

US perspective: Bitcoin reporting and the taxman

Even though Bitcoin has been present as a cryptocurrency for almost 10 years, there are still few Internal Revenue Service (IRS) regulations on the digital payment system. Mike DeBlis, partner at DeBlis Law explains the implications around reporting Bitcoin for Foreign Bank Account Report (FBAR) purposes

In the US, as elsewhere in the world, many lawyers are borderline technophobes.

28 Jun 2017

In 2014, Chief Justice John Roberts wrote that the Supreme Court still used vacuum tubes to distribute messages long after these systems became available in Washington-area yard sales.

'Judges and court executives are understandably circumspect in introducing change to a court system that works well until they are satisfied that they are introducing change for the good,' he reasoned. That analysis is basically Lawyer speak for 'judges don't like technological innovation.' There may be some basis for that attitude, albeit not much.

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For the same reason that many lawyers pine for the good old days when their laptops had A-drives, the law is usually well behind technology, and Bitcoin is an excellent example. Although the crypto-currency has been around for almost a decade, there are very few IRS regulations on the subject and almost no guidance whatsoever when it comes to foreign bank accounts.

Moses has not come down from the mountain with anything definitive, and for a while it seemed like the IRS might believe that regulating Bitcoin for FBAR purposes might be more trouble than it's worth. But a recent decision from a California federal judge might be a game-changer.

Assets and Income

Most of us rightly think that money is money and it does not matter if the money is tied up in a land investment deal or stuck between the sofa cushions. However, most of us do not work for the IRS, and to these bureaucrats, there may be a difference.

Currently, the IRS classifies Bitcoin as a capital asset, as if it were a precious metal or corporate stock. There is some consistency there, as gold and silver bars, no matter how big they are, buy nothing at Walmart. Just like foreign account holders do not have to report precious metals in offshore safe deposit boxes, taxpayers also do not have to report Bitcoin in virtual wallets.

That was the view that IRS analyst Rod Lundquist espoused in June 2014, a date that seems like light-years ago now. Speaking at a conference at the time, Lundquist said 'virtual currency is not going to be reportable on the FBAR, at least for this filing season.' In legal terms, this pronouncement has exactly zero effect, but it does offer insight into the IRS's attitude toward crypto-currency.

There is another caveat as well, in terms of the type of account. To return to the precious metals analogy, gold and silver exchange accounts are reportable on the FBAR, because if the taxpayer has a ready way to convert assets into income, the IRS wants a piece of the action. The same thing applies to Bitcoin exchange accounts. If the taxpayer can convert assets into income with almost literally the click of a mouse, the account is definitely reportable.

Current thought

A lot has happened since 2014. The Cubs won the World Series, American Idol breathed its last breath, there was that whole election thing, and an obscure federal judge ordered a virtual currency exchange in San Francisco to hand over information to the IRS. Earlier, the IRS had served a 'John Doe' subpoena on Coinbase, seeking information about people who might have violated US tax law. Why did the Service go sniffing around a Bitcoin exchange that, according to its own rules, may not have contained taxable income?

Predictably, there was a method to the madness. The explosive growth in the crypto-currency sector has created ‘questions about tax compliance,’ according to Deputy Assistant Attorney General Caroline D. Ciraolo.

IRS Commissioner John Koskinen dropped this potential bomb: ‘Transactions in virtual currency are taxable just like those in any other property.’ Since the Commissioner did not use the i-word (income), he may have been referring to the existing rule regarding Bitcoin exchanges or, his pronouncement may signal a more assertive stance. The whole IRS scene is very fluid right now.

According to various reports, Commissioner Koskinen, whom some Republicans tried to impeach last year, may be on his way out. What a new Commissioner would do about the Bitcoin/FBAR rules, if anything, is a matter of reading the tea leaves.

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This article first appeared in Global Tax Weekly, No. 224, published 23 Feb 2017. © Wolters Kluwer (UK) Limited

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