Tax Consequences of Cryptocurrency Transactions and Correcting Historical Noncompliance

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Compliance with the internal revenue laws relating to cryptocurrency is sorely deficient. As of Dec. 31, 2015, the market capitalization of cryptocurrencies was roughly $7 billion spread among 5.8 million active digital wallets, 34 percent of which (or 1.97 million wallets) were attributable to U.S.-based users. Despite the prevalence of U.S.-based cryptocurrency users, of the 128 million tax returns electronically filed during 2015, a mere 802 returns reported cryptocurrency gains.

In light of these statistics, the Internal Revenue Service (IRS) and the U.S. Department of Justice (DOJ) have threatened civil penalties and criminal prosecution for taxpayers who violate tax laws while using cryptocurrency. For taxpayers who engaged in cryptocurrency transactions but did not report the transactions for federal, state or local income tax purposes, a qualified amended return or voluntary disclosure may create a path to compliance that limits the likelihood of civil or criminal penalties. Section references are to the Internal Revenue Code of 1986, as amended.

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