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Wyoming Could Serve As Cryptocurrency Tax Bellwether

By **Amy Lee Rosen**

Law360 (May 4, 2018, 7:32 PM EDT) -- Wyoming is taking a different approach from the Internal Revenue Service in taxing cryptocurrencies, and while the state's departure from the norm is unlikely to affect federal policy, it could influence other states to consider alternate taxing methods in an attempt to attract more crypto businesses.

The state's Republican Gov. Matt Mead signed state S.B. 111 into law this year, exempting virtual currencies from state property taxation. The statute defined "virtual currency" as any type of digital representation of value that is used as a medium of exchange, unit of amount or store of value and is not recognized as legal tender by the U.S. government. It was meant to make Wyoming more welcoming to the blockchain industry, according to state Sen. Ogden Driskill, R-Devils Tower, who introduced the bill in February.

While Wyoming, like the IRS, still treats cryptocurrency as property, the IRS' approach says that even though virtual currencies may be treated as a currency elsewhere and be subject to fewer taxes, any capital gain or loss from the sale or exchange of cryptocurrency in the U.S. must be reported the same way as any other payments made with property.

Thomas Newman, senior counsel at Perkins Coie LLP, said it is unlikely the Internal Revenue Service will be influenced by Wyoming's approach to exempting cryptocurrencies from property tax because there is no overarching policy reason why owners of virtual currencies should be treated differently from other property owners.

"Cryptocurrency should not be exempt from any federal tax because there is no reason to distinguish it from other property" or to treat owners of virtual currencies differently from other taxpayers, he said. For example, if one person earned $30,000 in wages in one year and a second person earned $30,000 selling cryptocurrency, there is no reason why only the wage earner should be taxed and not the crypto-earner, Newman said.

Wyoming's proposal does not actually change the tax treatment of cryptocurrency, since it is still treated as property, which would originally be subject to capital gains or losses under federal law, but now that property is exempt from state property taxes, he said.

At the federal level, if someone uses cryptocurrency to pay for something, that person has to report the sale of it, and the receiver of the virtual currency has to report receiving it, so every transaction would have two reporting obligations, Newman said.

Newman said the federal system has complicated reporting requirements, but there is nothing to indicate the U.S. will change its policy even though Wyoming's measure makes reporting easier.

"It would eliminate a lot of the reporting requirements if cryptocurrency was being used as a currency to buy and sell something, including other types of cryptocurrency," he said. "It would eliminate a burden on a lot of owners of cryptocurrency who are buying and selling cryptocurrency."

Shiukay Hung, who is of counsel at Morrison & Foerster LLP, agreed the IRS is unlikely to change because it has a monopoly on the taxation of bitcoin and other virtual currencies, but said that attitude could change as the U.S. competes with other countries to attract crypto businesses.

"The IRS is in competition with places like Canada, the U.K., Singapore or Hong Kong," he said. "So while the IRS or Congress might not be necessarily influenced by Wyoming's tax policies per se, they may be influenced by the tax policies of the other G-20 countries."

Hung said if a trend develops whereby most G-20 countries provide tax benefits for virtual currency businesses, that may prompt Congress and the IRS to consider and enact similar policies.

As for why Wyoming enacted the property tax exemption, Hung said the tax policy provides an interesting tax incentive for cryptocurrency companies and is generally consistent with favorable nontax policies in Wyoming.

"Wyoming is trying to set itself up as the Delaware of cryptocurrency," he said, because such businesses are highly mobile and this legislation sends a signal that the state would like to court blockchain businesses.

Hung said Wyoming is the first out of the gate to say it is going to be a favorable jurisdiction for cryptocurrency, but Maryland has also been especially active in the blockchain space, so it is possible Maryland will try to compete with Wyoming.

Carol R. Van Cleef, a partner at LeClairRyan, said many lobbyists involved in Wyoming have moved to other states to push for similar legislation across the U.S.

"I have compared the lobbying efforts in Wyoming to that of the Minutemen in the U.S. War of Independence," she said. "It is a model for achieving legislative reform in other states."

She told Law360 that slowly but surely, other states will become aware of the benefits of setting up friendly policies toward cryptocurrencies because it creates a unique opportunity for job creation.

Roger McEowen, a Kansas Farm Bureau professor of agricultural law and taxation at Washburn University School of Law, agreed that the IRS is unlikely to change and that Wyoming is using this tax policy to attract crypto businesses, but said Wyoming could be in competition with South Dakota.

"The Wyoming legislation could be followed in other states such as South Dakota," he wrote in an email. "Those two states are very aggressive in attracting investment into the states that don't require people and use of water (which is scarce)."

South Dakota is pushing for the creation of trusts in the state in trying to get out-of-state investments, and what Wyoming is doing with cryptocurrency falls in line with what South Dakota is doing, McEowen said.

The only current federal legislation that relates to cryptocurrency is H.R. 3708, which was introduced in September and would allow consumers to make small purchases with virtual currencies up to $600 without having to meet the complicated reporting requirements. Rep. Jared Polis, D-Colo., and Rep. David Schweikert, R-Ariz., who are co-chairs of the Congressional Blockchain Caucus and introduced the measure, tried to add their Cryptocurrency Tax Fairness Act of 2017 to the House version of the tax legislation overhaul in December, but were unsuccessful.

“As for the federal legislation, the wheels of the legislative process grind slowly and this will take some time,” McEowen said. “Cryptocurrency is still viewed largely as a speculative device with widely fluctuating values from day to day. Those in the Congress will be careful before moving on a bill such as that proposed by Rep. Polis."

When Schweikert introduced the bill in September, he said the purpose of the H.R. 3708 was to allow all cryptocurrencies to be used for small everyday transactions, because the U.S. has made cryptocurrency use more of a challenge than it needs to be.

When contacted by Law360, a representative of Schweikert’s office said she did not believe he was following Wyoming’s legislation, but offered remarks later after additional correspondence.

“The congressman’s view is that anything done at the state level is a good start and a way to show small businesses in this space they have willing partners, but this needs to be done at a federal level and needs to be done quickly,” said Katherina Dimenstein, Schweikert’s legislative director.

Polis, the other co-sponsor of the Cryptocurrency Tax Fairness Act of 2017, expressed optimism toward H.R. 3708, saying he and Schweikert introduced the measure because they saw a need to provide certainty for cryptocurrency exchanges and digital wallets, as evidenced by the small amount of IRS guidance from 2014, which does little to help explain what to do when reporting large transactions.

“I will continue to try to move this as a bill or amendment,” he told Law360, because it does not make sense to pay federal tax on a cup of coffee.

As for Wyoming’s law exempting cryptocurrency from state property tax, Polis said it is an example of how states are allowed to set up their own tax systems, and some impose an income tax while other states do not.

“What Wyoming is doing is nothing different than any state when deciding what will be taxed and how much,” he said. “Right now, because H.R. 3708 has not been adopted, it’s unclear to crypto-holders what their tax obligations may be — so until that happens at the federal level, states can continue to do what they want with cryptocurrency regulation.”

--Editing by Tim Ruel and John Oudens.
