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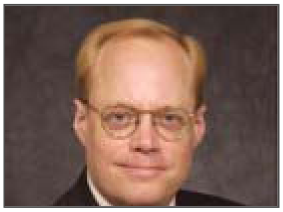

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Finding Lost Bitcoin Could Mean IRS Finds You

The bankrupt Japanese Bitcoin exchange MtGox discovered over 200,000 lost Bitcoins valued at over $116 million. The coins apparently showed up in an old Bitcoin wallet format. MtGox's CEO said he thought it no longer contained any Bitcoins. This is good news in a bankruptcy filing, of course, and would be good news for anyone. You can see the bankruptcy disclosure here.

There's no tax issue for MtGox, of course, but there could be for someone else who finds Bitcoin or anything else of value. Imagine finding millions in your old jeans pocket! Under U.S. tax law, if you find something it is generally income unless you can show it was rightly yours all along. And that can be the rub, whether it's cash or art or anything else.

Bitcoin Wallpaper (2560×1600) (Photo credit: PerfectHue)

If you get back your *own* money or property, it generally shouldn't be income. After all, you are just getting back what you owned. As you remain the rightful owner of it, you don't have income for tax purposes, even if the item has appreciated in value during the hiatus. Happily, that means the IRS can't tax it.

However, even if you are getting your *own* property back, if you claimed a tax loss when you lost it, beware. You may have to report the item as income when you recover it. Under the tax benefit rule, since you claimed a tax benefit, you must take the item back into income when you recover it.

This tax benefit rule can be tricky, since your tax benefit might not have saved you much if any on your taxes. In short, it can seem punitive. From lost loot, Nazi art, and lost gold coins, finding something can bring surprise tax problems, even if getting back your property is gratifying. The tax result can be unexpected and even downright distressing.

The worst tax position is if you didn't own it to begin with–or can't prove that you did. You have found what the IRS appropriately enough calls treasure trove. Remember the anonymous couple in California's gold country who found $10 million in rare gold coins buried in cans on their property?

They made the biggest and best coin discovery in U.S. history. So said Davis Hall of Professional Coin Grading Service. Walking their dog, the couple dug up a protruding rusty metal can. Lo and behold, it contained 1,400 rare U.S. gold coins from 1847 to 1894. Their face value was more than $28,000, and their market value was said to be over $10 million.

Most tax experts agreed that is all income to the couple–the full $10 million, not just the $28,000 face value. Approximately 90% of the coins will go up on Amazon.com's "Collectibles" site. The couple said they plan to keep some of the coins and sell others, donating part of the proceeds to charity.

Treasure trove is just one example of the astounding breadth of what is income for U.S. tax purposes. The most famous case on treasure trove is Cesarini v. United States, 296 F. Supp. 3 – 1969. Mr. Cesarini bought a used piano for $15 and found nearly $5,000 in cash inside.

Imagine his surprise and delight over such good luck! But then the IRS said it was taxable income. Mr. Cesarini went to court over it, but the court agreed with the IRS. Mr. Cesarini appealed, but the 6th Circuit Court of Appeals agreed too. See Cesarini v. United States, 428 F. 2d 812 – 1970.

Sure, finding something is great, but after the euphoria wears off, consider taxes. The IRS sure does.

You can reach me at Wood@WoodLLP.com. This discussion is not intended as legal advice, and cannot be relied upon for any purpose without the services of a qualified professional.