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IRS Takes A Bite Out Of Bitcoin

Bitcoin is virtual currency much in the news these days. It's peer-to-peer so there's no central bank or government. But if you think that means the IRS won't get a piece, think again.

The IRS already gets a piece where you swap one product or service for another, as the IRS explains at its [Bartering Tax Center](#). Soon the IRS may have a Bitcoin Center too. The Treasury unit called FinCEN, the Financial Crimes Enforcement Network, already has rules about Bitcoin and the IRS is likely to follow.

In the meantime, the tax rules seem pretty clear. If you provide services or sell goods for Bitcoin, you have income. If you exchange Bitcoins for cash, whether you have gain may depend on whether Bitcoin is really currency or commodity. The latter seems more likely, meaning you have gain to the extent of the appreciation in your Bitcoin.

Income is income, whether you get it in cash or in kind. Bitcoin may be accepted as currency and may not be easy to trace but so are trades and barterers. When you barter or swap one item for another, both parties have tax consequences. That's so even if one party wants credit for later.



The bitcoin logo (Photo credit: Wikipedia)

Trade or barter dollars allow you to barter when one party wants goods or services and the other wants credit for the future. Earning trade or barter dollars through a barter exchange is considered taxable income, just as if your product or service was sold for cash. And even trades are still taxed.

Plumbing for dental work? The IRS taxes it. You name the swap, it's income to both sides just like cash. Both must report the fair market value of goods or services received on their tax returns. See [Do You Barter? The IRS Wants Its Cut](#).

Most casual barter exchanges probably aren't on the tax radar. Most Bitcoin transactions aren't either. But even simple trades trigger multiple tax rules. If you receive \$1,000 of dental work for your gardening services, you have \$1,000 of income.

If you swap your wristwatch for a painting, it's two separate taxable transactions. Say you inherited the watch from your uncle when it was worth \$5,000. If it's doubled in value to \$10,000 and the painting is also worth \$10,000, you have \$5,000 of income. ([Section 1031 exchanges](#) of some business and investment property can be tax-free, but that's no help here.)

How will the IRS know about your swap? They probably won't unless you receive a [Form 1099](#). Still, the IRS says you must report any income on your return regardless of whether you receive a Form 1099. See [IRS Form 1099: God Particle Of The Tax System](#).

The FinCEN rules say Bitcoin exchanges and Bitcoin miners should register as Money Services Businesses (MSBs) and comply with anti-money laundering regulations. Ordinary Bitcoin users don't have to register just to purchase goods and services. But will Forms 1099 and other nettlesome signs of civilization soon bite Bitcoin? Yes, and probably soon.

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