



Robert W. Wood

THE TAX LAWYER

TAXES 9/8/2017

Bitcoin, Virtual Currency Deals Under \$600 Could Become Tax Exempt

The IRS is hunting digital currency users, since very few people seem to be reporting their transactions. The IRS is using [John Doe summonses to obtain data on bitcoin and other digital currency users](#). The IRS is even hunting [bitcoin user identities with software](#). IRS scrutiny is causing many people to worry that they may owe taxes, penalties and interest. Even worse, in extreme cases, the IRS could pursue tax scofflaws criminally. However, help could be on the way. A [bipartisan bill](#), "The CryptoCurrency Tax Fairness Act," was introduced in the House by [Rep. Jared Polis \(D-Co\)](#) and [Rep. David Schweikert \(R-Az\)](#).

It calls for a tax exemption for transactions under \$600. If it passes, it might be a little bit like foreign bank accounts that in the aggregate have less than \$10,000 at all times during the year. Despite the IRS's obsession with offshore bank accounts, those little accounts are exempt from FBAR reporting (but you still have to report any earnings from the small account on your taxes).



However, the CryptoCurrency Tax Fairness Act would go further. Remember, the IRS announced in [Notice 2014-21](#) that bitcoin and other digital currency is property for tax purposes, *not* currency. That means gain or loss from the sale or exchange of virtual currency depends on whether the virtual currency is a capital asset in your

hands. And every time you buy something is a trade. A payment made using virtual currency is [subject to Form 1099 reporting](#) too. Wages paid to employees using virtual currency are taxable, must be reported on a [Form W-2](#), and are subject to federal income tax withholding and payroll taxes.

If you pay someone in property, how do you withhold taxes? You pay the employee some cash and some bitcoin and withhold plenty on the cash. Or you sell some of the bitcoin to get dollars to pay the IRS. Virtual currency payments to independent contractors are taxable, and payers must issue [Form 1099](#). You can't enter "1,000 bitcoin" on the 1099. You must value it in dollars as of the time of payment. Valuation swings can be brutal. So under the bill, any transaction under \$600 would be completely exempt. It would mean not having to worry about keeping track of gains on small transactions. Plus, the bill calls for the Treasury Department to provide guidelines for reporting on profits and losses tied to digital currencies.

As the IRS and Coinbase fence over user records, it is worth remembering that the IRS used a John Doe Summons to get names of Swiss bank account holders from UBS. After that, offshore banking changed forever, with all other Swiss (and other) banks eventually coming clean. The IRS ended up [collecting over \\$10 billion](#). The IRS pursued Coinbase in the same way. Small fries may be OK, though. The IRS agreed to limit its request for customer records from Coinbase to accounts with transactions [over \\$20,000](#). Beyond that, the IRS will clearly do more data mining for digital currency users.

[After all, reports](#) underscore the IRS claims that only 802 people declared a capital gain or loss related to bitcoin in 2015. With millions of transactions, 802 taxpayers reporting in 2015 seems, well, small. This suggests that the bulk—the vast bulk—of bitcoin transaction are not reported. But in 2017, there may be more awareness, and more fear. The estimated value of the cryptocurrency economy is something on the order of \$162 billion. With millions of transactions and the meteoric rise of bitcoin from under \$100 to over \$4,000 in just a few years, the IRS is gearing up.

The *Daily Beast* revealed the Chainalysis software [contract](#) to identify owners of digital wallets is now part of IRS enforcement. Taxpayers who have hidden income could face taxes, and potentially big penalties. But the record keeping and gain and loss determinations can be dizzying. If this bill passes, many transactions would be in the clear. That would be welcome news for the digital currency community.

For alerts to future tax articles, email me at Wood@WoodLLP.com. This discussion is not legal advice.