



Virtual Currency: Tax Treatment and Blockchain Fundamentals

Course #33551B

Taxes

2 Credit Hours

Support@PacificCPE.com | (800) 787-5313

PacificCPE.com

VIRTUAL CURRENCY: TAX TREATMENT AND BLOCKCHAIN FUNDAMENTALS

This course provides a comprehensive overview of virtual currency, including how it functions, how it differs from central bank digital currencies (CBDCs) and stablecoins, and how blockchain technology secures transactions. It covers the calculation of adjusted cost basis for purchased, mined, or gifted virtual currency, as well as the tax treatment of charitable donations and partial disposals. The course offers essential guidance for understanding and reporting virtual currency transactions accurately.

LEARNING ASSIGNMENTS AND OBJECTIVES

As a result of studying each assignment, you should be able to meet the objectives listed below each individual assignment.

SUBJECTS

Introduction

Nature of Virtual Currency

Tax Treatment and Reporting

Study the course materials

Complete the review questions at the end of each chapter

Answer the exam questions 1 to 10

Objectives:

- Recognize virtual currency.
- Recall how central bank digital currency (CBDC) is used.
- Recognize how stablecoins differ from unbacked cryptocurrency.
- Recall how virtual currency networks maintain security.
- Recognize how blockchain is employed with respect to virtual currency transactions.
- Identify how to calculate the adjusted cost basis of virtual currency that is purchased, mined, or received as a gift.
- Recall the tax treatment of virtual currency given as a charitable gift.
- Recognize the tax treatment given virtual currency when less than all is sold, exchanged, or otherwise disposed of.

NOTICE

Limit of Liability/Disclaimer of Warranty: While the publisher and author have used their best efforts in preparing this book, they make no representations or warranties with respect to the accuracy or completeness of the contents of this book and specifically disclaim any implied warranties or merchantability or fitness for a particular purpose. No warranty may be created or extended by sales representatives or written sales materials. The advice and strategies contained herein may not be suitable for your situation. You should consult with a professional where appropriate. Neither the publisher nor author shall be liable for any loss of profit or any other commercial damages, including but not limited to special, incidental, consequential, or other damages.

The End User shall be permitted to use the Licensed Content for internal purposes only and not for resale or distribution. The Licensed Content is provided on an "as is" basis and without any warranties of any kind, express or implied. CCH INCORPORATED AND ITS LICENSORS AND AFFILIATES DISCLAIM ALL WARRANTIES WITH RESPECT TO THE LICENSED CONTENT, EXPRESS OR IMPLIED, INCLUDING BUT NOT LIMITED TO, WARRANTIES OF MERCHANTABILITY, FITNESS FOR A PARTICULAR PURPOSE, NON-INFRINGEMENT, TITLE, QUIET ENJOYMENT AND INFORMATION COMPLETENESS, CURRENCY OR ACCURACY.

End User assumes all responsibilities and obligations with respect to the selection of the Licensed Content to achieve End User's intended results. End User assumes all responsibilities and obligations with respect to any decision or advice made or given as a result of the use or application of the Licensed Content. CCH and its licensors and affiliates are not engaged in the rendering of legal, accounting, tax or other professional advice or services. If legal, accounting, tax or other expert assistance is required, the services of a competent professional should be sought.

This course is sold with the understanding that the publisher is not engaged in rendering legal, accounting, or other professional advice and assumes no liability whatsoever in connection with its use. Since laws are constantly changing, and are subject to differing interpretations, we urge you to do additional research and consult appropriate experts before relying on the information contained in this course to render professional advice.

© Pacific CPE, LP 2025

Program publication date 2/18/25

EXAM OUTLINE

- **TEST FORMAT:** The final exam for this course consists of 10 multiple-choice questions and is based specifically on the information covered in the course materials.
- **ACCESS FINAL EXAM:** Log in to your account and click Take Exam. A copy of the final exam is provided at the end of these course materials for your convenience, however you must submit your answers online to receive credit for the course.
- **LICENSE RENEWAL INFORMATION:** This course qualifies for **2 CPE hours**.
- **PROCESSING:** You will receive the score for your final exam immediately after it is submitted. A score of 70% or better is required to pass.
- **CERTIFICATE OF COMPLETION:** Will be available in your account to view online or print. If you do not pass an exam, it can be retaken free of charge.

TABLE OF CONTENTS

Introduction	1
Course Learning Objectives	1
Chapter 1: Nature of Virtual Currency	2
Introduction	2
The Lexicon of Virtual Currency	2
Virtual Currency Defined	2
Obtaining Virtual Currency	5
Storing Virtual Currency	7
Virtual Currency Transactions	9
Blockchain	11
Summary	11
Chapter 1: Test Your Knowledge	14
Chapter 1: Solutions and Suggested Responses	16
Chapter 2: Tax Treatment and Reporting	18
Introduction	18
Virtual Currency Transactions	18
Determining the Cost Basis of Virtual Currency	19
Tax Treatment of Virtual Currency Received for Services	24
Tax Treatment of Virtual Currency Transactions	27
Reporting	31
Recordkeeping	32
Summary	33
Chapter 2: Test Your Knowledge	36
Chapter 2: Solutions and Suggested Responses	38
Glossary	41
Index	45
Final Exam Copy	46

INTRODUCTION

According to a survey done by the Pew Research Center whose results were published in April 2023, 17% of Americans indicated they personally have invested in, traded or otherwise used virtual currency.¹ Additionally, the number of people investing in or engaging in transactions involving virtual currency continue to increase. These statistics strongly suggest that tax preparers must be aware of the nature of virtual currency and its tax treatment. It's to provide that awareness that Tax Treatment of Virtual Currency was written.

COURSE LEARNING OBJECTIVES

After completing this course, students should be able to:

- Recognize virtual currency.
- Recall how central bank digital currency (CBDC) is used.
- Recognize how stablecoins differ from unbacked cryptocurrency.
- Recall how virtual currency networks maintain security.
- Recognize how blockchain is employed with respect to virtual currency transactions.
- Identify how to calculate the adjusted cost basis of virtual currency that is purchased, mined, or received as a gift.
- Recall the tax treatment of virtual currency given as a charitable gift.
- Recognize the tax treatment given virtual currency when less than all is sold, exchanged, or otherwise disposed of.

1. The Pew Research Center fact sheet may be accessed at <https://www.pewresearch.org/short-reads/2023/04/10/majority-of-americans-arent-confident-in-the-safety-and-reliability-of-cryptocurrency/>.

CHAPTER 1: NATURE OF VIRTUAL CURRENCY

Chapter Objectives

After completing this chapter, you should be able to:

- Recognize virtual currency.
- Recall how central bank digital currency (CBDC) is used.
- Recognize how stablecoins differ from unbacked cryptocurrency.
- Recall how virtual currency networks maintain security.
- Recognize how blockchain is employed with respect to virtual currency transactions.

INTRODUCTION

Virtual currency use appears to be increasing continually and, according to a Pew survey, roughly 3 in 10 Americans younger than age 30 indicate they have invested in, traded, or used a virtual currency, such as Bitcoin or Ethereum. As a result, tax preparers are more likely than ever to encounter clients who have engaged in one or more virtual currency transactions during the year and who may have taxable income as a result. This chapter begins the course with a discussion of the nature of virtual currency and how transactions in virtual currency occur and are recorded.

THE LEXICON OF VIRTUAL CURRENCY

Understanding the U.S. tax treatment of virtual currency requires that we have an understanding of the nature of virtual currency which, in turn, means we need to understand the terms and language used to describe it and the ecosystem in which it exists. To that end, the lexicon, based on the Blockchain Universal Glossary published by the Association of International Certified Professional Accountants is included in the Glossary¹ and is used in the following text.

VIRTUAL CURRENCY DEFINED

With the flurry of types of currency mentioned in conversations—digital currency, virtual currency, cryptocurrency, and the like—it's often difficult to be sure what people mean when they talk about it. Virtual currency was initially defined by the European Central Bank in a 2012 report² titled Virtual Currency Schemes as “a type of unregulated, digital money, which is issued and usually controlled by its developers, and used and accepted among the members of a specific virtual community.”

In 2014 the IRS, in Notice 2014-21, observed that “virtual currency... is customarily used and accepted as a medium of exchange in the country of issuance—but it does not have legal tender status in any

1. “Blockchain Universal Glossary” may be accessed at <https://us.aicpa.org/content/dam/aicpa/interestareas/informationtechnology/downloadabledocuments/blockchain-universal-glossary.pdf>

2. Virtual Currency Schemes may be accessed at <https://www.ecb.europa.eu/pub/pdf/other/virtualcurrencyschemes201210en.pdf>.

jurisdiction.”³ Similarly, in IRS Revenue Ruling 2019-24, the IRS declared that “Virtual currency is a digital representation of value... and a store of value other than a representation of the United States dollar or a foreign currency”⁴ and further went on to equate foreign currency with the money of a foreign country designated as legal tender. In short, it reiterated that virtual currency was not the legal tender of any foreign country.

In September, 2021 El Salvador made that statement incorrect by declaring Bitcoin legal tender, giving it a status in the country similar to the U.S. dollar. In light of the historically high level of remittances to Latin American countries and the costs and delays normally associated with cross-border payments, it is possible that virtual currency will become legal tender in additional Latin American and other countries as they observe the effect virtual currency’s status as legal tender has on El Salvador’s banking system and the well-being of its citizens.

One of the characteristics central to the ability of virtual currency to gain acceptance is its adherence to a set of rules to ensure the values recorded in the ledger memorializing virtual currency transactions are correct. That is accomplished through its consensus protocol, the mechanism defining the steps required to achieve agreement on the values recorded by the various participants on the blockchain. The term “protocol,” when used in this sense is generally defined as a set of rules governing the communication and transfer of data between machines, as in a computer system.

Digital Currency

The various notices, rulings and reports refer to virtual currency as “digital.” To forestall confusion and clearly identify the subject of this course, it’s appropriate to briefly examine the relationship of digital currency to virtual currency. Digital currency is a fairly broad term referring to a method of payment existing entirely in an electronic form. As an electronic method of payment, it is transferred to a payee using an online system.

CBDCs – Regulated Digital Currency

Digital currency may be regulated or unregulated. Regulated digital currency is currency issued by a country’s central bank and generally referred to as central bank digital currency (CBDC). Among other uses, CBDCs are employed for monetary transactions between banks and other financial institutions.

The Federal Reserve Board released a paper titled *Money and Payments: The U.S. Dollar in the Age of Digital Transformation* in January 2022, examining the pros and cons of a U.S. central bank digital currency⁵ and inviting public comments. The paper summarizes the domestic payments system, discussing the various digital payment methods and assets, including stablecoins and other types of cryptocurrencies. Without taking a position, the paper examines CBDCs, considers the potential benefits and risks their issuance poses, and identifies the policy considerations associated with such a step. For purposes of the paper, a CBDC is defined “as a digital liability of a central bank that is widely available to the general public. In this respect, it is analogous to a digital form of paper money.”

3. IRS Notice 2014-21 may be accessed at <https://www.irs.gov/pub/irs-drop/n-14-21.pdf>.

4. IRS Revenue Ruling 2019-24 may be accessed at <https://www.irs.gov/pub/irs-drop/rr-19-24.pdf>.

5. *Money and Payments: The U.S. Dollar in the Age of Digital Transformation* may be accessed at <https://www.federalreserve.gov/publications/files/money-and-payments-20220120.pdf>.