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## Cryptocurrency Loans: Are They Loans for Tax Purposes? Expert Blog



### EXPERT TAKE

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When you borrow money, it is not income for tax purposes because you have to pay it back. When you lend money, you get no tax deduction or other taxable event. You just changed your money into a promise that the borrower will pay you back. So, to the IRS not much has happened.

Sure, there may be interest paid or interest received. Plus, if you are relieved of the obligation to pay *back* a [loan](#), that *is* income in the amount of the debt forgiven. Mostly, though, loans can be neutral from a tax viewpoint. How about loans in [Bitcoin](#) or other digital currency?

## Loans and taxes

That's not so clear. With loans in dollars, money is fungible. When you receive a loan in cash, the lender usually knows that you will invest or spend the money. Everyone understands that you will pay the lender back with *other* money. But the IRS says cryptocurrency is property.

Say you lend your car to another person. If the borrower returns a *different* car, that transaction could be viewed as the sale of the original vehicle, rather than a loan of the vehicle for tax purposes. If you end up with a different car, the IRS might say that was a *sale* of the car, followed by the purchase of another car.

The IRS likes finding more chances to tax something! That can mean gain or loss, even if the deal ends up netting you a different car with the same value. Except for certain special tax provisions such as Section 1031 exchanges that allow tax-free swaps of property under certain conditions, just about *everything* you trade is taxed.

## Bitcoin is property, not currency?

In 2014, the IRS [issued a Notice](#) saying that digital currency like Bitcoin is property, *not* currency. Most property is not fungible for tax purposes. With loans of cryptocurrency, the parties probably *intend* the cryptocurrency lent to be treated as fungible currency, rather than like property. For example, a borrower may receive Bitcoins and then sell them.

He may repay the lender with different, newly acquired Bitcoins. The Bitcoins are intended to operate as fungible currency so that the repaid Bitcoins are considered a continuation of the Bitcoins that were lent (with the same tax basis and the same acquisition date). But will the IRS agree? No one seems to know the answer to this question.

## Risks

Despite the parties' intentions, the IRS may not agree that this is just a loan. Think about the fluctuating value of cryptocurrency and these tax issues could be big. There is a risk that the IRS will view Bitcoins received in repayment of a loan as *different* Bitcoins than the Bitcoins lent. So a loan could end up as a sale to the IRS.

Moreover, even if the IRS agrees that loan treatment is appropriate, it is not clear how interest payments will be treated. It might be wise to emphasize in any documents that the transaction is *intended* to be a loan, not a sale or disposition. You could also document clearly that both parties will report the loan in this manner for tax and accounting purposes.

If the transaction has any profit sharing or equity provisions, that could complicate the argument for loan treatment. Another concern is fungibility. The loan documentation could emphasize that repayment should be made in digital currency that is *identical in value and denomination* (i.e., Bitcoins for Bitcoins, Ripples for Ripples, etc.) to the digital currency lent. Perhaps the document could even require that repayment be made with the *exact same* cryptocurrency lent.

In practice, this may not be possible, of course. Still, a requirement that the loan repayments be made from the same wallet to which it was lent (and ideally one segregated from other funds) might help strengthen the argument that the very same property has been repaid.

## Against all challenges

It isn't clear what is the best strategy. Some parties may want to emphasize in loan documentation that the cryptocurrency is a fungible asset. Perhaps they want to state that the cryptocurrency received in repayment will be considered identical to the cryptocurrency lent (that will use the same acquisition date and tax basis).

Loan documentation might also distinguish between transfers made in repayment of loan principal and transfers as payments of interest. The IRS may have a stronger hand to argue against loan treatment if the transaction history is muddled, such as where it is not clear which payments are for interest and which are for principal. The loan documentation could spell this out.

But making sure that principal and interest payments are made according to the procedures in the loan documentation may help too. A loan transaction that began with Bitcoin might become even more problematic when the lent funds are now represented by both Bitcoin and [Bitcoin Cash](#). Parties should anticipate what to do in these circumstances, and consider how to emphasize in the loan documentation that repayment is still being made from the same source and property.

Taking steps of this sort may not prevent the IRS from successfully challenging an intended loan. Even so, it may help put you in a better position in case the loans are examined.

*Disclaimer: This article is adapted from one appearing on Forbes.com. This discussion is not intended as legal advice and does not necessarily represent the views of the Cointelegraph.*

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