

# Cryptocurrency Taxation

March 26, 2018

With the individual tax filing deadline approaching it is a good time to visit the tax treatment of your bitcoin and other cryptocurrency transactions from 2017.

With the increase in publicity and use of cryptocurrencies, the IRS will be questioning the reporting of cryptocurrency transactions so it is important for taxpayers to correctly report any income related to cryptocurrency transactions. It is crucial for taxpayers to keep records of their cryptocurrency transactions - The taxpayer should keep track of the dates and value when cryptocurrency is purchased, mined, received as payment for goods or services, sold or traded in order to track the taxpayer's basis and any income earned and properly report any associated gain or loss.

The IRS treats cryptocurrencies as "property"- not currency. This means that cryptocurrency is treated in the same manner for tax purposes as if the taxpayer held stock.

Mining The IRS treats the value of cryptocurrencies obtained through mining activities as taxable income in the year received. If the mining is a trade or business, the taxpayer should be able to deduct associated direct expenses to reduce the taxable income earned from the mining activities.

1031 Exchanges The Tax Cuts and Jobs Tax Act of 2017 eliminated the availability of 1031 exchange treatment for personal property exchanges (limiting 1031 availability to real property exchanges). In a 1031 exchange a taxpayer is allowed to defer gain recognition on the exchange until the replacement property is later sold, and the taxpayer's basis in the exchanged property carries over to the property received. For 2018 the exchange of one cryptocurrency for another can no longer be claimed as a tax free exchange under Tax Code §1031. For 2017, the usage of §1031 may still be available for a taxpayer to defer gain on sale transactions.

Sales / Exchanges If a cryptocurrency is converted to cash the transaction results in gain or loss to the taxpayer in an amount equal to the cash received over the taxpayer's basis in the cryptocurrency. Because cryptocurrency is treated as property for tax purposes, using a cryptocurrency to purchase goods or services also triggers a gain or loss (if any) in the cryptocurrency. The taxpayer is treated as having "sold" the cryptocurrency in exchange for the value of the goods or services received by the taxpayer. If the value of the goods or services received exceeds the taxpayer's basis in the cryptocurrency, then the taxpayer has



a gain resulting from the purchase transaction. Similarly, if a taxpayer pays a worker or independent contractor in cryptocurrency, the taxpayer would recognize gain if the value of the cryptocurrency at the time of payment exceeds the taxpayer's basis in the cryptocurrency transferred.

Sales of cryptocurrency that are held by the taxpayer less than a year are taxed as regular income and taxed at the investor's income tax rates. If the cryptocurrency is a capital asset to the taxpayer and was held longer than one year, the gain is taxed at capital gains rates. If the taxpayer utilized a 1031 exchange, the holding time for the exchanged cryptocurrency is added to the holding time for the cryptocurrency sold in determining whether the cryptocurrency was held for more than a year.

Stay tuned for more cryptocurrency tax developments. By this time next year, several taxing jurisdictions may be accepting cryptocurrencies in payment of tax bills!



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