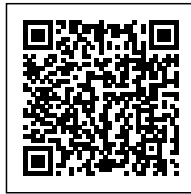


INITIAL COIN OFFERINGS: UNCERTAIN TAX CONSEQUENCES

Posted on March 29, 2018 by Michelle F. Schwerin



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Part Three of Three: In the prior blog posts in this series, I described generally how an Initial Coin Offering (ICO) operates and discussed how the Securities and Exchange Commission views the coins or tokens generated from an ICO. In this post, I explore the guidance (or lack-thereof) from the Internal Revenue Service.

- **PART ONE:** [Initial Coin Offerings: A Primer and Suggestion of Impending Issues](#)
- **PART TWO:** [Initial Coin Offerings: The Securities and Exchange Commission's View](#)
- **PART THREE:** [Initial Coin Offerings: Uncertain Tax Consequences](#)

IRS Guidance on Initial Coin Offerings

The IRS has yet to issue specific guidance as to the tax treatment of the purchase of or transactions involving coins or tokens from an ICO.

In March 2014, the IRS published [Notice 2014-21](#), which describes general tax principles as applied to virtual currency transactions. Per this Notice, the exchange of virtual currency (e.g., Bitcoin or Ethereum) for a good or service is considered a taxable transaction. At first consideration, it seems there is no reason to believe the purchase and sale of coins or tokens through an ICO would be treated any differently. The Notice, however, explicitly states that "no inference should be drawn with respect to virtual currencies not described in this notice." ICO coins or tokens are not necessarily

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virtual currency, so and the applicability of the IRS guidance to such coins or token is far from clear.

Token or Coin Issuers

From the issuer's side, the majority perspective is that the issuer must recognize the value received from the sale of the coin or token as revenue. As the coins or tokens are usually sold for virtual currency, the revenue reported will be based on the fair market value of the virtual currency received. If the issuer does not immediately exchange the virtual currency for U.S. dollars, it will also be subject to future capital gains or losses based on the appreciation or depreciation of the virtual currency between the time of the sale and the conversion.

Other questions from an issuer, such as whether distribution of coins or tokens to employees is compensation (a whole blog post could be dedicated to this topic, which is more complicated than it might seem), and how to value the distribution or how to treat tokens issued but not sold, are less clear.

Token or Coin Purchasers

From the purchaser's side, there is less of a consensus as to whether the purchase or sale of a coin or token should be reported and, if so, how it is treated. Generally, a coin or token does not have a purpose outside the issuer's application platform and cannot be easily exchanged for U.S. dollars on a market in the same way a virtual currency might. However, with developing secondary markets for these tokens, a purchaser may sell a token to another purchaser-investor for a higher value than he or she originally paid for the token. If the token is treated as property, then the purchase of the token gives the initial purchaser a basis in the token, which would generate a gain or loss following a subsequent transfer.

Many issues are still unsettled. Unfortunately, this leaves the taxpayer vulnerable to the IRS's disagreement with a taxpayer's position – in reporting or deciding not to report a transaction, treating secondary market sales, creating and holding token-based funds, etc. In addition, taxpayers must be aware of issues such as the location of a virtual wallet and whether its location triggers a foreign account reporting and/or state and local taxes consequences.

Ultimately, determination of the proper treatment will be driven primarily by the taxpayer's specific situation and requires careful scrutiny and analysis.

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