PacificCPE

COURSE
33551C

Virtual Currency Taxation: Core Concepts and Reporting

Get up to speed on the fundamentals of virtual currency and how the IRS expects it to be handled on tax returns. This course covers what virtual currency is, how it's classified, and the key tax treatment and reporting rules practitioners need to know. Whether you're new to the topic or looking to solidify your foundation, this course gives you the practical grounding to handle virtual currency questions with confidence in your practice.

CREDIT HOURS 2 | FIELD OF STUDY TAXES | EXAM QUESTIONS 10

Start Course ↓

Final Exam Copy ↓

LEARNING ASSIGNMENTS AND OBJECTIVES

Assignment

- Study the full course materials included here.
- Complete the review questions after each chapter.
- Answer 10 final exam questions.
- Final exam is scored immediately, 70% or better passes.
- Certificate of completion is available in your account.
- Failed exams can be retaken free of charge.

Course 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.

Copyright Notice

© 2026 Pacific CPE, LP. All rights reserved.

The materials in this course — including the text, illustrations, exhibits, examples, exam questions, and review questions — are the copyrighted property of Pacific CPE, LP. No portion of this course may be reproduced, stored in a retrieval system, distributed, or transmitted in any form or by any means (electronic, mechanical, photocopying, recording, or otherwise) without the prior written permission of Pacific CPE, LP, except for the personal, non-commercial use of the registered learner.

Pacific CPE, LP grants the registered learner a single-seat, non-transferable license to access this course for the purpose of completing the associated continuing professional education credit. Account credentials may not be shared. Group access requires a separate enterprise license.

This course is provided "as is" for educational purposes. While Pacific CPE, LP makes a reasonable effort to ensure the content is current and accurate, the materials should not be relied upon as a substitute for professional advice. Pacific CPE, LP disclaims all liability for any error, omission, or loss arising from the use of, or reliance on, the course content.

Questions about reproduction, licensing, or use of these materials should be directed to support@pacificcpe.com.

Publication Date: March 2026

TABLE OF CONTENTS

CHAPTER 00

Introduction 6

CHAPTER 01

Nature Of Virtual Currency 7

1.01 Introduction 7

1.02 Cbdcs – Regulated Digital Currency 9

1.03 Stablecoins – Backed Cryptocurrencies 9

1.04 Storing Virtual Currency 13

1.05 Hard Fork 17

1.06 Summary 18

Test Your Knowledge 22

CHAPTER 02

Tax Treatment And Reporting 27

2.01 Introduction 27

2.02 Formerly Gifted Inherited Virtual Currency 30

2.03 Cost Basis Of Gifted Property When Fmv Is Less Than Donor'S Adjusted Basis 32

2.04 Requirement For Substantiating Documentation 34

2.05 Reporting 43

2.06 Summary 46

Test Your Knowledge 49

Final Exam Copy 59
Glossary 54
Index .....

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 this course was written.

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 Objective

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 Certified Professional Accountants is included in the Glossary 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 report 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

jurisdiction." 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" 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. For 2026, the IRS continues to consider virtual currency as property rather than currency in its federal income tax treatment. Taxable events are treated as property when selling, trading, using cryptocurrencies to purchase goods and services,

and receiving cryptocurrency as payment for services and is taxed as ordinary income upon transaction.

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 currency 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

Although considerable international effort would be needed, CBDCs could facilitate cross-border payments and reduce costs through the use of new technologies, simplified distribution channels, and by creating additional opportunities for collaboration between countries.

Virtual Currency – Unregulated Digital Currency

Unlike CBDCs that are regulated digital currency, virtual currency is unregulated and may be either closed virtual currency—virtual currency that is used entirely in a controlled, private ecosystem and which cannot be converted into fiat currency—or open virtual currency. Open virtual currency, in contrast to closed virtual currency, is convertible into other forms of currency, including fiat and may be stablecoins or unbacked cryptocurrency.

Stablecoins – Backed Cryptocurrencies

Stablecoins are digital assets designed to maintain a stable value and are used in the United States to facilitate trading, lending, or borrowing of other digital assets. Although intended principally to provide stability and a level of safety when contrasted with unbacked cryptocurrency, stablecoins can vary from one another with respect to the risks they pose to holders because of the assets they hold as security. Thus, the reserve assets of some stablecoin arrangements are held in deposits at insured depository institutions or in U.S. Treasury bills, while other stablecoins may be backed by commercial paper, corporate and municipal bonds, and other digital assets.

Although both offer safety and security uncharacteristic of cryptocurrency, the level of safety provided obviously varies.

As discussed in a FINRA investor insights report titled Cryptocurrencies: Three Things to Know About Stablecoins dated April 17, 2020, currently-available stablecoins fall into four main categories:

- **Fiat-backed stablecoins** - stablecoins secured by fiat currency are the most prevalent type of stablecoins currently available. Fiat-backed stablecoins are secured by one or more currencies, such as U.S. dollars, Euros, Yen, or some other central bank-issued currency. The value of a fiat-backed stablecoin is typically equal to the value of the collateral held in reserve;
- **Commodity-backed stablecoins** - stablecoins backed by commodities are tied to tangible assets, such as silver, gold, or other precious metal and are typically more attractive to investors looking for exposure to physical assets. The value of a commodity-backed stablecoin is normally equal to one unit of the commodity. So, in the case of a commodity-backed stablecoin secured by gold, its value might reasonably be worth one ounce of gold. Similarly, an oil-backed stablecoin could be worth one barrel of oil. The physical commodities used to secure commodity-backed stablecoins are usually held by a third party who stores the assets in reserve;
- **Crypto-backed stablecoins** – crypto-backed stablecoins, whose value may be pegged to a fiat currency, are secured by other digital currencies rather than by the fiat currency to which their value is referenced. However, possibly in recognition of the volatility of crypto currency, the value of the reserves held as collateral is greater than the value of the outstanding stablecoins as a way of limiting the crypto-backed stablecoins' volatility; and
- **Algo-based stablecoins** - unlike other stablecoins, algo-backed stablecoins are not backed by collateral. Instead, they rely on smart contracts to maintain stable value. Smart contracts employ algorithms to adjust the supply of stablecoins based on market demand.

Unbacked Cryptocurrency

Unlike stablecoins that—other than algo-based stablecoins—are cryptocurrencies generally backed by, and whose value is based on, fiat currency, gold or other assets, unbacked cryptocurrencies derive their value principally as a result of the combination of demand and a relatively inelastic supply. Unbacked cryptocurrencies—whether Bitcoin, Ethereum or other unbacked digital currency—have no intrinsic value and are