

JUN 23, 2019

By Robert W. Wood

Bitcoin Prices Could Make Paying Taxes in Bitcoin Even More Attractive



EXPERT TAKE

Robert W. Wood is a tax lawyer representing clients worldwide from the offices at Wood LLP in San Francisco. He is the author of numerous tax books and writes frequently about taxes for Forbes, Tax Notes and other publications.

The views and opinions expressed here are solely those of the author and do not necessarily reflect the views of [Cointelegraph.com](https://cointelegraph.com). This discussion should not be regarded as legal advice.

[Bitcoin](#) and other crypto prices have recently been highly volatile. If you are holding bitcoin or other crypto, you may well not want to sell until the market recovers, when it is down. But if you owe [taxes](#) and the crypto market is up, how about paying them in bitcoin (or selling bitcoin to pay your tax in dollars)?

Selling may trigger tax losses that can be used next year, too. And in at least one American state, paying tax in bitcoin is a reality. In Ohio, you can now make state tax payments in bitcoin. It's only possible to pay in bitcoin, at present, but the permitted crypto should expand, according to OhioCrypto.com.

Ohio beat out others in the United States, such as Arizona, Georgia, Utah and New Hampshire, where efforts to accept crypto for taxes failed. The transaction fee is zero during an initial three-month introductory period and then 1% thereafter. Even if you owe taxes to Ohio, that does not necessarily mean you qualify.

So far, this is just for businesses operating in Ohio. If you operate a business in Ohio and have a tax bill, you can register at OhioCrypto.com. All payments are processed by third-party processor [BitPay](#). Payments are converted to dollars before their deposit into a state account.

Of course, it's important to remember the only big missive the U.S. Internal Revenue Service ([IRS](#)) has given about crypto. Way back in 2014, [the IRS ruled that cryptocurrency is property in Notice 2014-21](#). That classification as property has some big tax consequences, accentuated by wild price swings.

Volatility implications

If you owe \$10,000 in taxes, you could pay the \$10,000 in U.S. dollars. If you pay with \$10,000 worth of bitcoin, as long as the crypto is worth \$10,000 when you pay, you're home free, right? Not really. You need to consider the sale you just made.

The transfer of the crypto to the tax man is a sale, and that could mean more taxes for the year of the payment. If you bought the crypto for \$10,000 the day you pay your taxes, there's no gain. But suppose you bought the crypto a year ago for \$1,000 and it's worth \$10,000 when you use it to pay taxes? That's right, you have a \$9,000 gain.

Hopefully, it is a long-term capital gain, which would make the taxes lower, at least for federal tax purposes. Remember, [California taxes ordinary income and capital gain](#) at the same high tax rates. So even capital gain does not save you tax money in California, except for being able to apply your basis. That is, when you sell a capital asset, you should not have to pay tax on the money you used to invest.

If you actually tax in crypto, or sell crypto to pay tax in dollars, you still have taxes to pay — because of your tax payment. You could trigger a tax loss too, if you had bought the crypto for \$7,000 and transfer it for taxes when it is worth \$5,000. These days, a sale might well trigger a loss, which you may be able to use.

With crypto, of course, all sorts of transfers can trigger taxes. For example, payments using digital currency made to independent contractors are taxable transactions to both parties. The recipient has income measured by the market value at the time of receipt. Then, there are the reporting mechanics, which continue to be a big issue for many people.

Reporting taxes in crypto

If you are paying independent contractors with crypto, how do you report it? As with other payments to independent contractors, payers engaged in a business must issue [IRS Form 1099](#). You can't enter "1,000 bitcoins" on the IRS Form 1099.

Instead, you must value the payment in dollars, as of the time of payment. In short, a payment made using digital currency is subject to Form 1099 reporting just like any other payment made in property. What's more, the person paying the independent contractor with crypto just sold it. Whether that triggers a gain or loss depends on the payer's tax basis. The gain might be capital or ordinary. If you hold it for more than a year, the best deal is long-term capital gain treatment.

But actually, gain or loss depends on whether the digital currency is a capital asset in your hands. Most people can probably say they are investors in crypto, not a dealer or someone using it in their trade or business. But it is worth considering. Ordinary income vs. long-term capital gain treatment can spell a big difference. You might have to pay only 15% (to the IRS) on long-term capital gain. But the top long-term capital gain rates are 20%, plus the possibility of the 3.8% net investment income tax under the Affordable Care Act.

Remember, every time you transfer crypto, you might trigger a gain or loss. The tax basis and holding period are important, as is record-keeping. If you receive digital currency as payment, you must include its fair market value as income. Report the fair market value in U.S. dollars on the date you receive it. If you "mine" digital currency, you have income from [mining](#), and the fair market value of what you produced is income. Happy planning.