



## WHITE PAPER

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### Blockchain and Tax: Navigating Uncertainty

Virtual currencies (often called cryptocurrencies) such as bitcoin are perhaps blockchain's best-known application. As these and other blockchain-based digital assets become more common, and attract more regulatory and legislative attention, it will be crucial to keep up with the latest guidance—particularly given the often counterintuitive consequences of transacting with cryptocurrency for tax purposes. Since current tax law is limited to a single statement of sub-regulatory guidance published in 2014, however, taxpayers presently have more questions than answers.

This Jones Day *White Paper* will discuss briefly the technical and legal background of blockchain technology and cryptocurrencies, highlight key issues under the current (limited) tax regime for cryptocurrencies, and identify selected open issues that are creating some of the most uncertainty for taxpayers.

## TABLE OF CONTENTS

TECHNICAL BASICS .....	1
The Basics of Blockchain Technology .....	1
The Basics of Cryptocurrency .....	1
LEGAL BACKGROUND .....	1
The Concept of Convertible Virtual Currency .....	1
IRS Notice 2014-21: Cryptocurrency as Property .....	2
Acknowledging the Need for Guidance .....	2
KEY INCOME TAX ISSUES .....	3
Currency-Like Transactions with Property Results .....	3
Forks and Questions of Convertibility .....	3
OTHER POINTS OF INTEREST .....	5
Initial Coin Offerings .....	5
Mining Pools and Partnership Law .....	5
CONCLUSION .....	5
ENDNOTES .....	6
LAWYER CONTACTS .....	6

## TECHNICAL BASICS

### The Basics of Blockchain Technology

Blockchain is, at its essence, simply a method of recording peer-to-peer transactions. A network of computers simultaneously run blockchain software. These computers, called nodes, each keep their own copy of a digital ledger, or database, recording all user transactions on the network.

The basic unit of a blockchain, a “block,” is a collection of transactions between peers on the network. Each new transaction is broadcast to all nodes in the network. Nodes collect broadcast transactions until they have enough to make a block, as determined by the blockchain’s protocols. Once a node has collected a block, that node performs computational “work” searching for a special numeric value. The first node to discover the value wins the right to broadcast its block to all the other nodes in the network, which in turn add that block to their ledger. The process of compiling blocks, performing computational work, and broadcasting blocks back to the network is referred to as “mining.”<sup>1</sup>

At this point, the other nodes check the accuracy of the broadcast block against their own digital databases. If all the transactions match, the other nodes accept the broadcast block as complete. That completed block then becomes the starting point for the next collection of transactions. For the nodes to accept the next broadcast block, the block must contain both accurately validated transactions *and* proof that its calculations started from the last completed block. Every subsequent block is thus “chained” to the previous one by the confirmation of every prior block in the chain.<sup>2</sup>

### The Basics of Cryptocurrency

The first and probably best-known use of blockchain technology is virtual currency (i.e., cryptocurrency or digital currency). Bitcoin, the first decentralized cryptocurrency, uses blockchain to allow users to pay one another with electronic “coins.”

Every user in the bitcoin network has two “keys”: a public key and a private key. The entire network knows a user’s public key, while only the user knows its own private key. When a new transaction is broadcast to the network, that transaction is encoded and “signed” by the originator’s private key. Other

nodes use the corresponding public key to decode the transaction, so only transactions originating from a user’s private key are validated.<sup>3</sup> Thus, to transfer a coin, the current owner uses its private key to sign a transaction giving the coin to another user. The nodes decode the transaction with the public key and record the coin as transferred to the recipient in their next block.

Active mining is necessary to maintain the integrity of a blockchain.<sup>4</sup> Because mining can require an immense expenditure of resources (i.e., processing capacity, electricity), most cryptocurrencies have an internal incentive system. With bitcoin, for example, the user whose completed block is accepted by the network receives a set amount of new coins, called a “block reward,” as payment for helping maintain the blockchain.

## LEGAL BACKGROUND

### The Concept of Convertible Virtual Currency

Bitcoin first became available in 2009. Ten years later, more than 2,000 individual cryptocurrencies are listed on CoinMarketCap, which tracks non-zero trading volume cryptocurrencies on public exchanges.

The U.S. Department of the Treasury’s Financial Crimes Enforcement Network (“FinCEN”) issued interpretive guidance in March 2013 on the applicability of certain (non-tax) regulations to persons using, administering, or exchanging “virtual currencies.” For these purposes, “virtual currency” was defined as “a medium of exchange that operates like a currency in some environments, but does not have all the attributes of real currency”—e.g., virtual currency has no legal tender status in the United States.<sup>5</sup>

FinCEN also distinguished a narrower form of virtual currency, termed “convertible virtual currency” (“CVC”). CVC “either has an equivalent value in ‘real’ currency, or acts as a substitute for ‘real’ currency.”<sup>6</sup> FinCEN’s guidance applies only to CVC.

An important indicator that a cryptocurrency is actually a CVC is its presence on a cryptocurrency exchange. For example, a bitcoin exchange allows traders to buy and sell bitcoin using fiat currencies or other forms of cryptocurrency.

These exchanges generally operate like traditional currency exchanges. This is not only a means for converting cryptocurrency but also an indication that buyers are willing to pay fiat currency for the listed cryptocurrencies.

### **IRS Notice 2014-21: Cryptocurrency as Property**

The Internal Revenue Service (“IRS”) relied on the same concept of CVC when it published Notice 2014-21 (“Notice”) in 2014. The Notice generally describes “virtual currency” as a digital representation of value that functions in the same manner as a country’s traditional currency, borrowing from FinCEN’s definition of “CVC.”<sup>7</sup>

Unlike FinCEN, which generally treated CVC as akin to currency for many purposes of its 2013 regulations, the Notice treats CVC as property. General tax principles used in property (rather than currency) transactions therefore apply to CVC transactions for federal income tax purposes. This can sometimes lead to counterintuitive, and harsh, results for taxpayers.

The Notice provides no guidance with respect to any virtual currencies other than CVCs or any other applications of blockchain technology.

Five years later, the Notice still represents the IRS’s most current (and only) pronouncement on blockchain taxation, notwithstanding the rapid evolution and development of blockchain technologies and proliferation of virtual currencies since 2014.<sup>8</sup> The lack of clear guidance however, has not hindered the IRS’s enforcement efforts. It has, for example, published a “reminder” to taxpayers on the IRS website that failing to report virtual currency transactions could result in penalties and interest and, in some circumstances, criminal prosecution.<sup>9</sup> The IRS has also recently announced that it has specifically identified virtual currency transactions as posing particularly high non-compliance risk among certain taxpayers, and it has therefore initiated a formal compliance initiative (“campaign”) to strategically focus on the audit and enforcement of such transactions.<sup>10</sup> And in 2017, the Department of Justice was granted a petition for the issuance of John Doe summons to a major cryptocurrency exchange for records related to U.S. taxpayers who had conducted virtual currency transactions sought by the IRS. In other words, despite a dearth of much-needed tax guidance, the IRS is actively pursuing initiatives to ensure compliance—and to punish noncompliance.

### **Acknowledging the Need for Guidance**

Multiple private sector and government actors have urged the IRS to publish additional guidance on the tax treatment of cryptocurrencies.<sup>11</sup> In September 2016, the Office of the Treasury Inspector General for Tax Administration (“TIGTA”) issued a report evaluating the IRS’s virtual currency policy. Unsurprisingly, the report recommended, among other things, that the IRS develop a “coordinated virtual currency strategy” and “provide updated guidance” to the public.<sup>12</sup> Various members of Congress have likewise urged the IRS to act, emphasizing the importance of publishing updated guidance so taxpayers are able to comply with the rules.<sup>13</sup>

Congress itself has made at least limited attempts to address the tax implications of cryptocurrency. For example, in 2018, Congressmen Warren Davidson and Darren Soto introduced H.R. 7356, the Token Taxonomy Act (“TTA”). The TTA would have defined “virtual currency” for tax and securities purposes as “a digital representation of value that is used as a medium of exchange and is not otherwise currency under section 988” of the Internal Revenue Code (“Code”).<sup>14</sup> (Section 988 addresses the treatment of certain foreign currency transactions.) The TTA also would have amended Code section 1031 to allow like-kind exchanges of virtual currency, thus permitting taxpayers to defer the recognition of gain on the exchange of one virtual currency for another. Finally, the TTA would have added a de minimis exception from income for up to \$600 from the sale or exchange of virtual currency in a transaction for something other than cash (or cash equivalent).

This push has continued into the 116th Congress. A number of new bills requesting further study of how cryptocurrencies are used by terrorists and traffickers were introduced in early 2019, and the TTA was recently reintroduced in substantially the same form.

The IRS would obviously need to adapt its approach based on the form any such cryptocurrency legislation ultimately takes—especially if it contains taxpayer-friendly provisions of the type contemplated by the TTA.

As congressional intent takes shape and blockchain applications continue to evolve, the IRS will inevitably have to revisit the already-dated Notice. The need for updated and more detailed

guidance on CVC, and virtual currencies and blockchain more broadly, will only become more pressing with time.

## KEY INCOME TAX ISSUES

### Currency-Like Transactions with Property Results

Because of its convertibility and currency-like characteristics, many tend to think of CVC as currency. In light of the IRS's position set forth in the Notice, however, the tax implications of paying or being paid with CVC can differ significantly from those of paying or being paid with a traditional (fiat) currency.

**Paying with Cryptocurrency.** When buying goods with CVC, the purchased property is generally treated as any other purchased property acquired in a sale transaction. The buyer's basis in the purchased property is generally the amount paid for it.<sup>15</sup> The payment of the purchase price with CVC, however, is itself (also) treated as a sale of property, rather than a payment with currency. This causes the transaction to be a property-for-property exchange rather than a cash purchase of property. Consequently, the buyer realizes a taxable gain if the fair market value of the purchased item exceeds the buyer's basis in the CVC used to pay for the item. Conversely, the buyer has a loss if the fair market value of the purchased item is less than the buyer's basis in the CVC.<sup>16</sup> The fair market value of the CVC is determined in U.S. dollars on the date of receipt. If the CVC is listed on an exchange and "the exchange rate is established by market supply and demand," the taxpayer may use that exchange rate to determine fair market value.<sup>17</sup>

For example: A buys B's widget with a fair market value of \$10. If A pays with \$10 cash, A realizes no taxable gain or loss on the purchase transaction. Alternatively, if A pays with CVC valued at \$10 that A acquired on a cryptocurrency exchange last year for \$20, A realizes a \$10 loss from the transaction. (Assume on the date of the transaction the exchange rate for A's CVC was \$10.) If A had instead acquired the CVC for \$5, A would have realized \$5 of gain on the purchase transaction.

**Receiving Cryptocurrency as Payment.** The tax implications of the seller are less surprising—a seller receiving payment in CVC for the sale of goods must use the fair market value of the CVC on the date of the transaction in computing its gain (or loss) from the sale transaction.<sup>18</sup> Consider again B selling the widget to A. If B has an adjusted basis of \$3 in the widget

and the fair market value of the CVC on the sale date is \$10, B has taxable gain of \$7.

Miners must also include the value of any block rewards or transaction fees received in their gross income.<sup>19</sup> If a U.S. taxpayer's mining activities constitute a trade or business, the net earnings from mining constitute self-employment income and are subject to self-employment tax.<sup>20</sup>

**Exchanging Cryptocurrency.** In addition to spending or receiving CVC, a person may exchange one CVC for another, just as one can exchange foreign currency. Unlike exchanging fiat currencies, however, exchanging one form of CVC for another is a taxable event and triggers a gain or loss for the taxpayer.<sup>21</sup> The character of the gain or loss depends on whether the CVC is being held as a capital asset.<sup>22</sup> If the CVC is a capital asset, the taxpayer generally realizes a capital gain or loss on the sale.<sup>23</sup> If the CVC is held as a noncapital asset, the taxpayer instead generally realizes an ordinary gain or loss. Either way, the gain or loss is not considered a foreign currency gain or loss.<sup>24</sup>

Exchanging a CVC for a fiat currency is effectively a sale of cryptocurrency for fiat currency. As with exchanging CVC, selling cryptocurrency triggers a gain or loss for the selling taxpayer. The character of the gain or loss also depends on whether the CVC is being held as a capital asset, and similarly would not give rise to foreign currency gains or losses.

When a taxpayer buys CVC with fiat currency, the transaction is treated as the purchase of property. No gain or loss is generally triggered by this purchase, and the taxpayer's basis in the CVC is the price paid for the CVC.<sup>25</sup>

### Forks and Questions of Convertibility

In addition to actively transacting with CVC, a taxpayer may passively receive a new asset if a CVC's blockchain experiences a "fork." That asset may be new CVC, or it may instead be an asset outside the Notice's scope. Further, depending on market reaction to the fork, the property may have inherent value, be valueless or, as is often the case, have an indeterminate value, at least temporarily.

**The Basics of "Forked" Chains.** All blockchains run software. Like any software program, blockchain software needs to be upgraded from time to time. There are two main types of programming upgrades in the blockchain ecosystem: hard forks

and soft forks. A soft fork is an upgrade that is compatible with older versions. When a soft fork occurs, the protocol changes but the chain is not split into two, and a new cryptocurrency is not created.

A hard fork, on the other hand, is not compatible with older versions. When a hard fork occurs, the original chain splits into two distinct chains. Because a blockchain has no central authority forcing users to accept modifications, some users may instruct their node to reject the modification and continue with the old protocols. Any nodes that accept the upgrade, however, will reject blocks following the old protocols and accept the first broadcast block that complies with the new ones. This results in a new “branch” that has effectively split from the original blockchain and is thereafter separately maintained. Any nodes still running the old version will accept the first broadcast block to comply with the old protocols, forking those nodes away from the nodes with the modification.<sup>26</sup>

In the event of a hard fork, those persons whose ownership of a CVC was recorded on the original blockchain continue to own the original CVC, but they also become entitled to claim a specified amount of the (new) virtual currency maintained on the new blockchain. Hard forks generally create new, distinct cryptocurrencies, such as when Ethereum forked into Ethereum and Ethereum Classic.

Sometimes when hard forks occur, cryptocurrency exchanges choose to continue supporting only one currency and to not host trading of the other. More often, this is a rejection of the new forked currency, leaving the original CVC unaffected. The rejected currency may still be a CVC if there are at least some individuals willing to trade fiat currency for it. In that case, the rejected currency would most likely retain its CVC status, although determining value becomes more difficult. Being shut out from the cryptocurrency exchanges could, however, mean the creation of either a closed-flow virtual currency or a worthless asset.<sup>27</sup>

**Questions of Convertibility and Basis.** There are many questions, and virtually no answers, for the characterization and tax treatment of hard forks and their newly created virtual currencies. The most pressing question is whether the receipt of the new forked currency is itself a realization event and thus

taxable to the recipient. Commentators are divided, and the IRS remains silent. On the one hand, there is often an apparent “accession to wealth” in the sense that the holder, by virtue of owning the original virtual currency, now (also) holds some amount of the new currency, which has—or will have—a distinct, discernable value.<sup>28</sup> On the other hand, the possibility of a hard fork occurring is inherent in virtual currency and, arguably, this prospect is already priced into a virtual currency when purchased. Under this theory, a hard fork would be more akin to nontaxable situations like subdividing a parcel of land, a tax-free distribution of certain stock dividends to an existing shareholder, or the birth of a calf, which is generally not taxable to the cow’s owner.<sup>29</sup>

Assuming, for the sake of argument, that a hard fork is a taxable event, this gives rise to a number of additional, related questions. For example, what is the amount subject to tax? It can be difficult to price virtual currencies, especially newly created ones that have never before been traded and do not yet have a market.

Further, on what date is the taxable event deemed to happen? The receipt of property is not taxable until the recipient has dominion and control over the property.<sup>30</sup> When a hard fork occurs, there can be a (sometimes not insignificant) lag between when the new forked currency comes into existence and when holders can actually access it. For example, there may be affirmative steps that need to be taken (e.g., software upgrades) by the holder or the commercial “wallet” provider maintaining the holder’s digital assets.

Finally, what is the holder’s tax basis in the new forked currency? Presumably, it could be zero since nothing was paid for the new forked currency, or it could be the fair market value of the new forked currency (assuming such value can be determined). Alternatively, it could be some portion of the holder’s basis in the original forked currency, which must somehow be divvied between the holder’s original and new virtual currency.

These open issues are so problematic that multiple professional organizations and even Congress have encouraged the IRS to adopt temporary safe harbors for tax and reporting purposes until formal guidance is published.<sup>31</sup> So far, the IRS has not taken them up on this request.

## OTHER POINTS OF INTEREST

Two other points of interest with uncertain tax implications are initial coin offerings (“ICO”) and mining pool organization. Both are areas for which there is no formal guidance, and a case-by-case analysis is required to (try to) determine the tax consequences, usually by analogy to an unrelated area of tax law.<sup>32</sup>

### Initial Coin Offerings

An ICO is another popular use of blockchain technology. Similar to an initial public offering, an ICO is typically the sale of a “token” representing some rights related to the issuing organization.<sup>33</sup> These tokens, like CVC, are recorded and transferred on a blockchain. While some tokens may be a CVC, or ultimately become a CVC, others are created to provide various rights or represent ownership. For example, tokens may operate as a license, be exchangeable for present or future services, or carry a right to the issuer’s profits.<sup>34</sup> This raises the question of how to classify ICO tokens and, correspondingly, their issuance and receipt for tax purposes. The tax result ultimately comes down to understanding exactly what intangible rights and value the token represents.

The complexity and variety of ICOs has increased dramatically in recent years. The unique properties of individual tokens in different ICOs have made ICOs as a whole increasingly difficult to generalize, especially for tax purposes. Because the term is now used for such a broad variety of offerings, it is crucial for each ICO to be assessed from a tax perspective on a case-by-case basis. The tax treatment of any given ICO token is likely to depend on whether that token represents a CVC, a potential CVC, the right to profit in an established entity or in an entity as yet to be formed (or other equity ownership-type rights), a debt-type obligation, or something else entirely (including, potentially, some combination of the aforementioned rights). All factors must be considered for the individual token in question, in order to best determine the characterization and tax consequences of any given ICO.

### Mining Pools and Partnership Law

A mining pool is generally a coordinated group of miners that aggregate their individual resources. This is increasingly common due to the substantial resource demands involved in mining. In return for sharing their processing power with the pool, miners receive a payout of block rewards earned by the pool.

There are a variety of ways in which a block reward may be distributed, most of which are generally based on proofs submitted to the pool operator evidencing that a node was actually mining for the pool (called “shares”). The simplest mechanism is proportional rewards. Every time the pool receives a reward for mining a block, every node that submitted shares for the block receives a proportional payment from the block reward. Another popular method is the Pay-Per-Share (“PPS”) mechanism, in which nodes receive payments for every share submitted at a predetermined fixed rate.

The tax treatment of block rewards differs depending on the capacity in which a miner is acting—for example, whether the miner is undertaking the relevant activities as an employee or in the conduct of a trade or business. The differences among payment systems may also lead to different tax results. A PPS mechanism may be viewed as more akin to a contract payment, where actual work performed commands a fixed fee. A proportional mechanism, on the other hand, may be more analogous to a joint venture or partnership in which a miner’s participation generally entitles it to some share of the collective rewards. If a taxpayer is part of a CVC mining pool, particularly one utilizing a proportional mechanism, miners ought to consider the possibility that the arrangement may be treated as a de facto partnership for tax purposes.<sup>35</sup> Because of the variation among mining pool arrangements and their participants, it can be difficult to generalize the tax implications. Accordingly, taxpayers participating in pools should carefully consider the U.S. tax consequences of their participation in, and income earned from, such pools on a case-by-case basis.

## CONCLUSION

Blockchain technology and virtual currencies are here to stay. For the many taxpayers who participate, or wish to participate, in the CVC market, it is crucial to understand the distinctions between transacting with CVC and transacting with a fiat currency. The Notice provides a basic touchstone, albeit simplistic and dated, for understanding certain key tax consequences of making or receiving payment in virtual currencies.<sup>36</sup> As government regulatory schemes continue to develop, we anticipate Treasury and the IRS will begin to provide answers regarding the tax consequences of forks, ICOs, mining pools, and many other open questions.

In the interim, it is important for taxpayers to remain mindful of how they use and report CVC to the IRS and to take reasonable, principled, and consistent positions.<sup>37</sup>

## LAWYER CONTACTS

For further information, please contact your principal Firm representative or the lawyers listed below. General email messages may be sent using our “Contact Us” form, which can be found at [www.jonesday.com/contactus/](http://www.jonesday.com/contactus/).

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## ENDNOTES

1 There are actually different protocols for validating blocks, but “mining” is the most common.

2 For more information about the technology behind blockchain, see *Blockchain for Business Lawyers* 39 (Cox & Rasmussen eds., 2018). See also Satoshi Nakamoto, *Bitcoin: A Peer-to-Peer Electronic Cash System*.

3 For more information about the use of blockchain in the context of bitcoin, see *Blockchain for Business Lawyers* 39 (Cox & Rasmussen eds., 2018).

4 For more information on the structural importance of mining, see *Blockchain for Business Lawyers* 57 (Cox & Rasmussen eds., 2018).

5 Financial Crimes Enforcement Network, FIN-2013-G001, *Guidance on the Application of FinCEN’s Regulations to Persons Administering, Exchanging, or Using Virtual Currencies* 1 (2013).

6 *Id.*

7 Notice 2014-21, 2014-16 I.R.B. 938, A-1 (Apr. 14, 2014).

8 The IRS has provided limited instructions to its agents in the Internal Revenue Manual (“IRM”) in the form of applications of the Notice’s general principles to selected situations, but these do not address (much less answer) the significant open questions pertaining to blockchain taxation. See, e.g., IRM 4.23.5.19 (11-22-2017); IRM Procedural Update to IRM 4.19.3 (12-13-2018). The IRS website and Publication 525 (“Taxable and Nontaxable Income”) also contain limited, high-level summaries of certain key points contained in the Notice.

9 “IRS reminds taxpayers to report virtual currency transactions” (Mar. 23, 2018).

10 The Virtual Currency Compliance campaign. “IRS Announces the Identification and Selection of Five Large Business and International Compliance Campaigns” (July 2, 2018).

11 See, e.g., ABA, “Tax Treatment of Cryptocurrency Hard Forks for Taxable Year 2017” (Mar. 19, 2018); AICPA, “Updated Comments on Notice 2014-21: Virtual Currency Guidance” (May 30, 2018); ABA, “Comments on Notice 2014-21” (Mar. 24, 2015).

12 Treasury Inspector General for Tax Administration, “As the Use of Virtual Currencies in Taxable Transactions Becomes More Common, Additional Actions Are Needed to Ensure Taxpayer Compliance” (Sept. 2016), at 8-16.

13 See Letter from Jared Polis & David Schweikert, U.S. House of Representatives, to IRS Commissioner John Koskinen (Jun. 2, 2017); Letter from Committee on Ways and Means, U.S. House of Representatives, to IRS Commissioner David Kautter (Sept. 19, 2018).

14 Token Taxonomy Act, H.R. 7356, 115th Cong. § 7 (2nd Sess. 2018).

15 See *generally* I.R.C. §§ 1011, 1012.

16 IRS Notice 2014-21, at A-6. Whether such loss may be currently recognized under otherwise applicable tax law can be a more complicated matter.

17 IRS Notice 2014-21, at A-5. We note that different cryptocurrency exchanges/indexes do not always reflect the same prices, so determining such “fair market value” is not necessarily a straightforward task.

18 See *generally* I.R.C. § 1001; *Cottage Savings v. Comm’r*, 499 US 554 (1991); Rev. Rul. 90-80. Although Notice 2014-21 states that a taxpayer who receives CVC as payment “must, in computing gross income, include the fair market value of the virtual currency,” this is presumably intended to be read consistent with section 1001 and general income tax principles—such that the seller’s adjusted basis in the property sold must still be subtracted from the fair market value of the CVC received in order to arrive at the seller’s gain (loss). See *id.*

19 Notice 2014-21, at § A-8; see I.R.C. § 61. We note however, that § A-8 of the Notice states that “when a taxpayer successfully mines virtual currency, the fair market value of the virtual currency as of the date of receipt is includible in gross income” (emphasis added). Although not without some uncertainty, we assume for purposes of this general statement that the IRS does not literally intend that the full value of the virtual currency involved in the transaction(s)—versus the value of the amounts received by the miner for validating the transaction(s)—is includible in the miner’s gross income. In other words, despite the literal language of the Notice, we assume that a miner paid \$10 for validating a block of transactions involving \$100,000 of virtual currency must include the \$10 actually received, rather than the \$100,000, as taxable income.

- 20 Notice 2014-21, at § A-9.
- 21 For virtual currency exchanges effected prior to 2018, a strong argument could be made that the exchange of one CVC for another CVC may not have been a taxable event if the requirements of section 1031 (like-kind exchanges) were satisfied.
- 22 Notice 2014-21, at § A-7.
- 23 Notice 2014-21, at § A-7; see I.R.C. § 1221(a).
- 24 Notice 2014-21, at § A-7.
- 25 See I.R.C. § 1012(a). (We assume for these purposes that the purchase is made using USD as a U.S. taxpayer's own currency—rather than, for example, a purchase in yen or euros, which may itself trigger gain or loss.)
- 26 For a more detailed explanation of hard forks, see *Blockchain for Business Lawyers* 11 (Cox & Rasmussen eds., 2018).
- 27 A closed-flow virtual currency is one that can be used only within a particular virtual community (i.e., the currency system within a videogame, used to buy in-game items but without inherent “real world” value). Such closed-flow virtual currencies generally cannot be converted into fiat currency.
- 28 Cf. *Comm’r v. Glenshaw Glass*, 348 U.S. 426 (1955).
- 29 Cf. Treas. Reg. § 1.61-6(a), I.R.C. § 305(a); *Gamble v. Comm’r*, 68 T.C. 800 (1977). That one of the best analogies available involves birthing livestock should provide some indication of just how lacking formal guidance is in this area.
- 30 See *Comm’r v. Glenshaw Glass*, 348 U.S. 426 (1955).
- 31 See ABA, Comment Letter to the IRS regarding the Tax Treatment of Cryptocurrency Hard Forks for Taxable Year 2017 (Mar. 19, 2018); AICPA, Updated Comments on Notice 2014-21: Virtual Currency Guidance (May 30, 2018); H.R. 6973 “Safe Harbor for Taxpayers with Forked Assets Act of 2018” (115th Cong.).
- 32 This *White Paper* addresses only a handful of selected tax issues, but a host of additional open questions remain, particularly in the cross-border context—for example, there is significant uncertainty regarding U.S. taxing nexus, the sourcing and characterization of blockchain-related income, the applicable withholding and information reporting rules, and how to classify de facto partnerships created by mining pools.
- 33 Security token offerings, which generally follow the rules and regulations of federal securities laws, are an increasingly popular alternative to ICOs.
- 34 For further discussion of ICO tokens and the ICO process, see *Blockchain for Business Lawyers* 32-33 (Cox & Rasmussen eds., 2018) and John Conley, *Blockchain & the Economics of Cryptotokens & Initial Coin Offerings* 1-2 (Vanderbilt Univ., Working Paper 17-00008, 2017).
- 35 The Code and Treasury Regulations define “partnerships” fairly broadly. See I.R.C. § 761(a) (“[T]he term ‘partnership’ includes a syndicate, group, pool, joint venture or other unincorporated organization through or by means of which any business, financial operation, or venture is carried on, and which is not ... a corporation or a trust or estate.”); Treas. Reg. § 301.7701-1(a)(2). It is well established that an arrangement may be treated as a partnership for federal income tax purposes even if no entity is created under local law and the relationship is purely contractual.
- 36 Interestingly, in March 2019, Treasury announced that, while the IRS will not take positions inconsistent with its own subregulatory guidance issued outside of the notice-and-comment process, such guidance generally cannot be used to create new legislative rules. Further, the IRS will not argue that subregulatory guidance “has the force and effect of law” or seek judicial deference to interpretations set forth only in such guidance. The Notice is an example of subregulatory guidance.
- 37 IRS agents speaking publicly have indicated that taxpayers should take “reasonable positions” and “try to comply as best you can.” *Tax Notes*, “Lack of Virtual Currency Guidance May Not Be So Bad After All” (quoting an LB&I director and IRS Office of Associate Chief Counsel branch chief, speaking at the AICPA Fall Tax Meeting in Washington, D.C. on November 14, 2018) (Nov. 26, 2018).

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