Cryptocurrency

• What is it? How did it start?
• Isn’t it only for tax cheats?
• Is it here to stay?
• How are transactions reported?
• What guidance has been issued?
• What are the IRS’ top concerns?
Cryptocurrency – What Is It?

• A medium of exchange using cryptography to secure transactions
• Digital asset using blockchain technology
• Bought and sold on exchanges
• Uses decentralized control instead of centralized electronic money and banking systems
Cryptocurrency – How Did It Start?

- 1970s - Military and spy agency use
- 1990s - Cypherpunks believed that cryptography would promote social change and ensure privacy, anonymity
- 2008 - Bitcoin was released as a peer-to-peer electronic cash system
Cryptocurrency – How Did It Start? (con’t.)

• May 22, 2010, Laszlo Hanyecz bought two Papa John’s pizzas for 10,000 Bitcoins. Today, those two pizzas would have been sold for over $60 million!
Cryptocurrency – Fad or Here to Stay?

- Nearly 2,000 types of cryptocurrencies
- Over 100,000 businesses accept Bitcoin – Expedia, Overstock, Home Depot, Whole Foods, Lowes, Regal Cinemas, etc.
- Ohio Department of Revenue accepts digital currency
Cryptocurrency – Fad or here to stay? (con’t.)

• 18 states have blockchain legislation

• Stanford, UC Berkeley and UCLA have blockchain classes

• But, Deloitte analysis found only 8% of 86,000 blockchain projects launched on the GitHub platform had a lifespan over about one year.
IRS Guidance – Civil Compliance

• IRS Notice 2014-21

• Virtual currency is recognized as property

• Gain or loss on sale is treated like a sale or exchange of securities

• Basis is the FMV on date received

• If held as investment property, the gain or loss on sale is capital in nature
• Inherited cryptocurrency has the cost basis of the decedent

• Cryptocurrency paid as wages is subject to Federal tax withholding

• Cryptocurrency payments are subject to information reporting (e.g. Forms W-2, 1099, 1042 – Misc., etc.)
IRS Guidance – Unresolved Issues

• IRC Section 1031 – Like-Kind Exchanges
  – Prior to 1-1-2018, may be able to argue like-kind exchange for crypto-to-crypto trades
  – After 1-1-2018, like-kind exchanges must involve real estate
• Hard Forks – Is it a taxable event when a coin splits into two or more virtual currencies with a shared history?
• Accounting for gains and losses - FIFO or LIFO? Do taxpayers have the option?
# IRS – Forms Update

- Civil Installment Agreements and Offers in Compromise

**Fillable Form**

<table>
<thead>
<tr>
<th>Virtual currency</th>
<th>Name of virtual currency wallet, exchange or digital currency exchange (DCE)</th>
<th>Email address used to set-up with the virtual currency exchange or DCE</th>
<th>Location(s) of virtual currency</th>
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Current market value in U.S. dollars as of today

\[ \text{Value} \times 0.8 = \text{Value} \]

Total investment accounts from attachment. [current market value minus loan balance(s)]

\[ = (2c) \text{ Value} \]

\[ = (2d) \text{ Value} \]
IRS – Possible Civil Penalties

- IRC 6662 – Accuracy-Related Penalty
- IRC 6663 – Civil Fraud Penalty
- IRC 6721 – Failure to File Correct Information Returns
- IRC 6722 – Failure to Furnish Correct Payee Statements
- Reasonable Cause Defense
Financial Crimes Enforcement Network (FinCEN) Guidance

• 2013 - Money transmitters must register as Money Service Businesses (MSBs)

• MSBs must register, report, and follow BSA and other rules including Suspicious Transaction Reports (STRs) and Currency Transaction Reports (CTRs)
Financial Crimes Enforcement Network (FinCEN) Guidance (con’t.)

• A “User” obtains virtual currency to purchase goods or services. Not an MSB.
• An “Exchanger” trades virtual currency for other currencies. May be an MSB.
• An “Administrator” issues virtual currency and authorized to redeem virtual currency. May be an MSB.
Financial Crimes Enforcement Network (FinCEN) Guidance (con’t.)

• March 2018 – Regulations apply to the sale of Initial Coin Offerings (ICO)-derived cryptocurrencies

• April 2019 – First enforcement action against Eric Powers as peer-to-peer exchanger for willful failure to honor FinCEN obligations
IRS v. Coinbase

• In 2017, Coinbase (America’s largest platform for exchanging Bitcoin to U.S. dollars) had 5.9 million customers and served $6 billion exchanges in Bitcoin

• Only 800-900 taxpayers filed IRS Form 8949
• In November 2017, the U.S. District Court for the Northern District of California ordered Coinbase to produce documents on 14,000 customers who had at least $20,000 in any one transaction in one year between 2013 and 2015
IRS Issues Letters

Letter 6174 – May have duty to report; no response required

Letter 6174-A – May have reporting error; no response required

Letter 6173 – Response under penalties of perjury
IRS – Criminal Investigation Division

- CI employees now complete cyber training
- Belief the future of white collar crimes will have a cyber component in them
- Joint Chiefs of Global Tax Enforcement (J5)
- Challenges with prosecution
What to do?

- Show me the (digital) money!
- Correctly report transactions
- IRS Domestic Voluntary Disclosure
- Qualified amended returns
Questions?