promised the agency $80 billion, to be spread out over 10 years. This is in addition to IRS's regular annual funding. Over half the money is for increased enforcement and collection measures. This year, Congress clawed back 25% of the funding.

Last year, IRS released its operating plan, discussing what it would do with the extra money. On enforcement, IRS said it would do more audits of big C corporations and partnerships, individuals with high income or high wealth, cross-border activities, digital currency and more. IRS has now updated that plan, giving a bit more specific audit road map.

Large corporations would see their audit rates skyrocket under IRS's plan.

The overall audit rate for 2019 C corporation Form 1120 tax returns was 0.4%, while C corps reporting $250 million or more in assets had a nearly 9% audit rate. IRS wants to raise that 9% figure over time until it reaches 22.6% for 2026 returns. Expect audit rates of C corps with less than $250 million in assets to also go up.

Audit coverage of large partnerships and S corporations would increase to 1%. This number might seem small, but considering that for several years the audit rate for partnerships and S corps has hovered around 0.1%, it really is a sizable jump. IRS's updated plan projects that audit rates for pass-through entities with $10 million or more in assets would rise until they reach 1% for 2026 Forms 1065 and 1120-S.

Wealthy individuals with lots of income would also feel more audit heat.

IRS's overall audit rate for 2019 individual returns was 0.3%. But individuals reporting $1 million or more of income had a higher audit rate: 11% for 2019 returns reporting $10 million or more of income, 3.1% for returns with income of over $5 million and under $10 million, and 1.6% for returns reporting income between $1 million and $5 million. IRS wants to raise the 11% figure for people with $10 million or more of income to 16.5% for 2026 Form 1040s. Other high-incomers will see more audits, too. IRS will also use its regular annual funding to do audits of other individuals, as it has in the past. So knowing what auditors look for in selecting returns for exam is still crucial. Go to www.kiplinger.com/kpf/tax-audit for a list of 19 audit red flags.

IRS pledges to not hike audit rates for taxpayers earning $400,000 or less.

More specifically, the agency vows that individuals and small businesses with earnings of $400,000 or less will not see more audits when compared with historic rates. It is our understanding that this applies only to taxpayers with total positive incomes up to $400,000, meaning income before taking losses and deductions

on the return. Also, according to the IRS commissioner, the audit rate on 2018 returns will be used for the purpose of the historic rate comparison. The overall audit rate for 2018 returns was 0.3% for individuals, 0.6% for C corps and 0.1% for partnerships and S corps.

The Service is eyeing NIL collectives that claim 501(c)(3) tax exemption.

Now that college athletes can be compensated for their name, image and likeness, college boosters are setting up nonprofits to develop and fund or otherwise help to facilitate paid NIL deals for student athletes. Some groups vow to pay athletes up to 100% of the contributions the group receives. In the past, the agency had granted 501(c)(3) tax exemption to some groups. But in May 2023, IRS lawyers said informally that many NIL collectives operate primarily for nonexempt purposes by serving the private interest of athletes, and don't qualify for 501(c)(3) status. Last month, the IRS commissioner said in a hearing before Congress that agents have started revoking or denying 501(c)(3) status to some of these organizations. IRS confirms that it has begun an exam-focused compliance strategy in this area.

Here's an example in which IRS denied an NIL collective's 501(c)(3) status. The agency privately ruled that the group serves a private interest and not a public one because it confers benefits primarily on athletes of a specific school's sports team for the use of the athletes' NIL. Its main activity is to increase paid NIL opportunities for the athletes so they receive compensation. This isn't an exempt purpose, IRS says.

Promoting an illegal charitable deduction ploy leads to prison time.

A Florida lawyer designed a fraudulent tax shelter scheme. He and two cohorts promoted the plan to high-income people as a way to claim charitable write-offs. He set up fake charities for his clients to "donate" property to, while at the same time the clients retained control over those "donated" assets. He also backdated documents, allowing clients to claim deductions for prior years. He was audited by IRS, which determined the charities were shams. But that didn't stop the promoter, who just created new charities and continued marketing them. The Dept. of Justice filed criminal charges against him, and he was sentenced to prison for eight years plus three years of supervised release. He will also have to pay restitution.

From the Kiplinger Tax Letter – 5/23/2024 Issue

Incidents of cyberthieves scamming tax professionals are on the rise.

In the quest for taxpayer data, these increasingly sophisticated thieves seek sensitive preparer information, such as Centralized Authorization File numbers. To stem the tide, IRS is taking two actions: It's suspending CAF numbers that it suspects are compromised. Tax pros who face this issue will hear from IRS, and, after going through heightened security procedures, will get new CAF numbers. Also, tax pros face new security measures in getting transcripts for clients. All tax professionals who order federal tax transcripts for their clients by telephone must call IRS's Practitioner Priority Service line to ask that those transcripts be deposited into their Secure Object Repository mailbox. No other IRS phone lines will be available for this purpose. Callers will face enhanced security questions. If the operator on the PPS phone line can't verify the caller's identity, the agency won't immediately deliver the transcript to the requestor, but will instead mail it to the taxpayer's address on record, which of course will take a much longer time.

Having your wholly owned corporation pay your expenses is a tax loser.

A man who owned a C corp that operated a lobster brokerage business had his company pay $193,000 of his personal expenses, including credit card debt, auto leases and more. The tax law treats him as receiving a constructive dividend from the company's payment of those costs (Maderia, TC Summ. Op. 2024-5).

It's not all bad news. The shareholder in the case got a lucky break. He doesn't owe the 20% accuracy-related penalty because he had reasonable cause and acted in good faith. The Tax Court noted that IRS audited prior-year returns with no adjustments, even though his firm had paid his expenses in those years, too.

15 straight years of losses dooms an avid hunter's profit motive argument.

His ecotourism activity is a hobby and not an activity engaged in for profit. He's a real estate developer who years ago began conducting an ecotourism operation on a portion of land that he owned in Texas. The activity consisted of selling packages for hunting, fishing and other events. For years, he claimed big losses on Schedule F that offset income from other sources. The Tax Court analyzed factors for determining whether an activity is engaged in for profit, and decided three were most significant in its decision that the taxpayer didn't have an actual and honest profit objective: 15 years of big losses with no profit potential, personal pleasure derived by him, and he didn't carry on the activity in a businesslike manner. At the end of the day, the Court agreed with IRS's disallowance of the losses (*Schwarz,* TC Memo. 2024-55).

An IRS income tax summons on behalf of a foreign tax authority is valid, an appeals court says.

The third-party summons was issued by the Service on a U.S. bank used by a Spanish citizen at the request of Spain's tax agency, which was conducting an investigation into the man's Spanish tax liabilities. The individual opposed the summons, claiming he was not a resident of Spain or the U.S., but to no avail. The court allowed it because it was properly issued by IRS at the request of a U.S. treaty partner, along with a written declaration from an appropriate official at the Revenue Service (Rabassa, 11th Cir.).

Wages are not taxable. Paying taxes and filing returns are voluntary. The 16th Amendment is invalid.

These are examples of frivolous arguments that taxpayers have made over the years as excuses for not paying federal income tax or for filing false returns. Of course, these claims don't prevail with the courts. IRS can impose severe penalties for frivolous arguments…up to $25,000. But it doesn't always do so. Take this case of a teacher who filed 1040s for multiple years but didn't report his salary from teaching. For his 2015 return, the Service first assessed the frivolous return penalty, but then abated it. He then excluded his teacher's salary from his 2016, 2017, 2018 and 2019 returns. IRS audited his 2019 return and imposed the fine. The case went to Tax Court, which upheld a $15,000 frivolous return penalty (Swanson, TC Bench Opinion).

Among this year's priorities for IRS's Criminal Investigation division:

Clamping down on cybercrimes and illegal digital asset transactions. An initial IRS review showed up to a 75% noncompliance rate…some of it unlawful. CID created the Office of Cyber and Forensic Services to group CID's digital assets, cybercrimes, and digital and physical forensics units. CFS is aiding in criminal

probes across the Service entailing the illicit use of digital assets, and how they are used or can be used to illegally exploit the U.S. tax and financial system. Last year, CID deployed four cyber attachés to points around the globe to work with peers in other countries to help combat the ever-growing rise in international cybercrime.

Significant Civil and Criminal Tax Penalties for Non-reporting of Cryptocurrency Transactions

On August 29, 2023, Treasury and the IRS published proposed regulations that, if finalized, will require brokers (including digital asset trading platforms, digital asset payment processors, and certain digital asset hosted wallets) to report sales and exchanges of digital assets by their customers.

Under the proposed regulations, sales or exchanges of digital assets, i.e., 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, including non-fungible tokens ("NFTs"), that take place on or after January 1, 2025, will require brokers to report gross proceeds to the IRS on a newly developed Form 1099-DA (a draft of which was released by the IRS on April 18, 2024) and to provide similar statements to their customers.

Furthermore, brokers will be required to report gain or loss and basis information for sales that take place on or after January 1, 2026, on Form 1099-DA, as well as to their customers on a corollary statement. Additionally, the proposed regulations will require reporting on real estate purchasers who use digital assets to acquire real estate. Finally, the proposed regulations will require reporting in the case of transactions involving the exchange of digital assets for goods or services.

In addition to the new reporting regulations, since 2019, the IRS has been asking taxpayers whether they have received or disposed of digital assets. Specifically, at the very top of page one of the "U.S. Individual Income Tax Return" (Form 1040 of Form 1040-SR), right under the "Filing Status" is a section entitled "Digital Assets." That section asks the very simple "yes/no" question:

At any time [during the tax year] did you:

- receive a digital asset (as a reward, award, or a payment for property or services); or
- sell, exchange, or otherwise dispose of a digital asset (or financial interest in a digital asset).
- For this purpose, "digital assets" are any digital representation of value that are recorded on a cryptographically secured distributed ledger or similar technology. For example, digital assets include NFTs and virtual currencies, such as cryptocurrencies and stable-coins. If a particular asset has the characteristics of a digital asset, it will be treated as a digital asset for U.S. income tax purposes.

A taxpayer is considered to have a financial interest in a digital asset if he or she is the owner of record of a digital asset, including the rights and obligations to acquire a financial interest, or he or she owns a "wallet" that holds a digital asset.

The question cannot be left unanswered. A taxpayer must answer "Yes" or "No" by checking the appropriate box.

Reporting digital asset transactions; civil and criminal penalties for not reporting

If a taxpayer has disposed of any digital assets during the tax year which they held as a capital asset through a sale, trade, exchange, payment, or other transfer and have checked "Yes," the taxpayer uses Form 8949 "Sales and Other Dispositions of Capital Assets" to calculate capital gain or loss on Schedule D "Capital Gains and Losses" of Form 1040 or Form 1040-SR. If the taxpayer has received any digital asset as compensation for services or disposed of any digital asset that they held for the sale to customers in a trade or business as a dealer, the taxpayer must report the income as they would report other income of the same type (e.g., W-2 wages or inventory or services). Not reporting your cryptocurrency transactions can result in civil fines and penalties of up to $100,000 and criminal sanctions of up to five years in prison.

Proposed regulations

As noted above, on August 29, 2023, Treasury and the IRS published proposed regulations that, if finalized, will require brokers (including digital asset trading platforms, digital asset payment processors, and certain digital asset hosted wallets) to report sales and exchanges of digital assets by their customers. Under Code Sec. 6045, brokers are generally required to file informational returns showing gross proceeds, tax basis, gain or loss information, and the long-term or short-term capital gain treatment of such gain or loss on the sales effected through the broker by their customers.

The Infrastructure and Jobs Act of 2021 expanded the definition of "broker" to include "any person who (for consideration) is responsible for regularly providing any service effectuating transfers of digital assets on behalf of another person" and expanded the definition of "covered security" to include digital assets acquired on or after January 1, 2023.

As also noted above, on April 18, 2024, the IRS issued the new Form 1099-DA in draft form which will ultimately be the basis in which brokers fulfill their reporting obligations under Code Sec. 6045.

Absent the finalization of the proposed regulations, the IRS and Department of Justice (the "DOJ") have already signaled that they have begun to aggressively pursue civil and criminal charges against US taxpayers that do not report or have misreported their income from digital assets. Treasury and IRS officials held a public hearing on the proposed regulations on November 13, 2023, and final regulations have yet to be released.

The case of *US v. Frank Ahlgren III* is illustrative of the aggressive pursuit of civil and criminal penalties for the non-reporting of cryptocurrency transactions.

On February 7, 2024, the IRS and the DOJ made public their first indictment of an individual that dealt purely with undisclosed gains on the taxpayer's cryptocurrency transactions.

In a Texas federal court, they have alleged that Frank Ahlgren III failed to report capital gains from a nearly $4 million sale of bitcoin. Though no answer has yet been filed (nor has any other public statement been made by the defendant), Ahlgren was arrested on April 9, 2024, and has been ordered to remain in federal custody pending trial due to a determination that Ahlgren presents a substantial flight risk.

The IRS has indicated that this case is just the first of "hundreds" of cryptocurrency cases that will soon become public.

What should taxpayers do?

Moving forward, taxpayers should always answer the digital asset question on the Form 1040 and Form 1040-SR and should answer that question honestly. If a taxpayer has engaged in reportable cryptocurrency transactions during the tax year in question, those transactions must be reported and the attendant US federal income tax (if any) must be paid.

If there are tax years in which a taxpayer had cryptocurrency transactions and failed to meet their U.S. tax compliance obligations, a voluntary disclosure should be considered. With the enhanced scrutiny by the IRS and the DOJ, a taxpayer always wants to get to the government before the government gets to him or her.

IRS Increases Security Measures for Practitioners Obtaining Client Transcripts

In an attempt to stem the tide of identity theft and refund fraud, the IRS has announced increased security measures for the Centralized Authorization File (CAF) program and has adopted new guidelines for tax professionals requesting client transcripts by phone. (**IR 2024-136**, 5/9/2024)

Requirement that Taxpayer file FBAR is Not Unconstitutional (05/15/2024)

In *Mano v. Yellen, 2024 WL 1988834* (7th Cir. May 6, 2024), *aff'g*, 2023 WL 4943745, 132 AFTR2d 2023-5399 (S.D. Ind. 2023), the Seventh Circuit affirmed a district court decision that the law requiring that taxpayers file FBAR to report ownership of certain foreign financial accounts, and the provisions imposing civil monetary penalties for violations of the reporting requirement, do not violate the taxpayer's rights under the Fourth, Fifth, Ninth, and Tenth Amendments to the U.S. Constitution.

STATE AND LOCAL TAX

New Jersey: The New Jersey Division of Taxation has updated its guidance regarding the tax forms and withholding requirements that are required when real property is sold in New Jersey. The guidance applies to both residents and nonresidents of New Jersey although withholding is only required from nonresidents. Withholding is required at the higher of 10.75% of the net gain from the sale of the property or 2% of the consideration. (New Jersey Division of Taxation Technical Bulletin No. TB-57(R), 01/30/2024.)