VIEWS & VISIONS

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The best example I can share for this is, imagine your title company wants to ensure you have clear title to your property. In addition to searching every grantor and grantee the title company can find regarding your deed, the title company also must verify EVERY transaction on record for EVERY property in the United States before starting on yours. This is a rough analog for how the blockchain and its participants are continually building security onto a blockchain, thus preventing any single user from changing or erroneously recording information into the ledger.

Bitcoin is one of the first users of the blockchain, and new tokens and currencies are being developed every day. New companies have formed to build a nexus between currencies and software, effectively allowing tokens to be issued with specific utility baked into it. The most popular currency supporting these "smart contracts" is Ethereum, a platform that a company can use to issue their own token. These tokens can be used to raise funding, pay for services or represent some sort of action specific to the company.

Many startup companies are using this idea to create Initial Coin Offerings (ICO) and Security Token Offerings (STO). By issuing their own tokens, investors or users can buy directly from the company and hold the tokens in electronic wallets. As this concept gained momentum, regulators also took an interest and started to issue guidance regarding how these tokens can be used, and under what conditions individuals and companies must report, register and disclose their use.

The relationship between cryptocurrency and blockchain has started an "uprising" of its own. They are revolutionizing the way businesses and users think about how information is stored and currency is traded, presenting an endless frontier for businesses and investors to explore. V

Cryptocurrency and Taxes: Don't Get Stuck with the "Do Not Pass Go" Card

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For those who are not well-versed in the world of cryptocurrency, it may seem a lot like Monopoly money. And, like Monopoly, at some point every player lands on the "Income Tax" space of the gameboard.

While cryptocurrency may seem like "play" money, transactions of cryptocurrency are taxable events. In 2014, the IRS issued guidance on virtual currencies, defining cryptocurrencies as anything that is considered a "convertible virtual currency," meaning it has an equivalent value in real currency. Cryptocurrency under the IRS guidelines is treated like property rather than an actual currency. Therefore, the gains and losses should be tracked and reported as such.

Unless a virtual currency investor has realized a gain of over $20,000 and had at least 200 transactions, the transactions are not reported on an IRS Form 1099-K by a third-party settlement organization. Therefore, the cryptocurrency patron must self-report.

Because cryptocurrency is treated much like stock and real property, investors should track their basis to determine the capital gains and losses. However, with the nature of virtual currency trades, tracking virtual currency can prove difficult. Therefore, a "first in, first out" method of tracking is suggested.

There are some transactions in which cryptocurrency is treated as ordinary income. For example, if a person receives cryptocurrency as payment for services, salary or a product. Cryptocurrency acquired through air drops and mining is also considered ordinary income and should be reported as such.

The IRS has increased its investigation of unreported virtual currency transactions. To stay out of the crosshairs of the IRS, keep detailed records and be forthcoming with all virtual currency transactions. As stated above, the IRS has only issued guidance and not regulations, but the guidelines do address penalties, including fines and possible criminal prosecution. So, unlike Monopoly, there is not a "Get Out of Jail Free" card.

Alison A. Cox is an attorney in the Martinsburg, West Virginia office of Bowles Rice. As a member of the firm's Tax Team, her practice focuses on assisting individuals and business owners with matters related to estate planning and administration, wills, trusts and elder law.