



American Institute of CPAs
1455 Pennsylvania Avenue, NW
Washington, DC 20004-1081

June 10, 2016

Internal Revenue Service
Attn: CC:PA:LPD:PR (Notice 2014-21)
Room 5203
P.O. Box 7604
Ben Franklin Station
Washington, DC 20044

Re: Comments on Notice 2014-21: Virtual Currency Guidance

Dear Sir or Madam:

The American Institute of CPAs (AICPA) submits the following comments in response to the Internal Revenue Service (IRS) guidance on how existing general tax principles apply to transactions using virtual currency. The recommendations included in this letter were developed by the AICPA Individual & Self Employed Tax Technical Resource Panel (TRP) and approved by the AICPA Tax Executive Committee.

We applaud the IRS for working expeditiously to release guidance in the form of answers to frequently asked questions (FAQs) regarding the tax treatment of virtual currency transactions, an area that has quickly grown and become a prevalent concern for many taxpayers and tax practitioners. However, we recognize there are a few major issues, not addressed in Notice 2014-21, that may arise as virtual currency continues to expand and gain additional popularity in the marketplace.

The AICPA encourages the IRS to release additional, much needed, guidance on virtual currency. Specifically, we request further guidance on the following items:

1. Acceptable Valuation and Documentation

Issue further guidance and provide examples to better define “reasonable manner,” as described in Section 4, Q&A-5 of Notice 2014-21.

Q&A-5 refers to exchange rates established by market supply and demand. It also states that taxpayers are recommended to use a “reasonable manner that is consistently applied” to calculate the fair market value of virtual currency. In regards to this issue, please provide additional details on the following questions:

- a. Are taxpayers required to select one exchange and continue to use this same exchange?
- b. Are taxpayers allowed to use an average of different exchanges?
- c. May taxpayers use the average rate for the day to calculate the exchange rate or is there a specific time during the day to pull exchange rates?

With respect to bitcoin, there are a few published exchanges and the value reported on each exchange at any time of the day is unlikely the same.

For example, these bitcoin values were pulled on January 31, 2015 at 8:25 am (Eastern Time):

• Google	\$231.1462
• Bitcoin exchange rate	\$229.80
• Bitstamp	\$228.24
• CEX	\$231
• Winkdex	\$227.94

These values were pulled on May 20, 2015 at 10:20 am (Eastern Time):

• Google	\$234.2500
• Bitcoin exchange rate	\$234.21
• Bitstamp	\$233.67
• CEX	\$231
• Winkdex	\$232.29

2. Expenses of Obtaining Virtual Currency

Provide guidance on the treatment of the costs of mining and acquiring virtual currency. This guidance should also address when, if ever, any costs of acquiring virtual currency is capitalized.

Generally, the costs of acquiring property are treated as part of the basis of that property. Section 4, Q&A-8 of Notice 2014-21 states that when virtual currency is mined, gross income is realized upon receipt at fair market value. This language implies that mining is akin to a service activity, rather than a production activity where income is not realized until disposition of the property. Therefore, it seems the costs of mining virtual currency are treated similarly to expenses incurred in providing other services; i.e., expensed as paid or incurred.

3. Challenges with Specific Identification for Computing Gains and Losses

Allow an alternative treatment under section 1012¹ (e.g., first in first out (FIFO)).

The treatment of convertible virtual currency as non-cash property means that any time virtual currency is used to acquire goods or services, a barter transaction takes place, and the parties need to know the fair market value (FMV) of the currency on that day. The party exchanging the virtual currency for the goods or services will need to also track the basis of all of his or her currency to determine if a gain or loss has occurred and whether it is a short-term or long-term transaction. This determination involves a significant amount of recordkeeping, even if the transaction is valued at under \$10.

Currently, there are no alternative tracking methods provided for such transactions (other than for securities under Treas. Reg. § 1.1012-1(c)). Therefore, taxpayers are required to specifically identify which virtual currency lot was used for each transaction in order to properly determine the gain or loss for that particular transaction. In many cases, it is impossible for a taxpayer to track which specific virtual currency was used for a particular transaction.

4. General Guidance Regarding Property Transactions Rules

If the IRS believes any property transaction rules should apply differently to virtual currency than to other types of property, taxpayers will need additional guidance in order to properly distinguish the rules and regulations.

Section 4, Q&A-1 of Notice 2014-21 states that “general tax principles applicable to property transactions apply to transactions using virtual currency,” which is guidance that is generally helpful in determining the tax consequences of most virtual currency transactions. However, if there are particular factors that distinguish one virtual currency as like-kind to another virtual currency for section 1031 purposes, the IRS should clarify these details (e.g., allowing the treatment of virtual currency held for investment or business as like-kind to another virtual currency) in the form of published guidance. Similarly, taxpayers need specific guidance of special rules or statutory interpretations if the IRS determines that the installment method of section 453 is applied differently for virtual currency than for other types of property.

5. Nature of Virtual Currency Held by a Merchant

Provide guidance as to whether virtual currency held by a merchant is a capital or ordinary asset.

¹ All section references in this letter are to the Internal Revenue Code of 1986, as amended, or the Treasury regulations promulgated thereunder, unless otherwise specified.

A merchant may hold virtual currency for use in paying employees and suppliers. In this capacity, the virtual currency is used in the form of U.S. currency. However, due to the treatment of this currency as property, and the gain or loss that results each time a virtual currency is used, the character of this specific type of currency asset is an important determination.

6. Charitable Contributions

Provide guidance to explain when a donation of virtual currency, valued above \$5,000, does not need a qualified appraisal to substantiate a charitable contribution deduction. Additionally, provide guidance on how to document the virtual donation values.

A charitable contribution of property with a value in excess of \$5,000 requires a qualified appraisal from a qualified appraiser. An exception exists for contributions of publicly traded stock. The rationale is that the prices of these publicly traded stocks are available on published exchanges, thus not requiring a qualified appraisal. The same is true for most, if not all, types of virtual currency. That is, an exchange publishes the values of this currency on any given day. Therefore, a similar exception should apply for virtual currency donations in excess of a certain amount.

7. Virtual Currency as a “Commodity”

Provide guidance on whether virtual currency is considered a “commodity” subject to mark-to-market accounting under sections 475(e) and 475(f).

This particular issue is also under consideration by the Commodity Futures Trading Commission.²

8. Need for a De Minimis Election

Currently, section 988(e)(2) allows for an exclusion of up to \$200 per transaction for foreign currency exchange rate gain, if derived from a personal transaction. Can a similar rule apply for virtual currency transactions even though they are taxed as property (rather than as a currency)?

Some taxpayers may only have a minimal amount of virtual currency that is designated for making small purchases (such as buying coffee). Tracking the basis and FMV of

² Testimony of Commissioner Mark Wetjen before the U.S. House Committee on Agriculture Subcommittee on Commodity Exchanges, Energy, and Credit Subcommittee, April 14, 2015; <http://www.cftc.gov/PressRoom/SpeechesTestimony/opawetjen-12>. Also see Nermin Hajdarbegovic, “Commissioner Claims CFTC Can Intervene in Bitcoin Markets,” CoinDesk, Nov. 18, 2014; <http://www.coindesk.com/commissioner-claims-cftc-can-intervene-bitcoin-markets/>.

the virtual currency for each of these small purchases is time consuming, burdensome, and will yield a de *minimis* amount of gain or loss. A binding election applicable for a specified amount of virtual currency owned or classified for personal purposes is beneficial to taxpayers.³

9. Retirement Accounts

Provide guidance on whether retirement savings accounts are permitted to hold virtual currency investments. If yes, explain any special reporting rules or other requirements that exist if a retirement account contains this type of virtual property.

10. Foreign Reporting Requirements for Virtual Currency

Provide guidance on whether virtual currency accounts can become reportable on the Form 114, *Report of Foreign Bank and Financial Accounts* (FBAR) in future tax years. Also, explain whether there are circumstances that can alter virtual currency accounts into foreign financial assets under section 6038D, and therefore required for reporting on Form 8938, *Statement of Specified Foreign Financial Assets*.

Also, provide guidance on whether additional reporting obligations exist under the Foreign Account Tax Compliance Act (FATCA) or whether there are other requirements for money services businesses (MSB) that exchange virtual currency. For example, would the IRS consider this exchange a financial institution activity?

Taxpayers do not have guidance on how virtual currency rules will change for future tax years. An IRS analyst for the Small Business/Self-Employed Division stated,⁴ in June of 2014, that virtual currency accounts were not reportable on the Form 114, *Report of Foreign Bank and Financial Accounts*, for tax years ended 2014. However, no guidance was provided in regards to future tax years. Virtual currencies are intangible assets because they are represented by a code. These currencies, such as Bitcoin, operate in decentralized environments where no entity or person is in charge of controlling or monitoring the asset. Therefore, the currency appears to have no location, which is a characteristic that would complicate foreign reporting compliance.

* * * * *

³ If it is determined that statutory action is needed to enact such a rule, we encourage the IRS to reach out to Congress for this request.

⁴ Rod Lundquist, a senior program analyst for the Small Business/Self-Employed Division, stated in a webcast that, for FBAR purposes, Bitcoin is not reportable "...not at this time." Lundquist also stated that "FinCEN has said that virtually currency is not going to be reportable on the FBAR, at least for this filing season," broadcasted June 4, 2014, see archived webcast: <http://www.irsvideos.gov/ElectronicFBAR/>.

Virtual currency transactions, in which taxpayers increasingly engage, add a new layer of complexity to the analysis of a client's reporting requirements. The issuance of clear guidance in this area will not only reduce the confusion and burden for tax preparers but also allow taxpayers to accurately comply with IRS rules

The AICPA is the world's largest member association representing the accounting profession, with more than 412,000 members in 144 countries, and a history of serving the public interest since 1887. Our members advise clients on federal, state and international tax matters and prepare income and other tax returns for millions of Americans. Our members provide services to individuals, not-for-profit organizations, small and medium-sized businesses, as well as America's largest businesses.

We appreciate your consideration of our concerns and recommendations and welcome the opportunity to discuss these items further. If you have any questions, please feel free to contact me at (801) 523-1051, or tlewis@sisna.com; or you may contact Kenneth Rubin, Chair, AICPA Individual & Self-Employed Tax Technical Resource Panel, at (314) 290-3417, or ken.rubin@rubinbrown.com; or Amy Wang, AICPA Senior Technical Manager, at (202) 434-9264, or awang@aicpa.org.

Sincerely,

A handwritten signature in black ink, appearing to read "Troy K. Lewis". The signature is fluid and cursive, with the first name "Troy" being the most prominent.

Troy K. Lewis, CPA, CGMA
Chair, AICPA Tax Executive Committee

cc: The Honorable John A. Koskinen, Commissioner, Internal Revenue Service
The Honorable William J. Wilkins, Chief Counsel, Internal Revenue Service
Mr. Thomas C. West, Jr., Tax Legislative Counsel, Department of the Treasury