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Crypto Tax Report

Breaking new ground.
Illuminating the industry's future.

2020

Accounting Blockchain Coalition

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Foreword

As a long-time tax withholding and information reporting professional, I closely follow tax issues associated with emerging markets. At Sovos – a leading global provider of software that safeguards businesses from the burden and risk of modern tax – I work with some of the most notable exchanges and businesses involved in tax and cryptocurrency. I was excited to contribute to this report as it is a one-of-a-kind opportunity to learn more about the issues crypto investors are experiencing and the viewpoints of other tax and accounting professionals.

Last year's "Crypto Accounting: Insights Report" featured expert viewpoints from tax and accounting professionals. The report painted a picture of an emerging tax and accounting landscape[1], uncovered distinctive issues associated with crypto transactions, and highlighted the ways professionals were creating a framework in the absence of clear government regulation.

This year's report takes into account the flurry of growth and change in taxation that 2019 brought to the crypto industry. The report features a deeper glance at how well-versed investors are in their tax obligations and whether they understand strategies for limiting their exposure. The report also investigates whether practitioners believe the IRS guidance and education campaigns will result in the need to amend prior year returns or whether investors will wind up owing tax and penalty for underreporting.

Building on information that investors need in order to report income taxes correctly, the report examines the area of 1099 information return reporting and how payers that are obligated to issue those forms affect the overall tax process for crypto investors and practitioners alike. Rounding out the report is a survey of the common challenges tax and accounting practitioners face when attempting to prepare returns for crypto investors, and their associated feedback as it relates to technology solutions they could use to solve those issues.

Wendy Walker,
Solution Principal, Sovos

Introduction

Governments were not prepared for the arrival of Bitcoin, cryptocurrencies and various digital assets. And until recently, they did not provide clear direction on how cryptocurrency earnings should be reported. As a result, investors and businesses have struggled to remain in compliance. Even in the midst of new “regulation” that is not yet codified, professionals and investors alike remain confused and uncertain about the future of crypto regulation for accounting and tax.

The Crypto Tax Report 2020 addresses the immediate and future challenges for tax and accounting professionals tasked with reporting on cryptocurrency.

This report includes:

- **The legal and technical challenges accounting and tax professionals face when complying with evolving crypto reporting requirements**
- **Best practices for professionals supporting cryptocurrency clients**
- **Insights from leading crypto accountants and tax practitioners on crypto reporting, auditing, cost basis and taxation**
- **The benefits of modern software for cryptocurrency accounting, tax services and finance operations**

Blox collected all data for this report from U.S.-based verified CPAs that operate in a variety of capacities with cryptocurrency accounting and taxation. Participants range from firm-employed professionals to small-business owners, with some focusing exclusively on taxation. The participants consisted of professionals from across the United States, who facilitate accounting and tax services for cryptocurrency. Several of the professionals included in this report are educators and industry thought-leaders. They participated in this report by answering a series of short- and long-form questions, and Blox performed a statistical analysis based on the final results, experiences and insights of these professionals.

Blox and Sovos Identified 137 crypto tax professionals with CPA qualifications in the United States. Of those, **33 percent** responded to the survey. The number of participants represents a **30 percent** year-over-year increase, suggesting a growing number of crypto-qualified CPAs or a growing number willing to participate in industry reports to help produce more quantifiable data and insights.

Tax Liabilities and Crypto Reporting

Takeaways for this section:

Today's reported number of cryptocurrency investors does not match the reports generated by exchanges and other sources.

Crypto clients are still alarmingly unaware of how to handle crypto reporting and tax liabilities.

In 2020, many clients will work retroactively to ensure they filed prior year taxes according to the latest guidelines.

Tax professionals need complete client records of all cryptocurrency holdings and transactions to correctly report crypto tax and liabilities for clients.

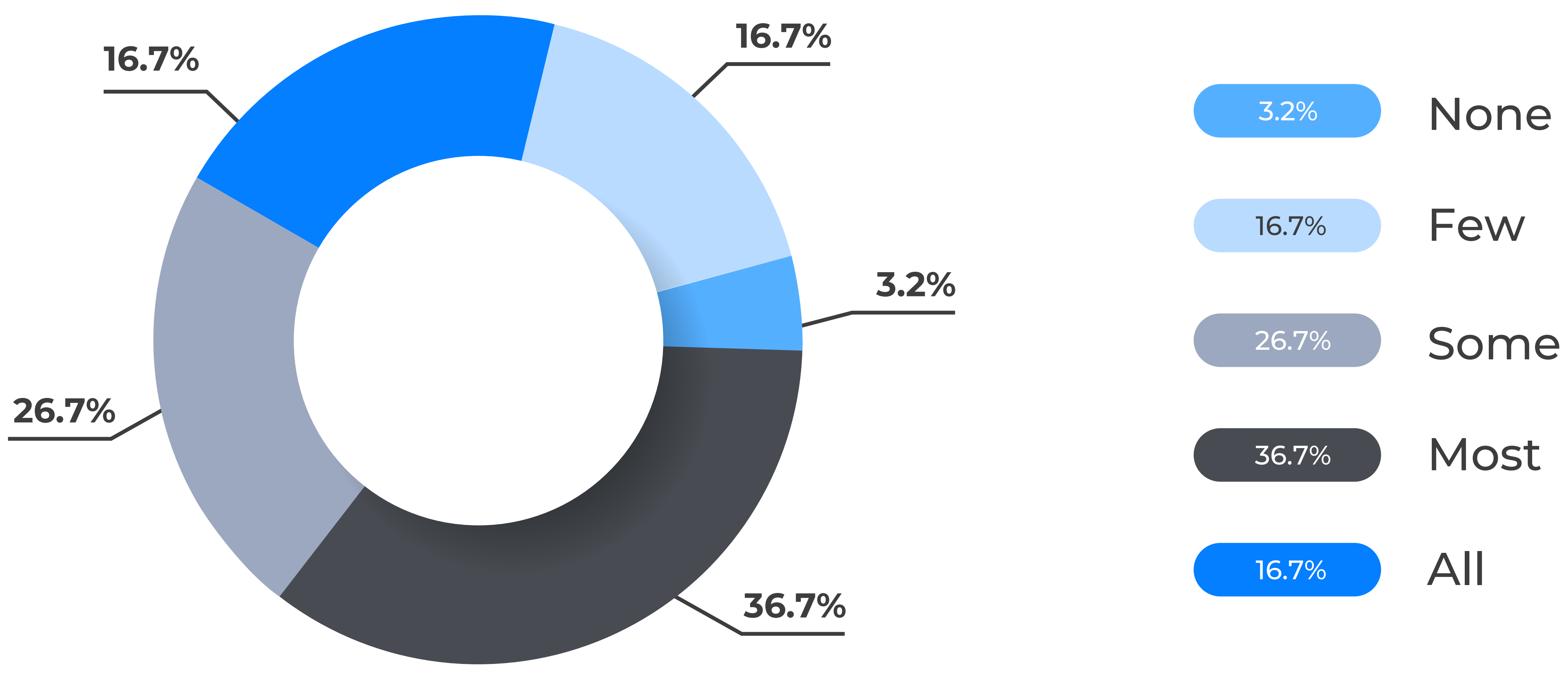
Tax Liabilities

After the birth of cryptocurrencies, few businesses or investors considered that cryptocurrency events such as buying, trading, selling and receiving airdrops would be taxable. The frenzy in the market created a convoluted ecosystem, and, ultimately, an accounting and taxation nightmare. In response, some crypto investors took a more proactive approach to crypto reporting. That group grew after the United States v. Coinbase, Inc. decision, in which thousands of taxpayers' information was turned over to the IRS.

This is not surprising given the lack of IRS guidance and enforcement related to crypto investments. Even IRS Notice 2014-21, which answered some questions, did not fully address how crypto should be reported.[1]

When asked how many of their clients understand taxable crypto events, surveyed professionals believed only 16.7 percent of their clients completely understand. This also indicates that professionals believe that more than half of their clients know very little or nothing at all when it comes to understanding taxable crypto activity.

How well do your clients understand taxable vs. non-taxable crypto events?

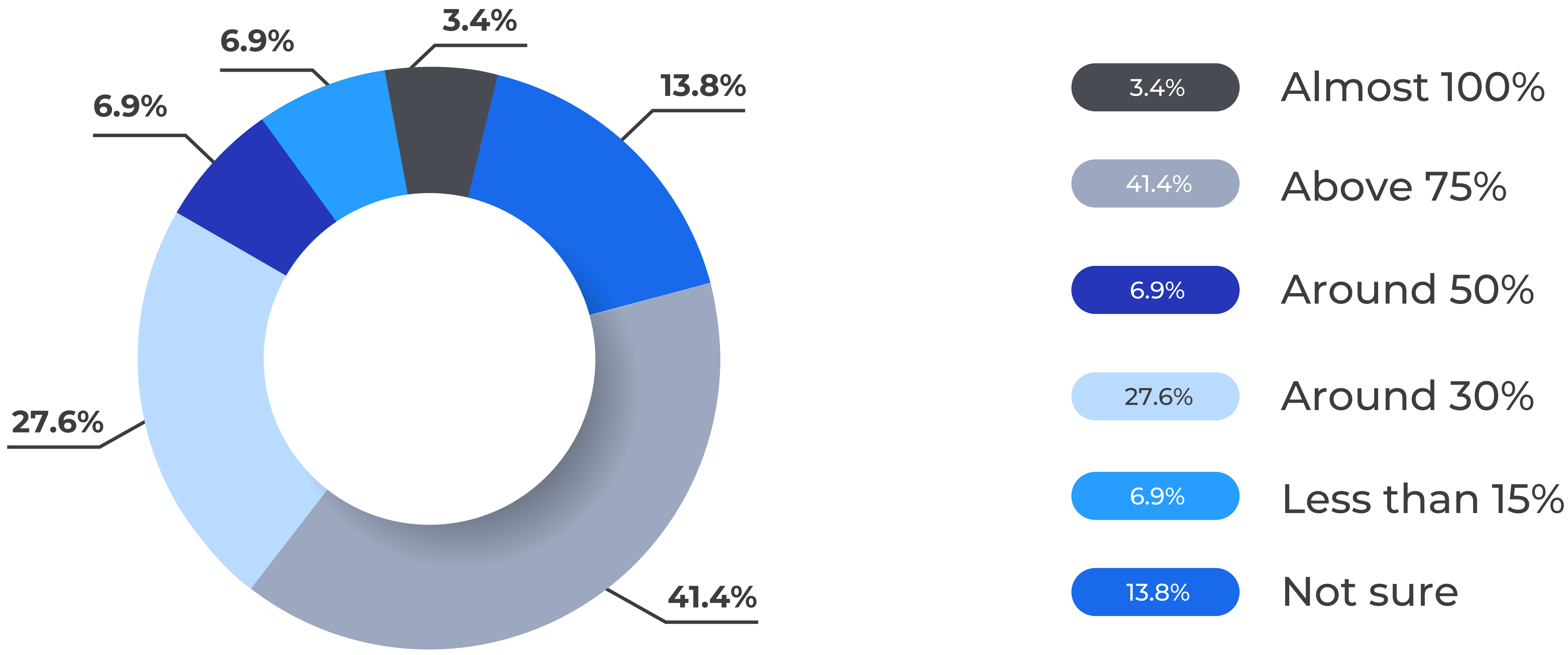


In July 2019, the IRS initiated enforcement and education letters targeted at more than 10,000 taxpayers, saying that the letters "...strive to help taxpayers understand their tax and filing obligations and how to correct past errors." The IRS also sent letters to virtual currency owners advising them to pay back taxes and file amended returns. [2]

Less than **20 percent** of respondents said the majority of their clients expect to be audited for prior years.

These statistics suggest there is still confusion about how to move forward with retroactive crypto tax collection. However, this confusion will be resolved as crypto exchanges [3] , investors and businesses face heightened scrutiny and tax reporting enforcement. **In contrast to their clients, the report finds that more than 50 percent of CPAs believe at least half of their clients likely owe crypto back taxes related to prior years.**

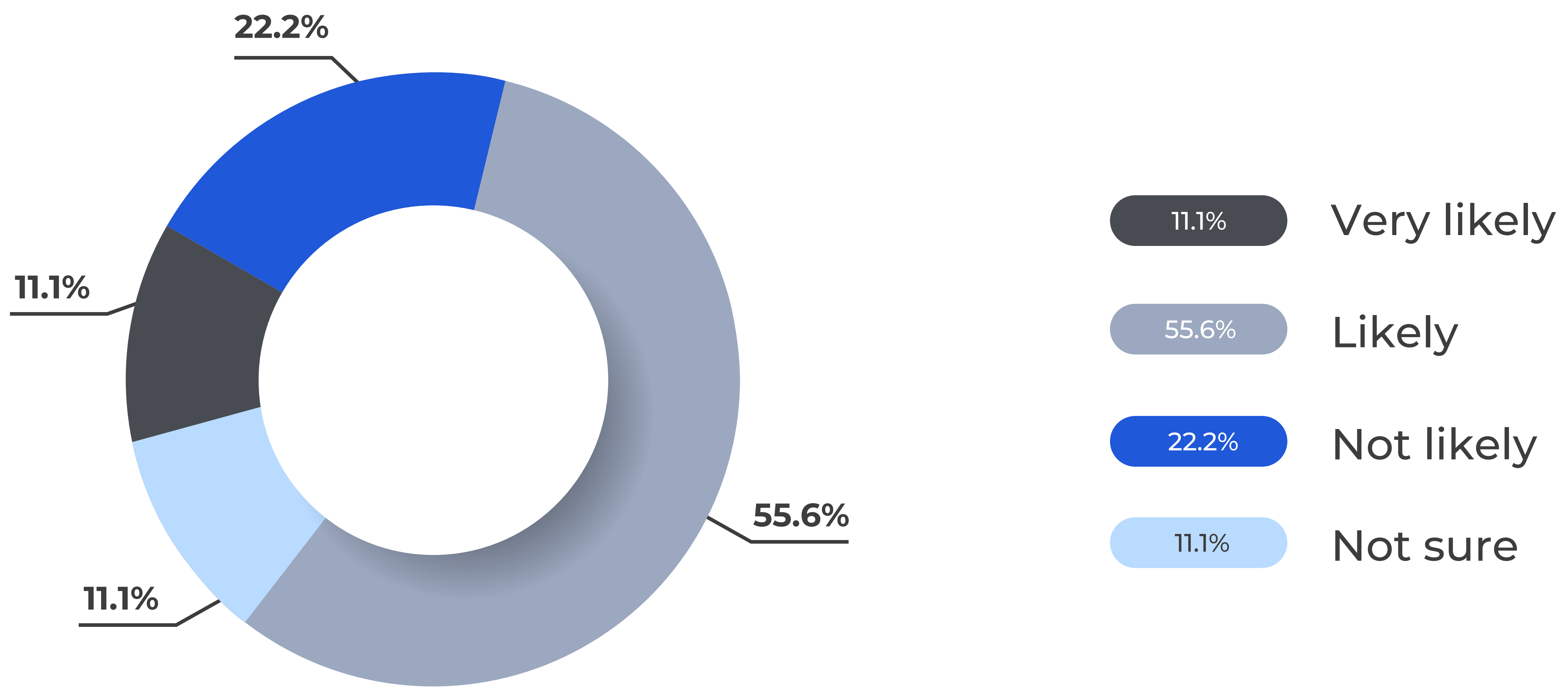
What portion of your clients expect to be audited for back taxes on their crypto holdings/transactions?



As the mainstream media and even the U.S. government publicly equated cryptocurrency to scams, investors became disillusioned. The industry experienced its first "crypto winter" in 2018 and into early 2019. Investors experienced significant losses, and some sought to claim those losses against gains earned for the year, in order to reduce tax liabilities. Unfortunately, many crypto investors didn't report crypto gains that would have allowed them to take those deductions. **From 2015 to 2018, the IRS reported that only about 800 individuals claimed crypto related gains and losses on income tax returns.**[4]

More than two-thirds (65 percent) of CPAs expect crypto clients will face underpayment penalties on their 2019 tax returns. This could be attributed to the fact that many investors have found themselves facing expensive tax obligations due to excess trading and transactions, resulting in high tax liabilities for the year. Another issue could be the lack of clear guidance about how to treat certain transactions for which the taxpayer may have to pay additional income taxes as the IRS gains better understanding of how this industry works.

How likely do you think it will be that crypto holders will have to pay underpayment penalties on their 2019 crypto tax returns?

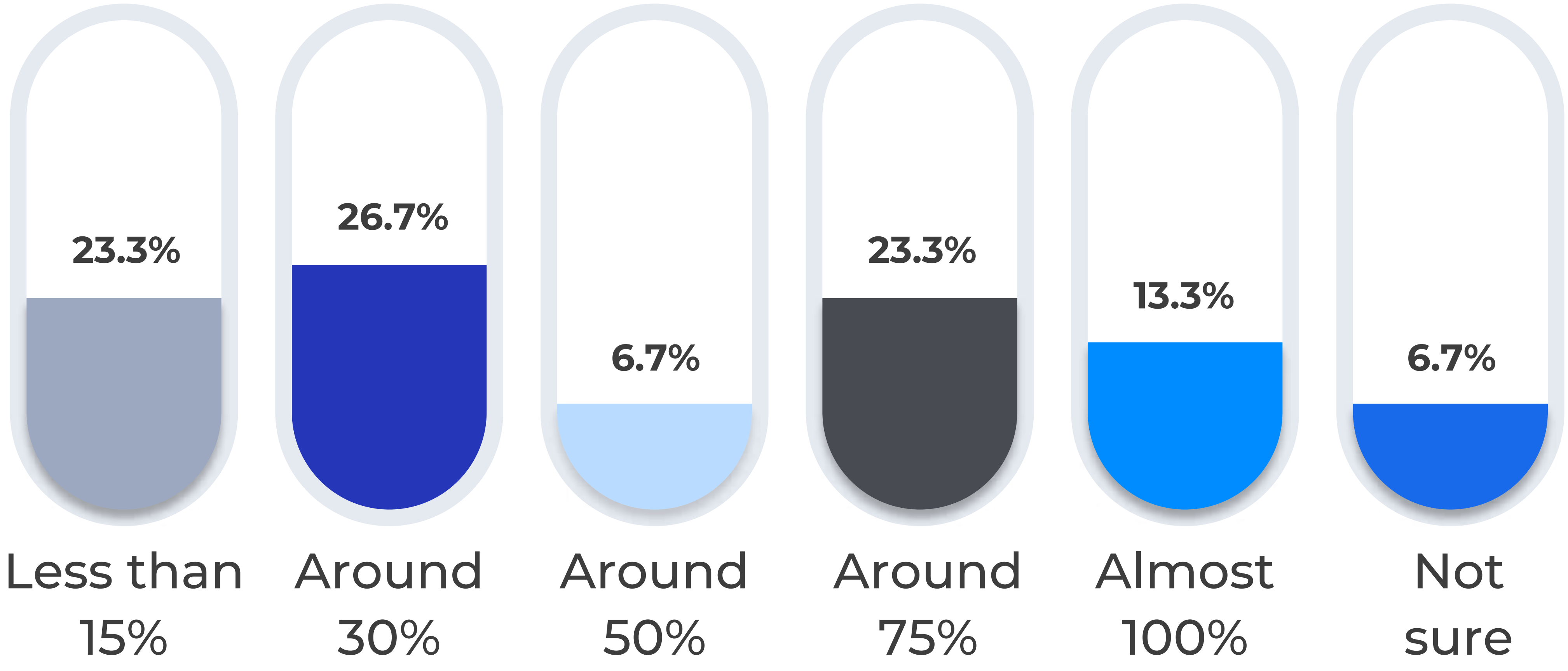


Penalties for underreporting can be costly. But reporting accurately can be costly, as well. **Many investors are still unaware of what is classified as a taxable activity.** Strategies such as tax loss harvesting and donating to offset gains can limit an investor's tax liability.

> **For professionals, having a plan in place and clients that understand how certain decisions have a net positive/negative tax effect, can add so much value.**
>
> Jordan Bass, CPA, Founder of Taxing Cryptocurrency

Cryptocurrency businesses and investors need to seek out education on the proper steps to report their digital assets. However, professionals believe that only **13 percent** of their clients are aware of ways to legally limit their tax liabilities.

How many of your clients are aware of ways to legally limit their tax liabilities?

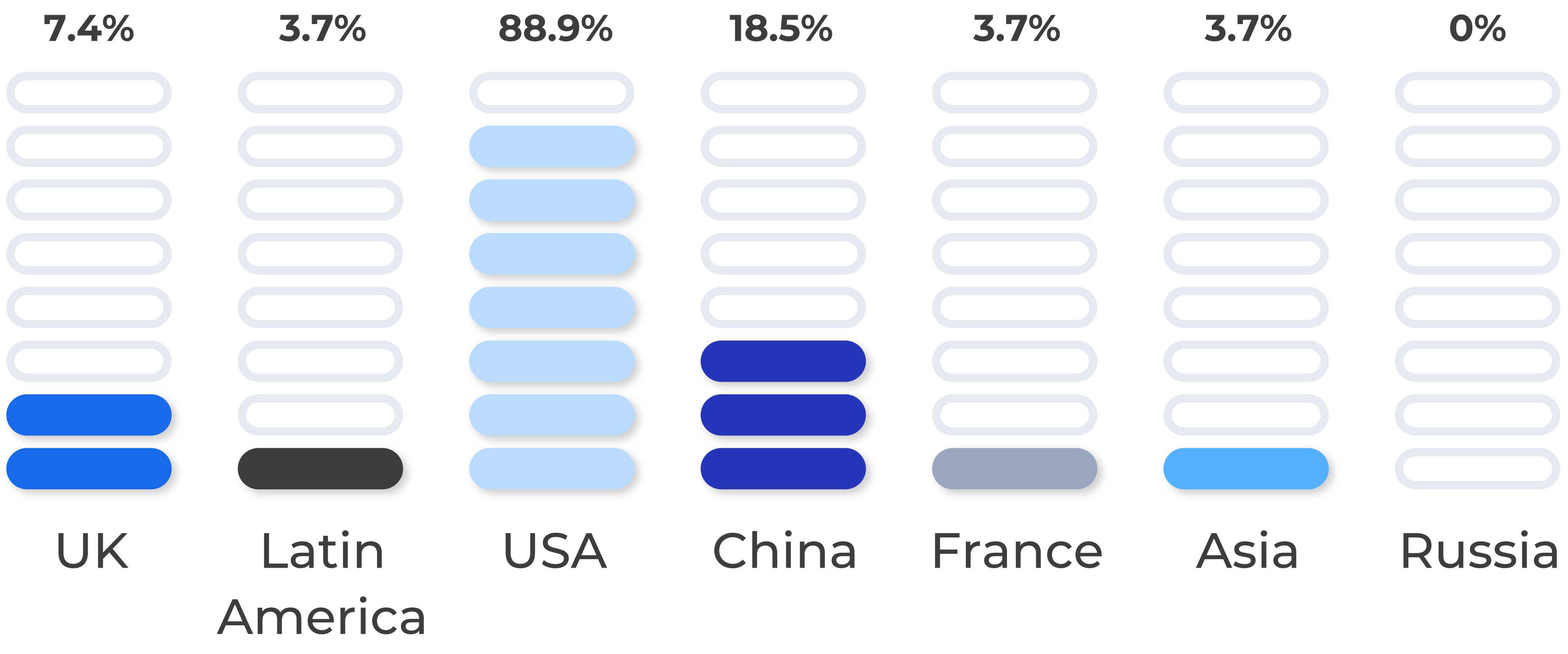


This all speaks to the general confusion and lack of education that affects the industry's accounting professionals. Associations like the Accounting Blockchain Coalition are dedicated to connecting investors and businesses with certified crypto professionals By establishing these connections, the tax accounting and cryptocurrency communities can use each other's expertise to more quickly achieve their goals.

> **This is an evolving space and good tax advice requires a comprehensive understanding of tax law and cryptocurrency transactions. No one should do it alone.**
>
> Nick Cerasuolo, Managing Partner at Blockchain Tax Partners

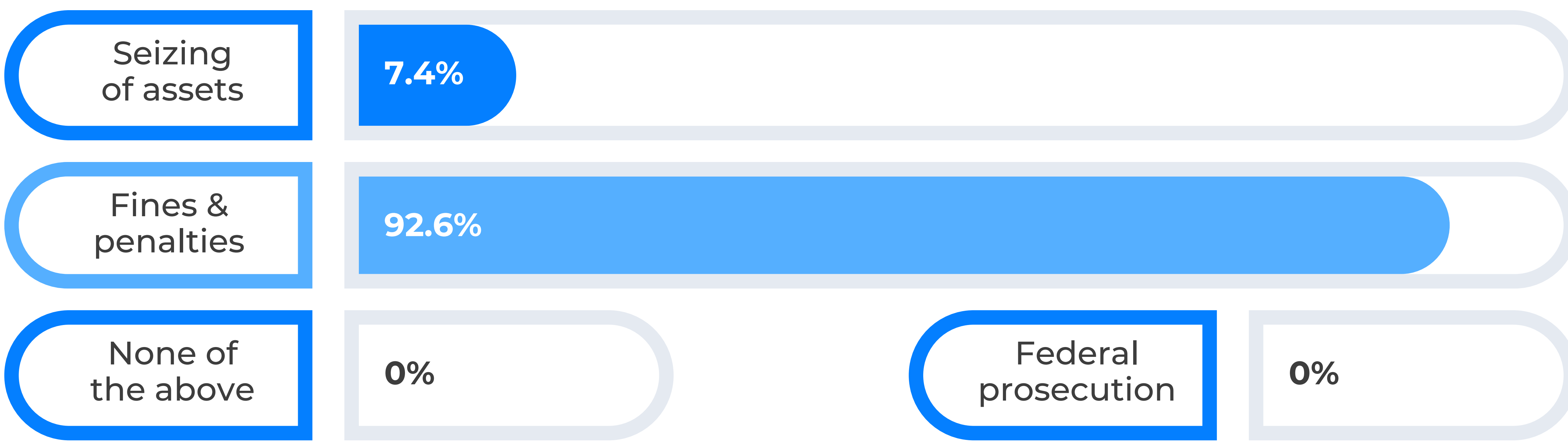
When participants were asked which country would face the toughest crackdown on cryptocurrency, it is no surprise they chose the United States. The U.S. is a powerhouse for advancing regulation and compliance with securities and financial instruments. U.S. tax authorities have already aimed[5] their sights on exchanges to ensure they provide customers and oversight organizations with the necessary data to ensure effective, fair and accurate crypto reporting.

Which country do you expect will have the toughest crackdown on crypto taxes in the next 12-months?



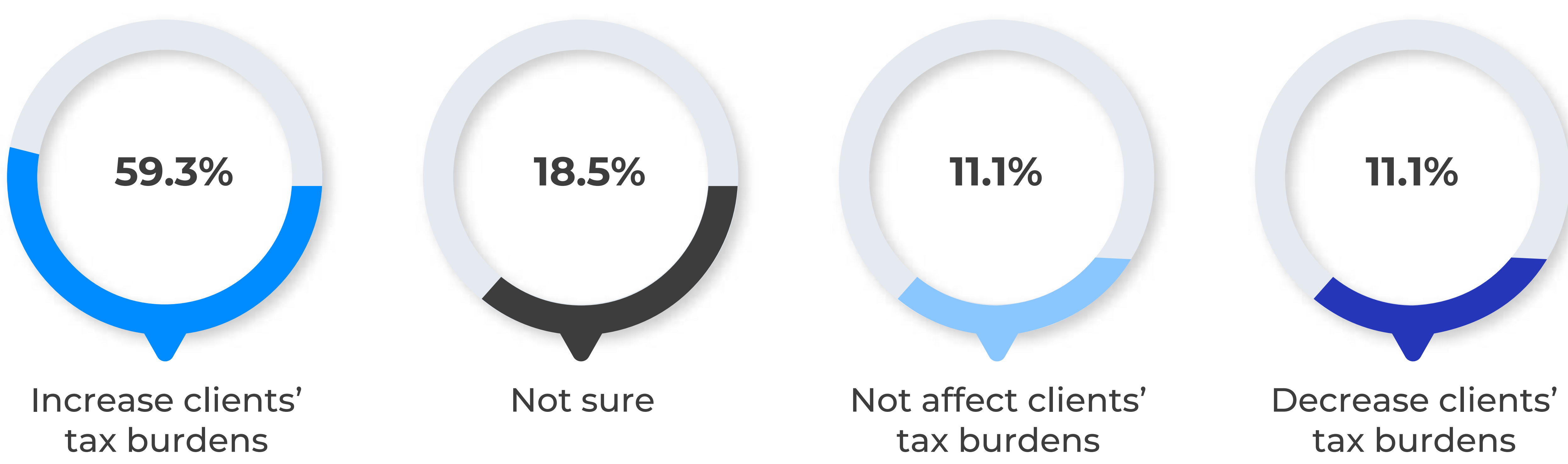
When asked what is the most likely measure the IRS could take for crypto holders who don't pay taxes, **92 percent** of respondents said they believed fines and penalties would be the maximum penalty. Yet, **7.4 percent** believe there is a possibility of asset seizure. The average taxpayer is unlikely to encounter this scenario, but the U.S. government is no stranger to seizing cryptocurrencies. [6] The industry expects investors who report inaccurately will only pay penalties. But these measures can change with one letter from the IRS.

What is the most likely measure the IRS could take for crypto holders who don't pay their taxes?



Many cryptocurrency advocates believe IRS and government involvement in the market goes against the core, ungoverned nature of cryptocurrencies. However, the IRS exists to enforce a code of conduct and collect taxes from any sector, business or individual. Almost **60 percent** of the tax professionals responded to this survey believe the IRS will increase clients' tax burdens.

Generally, do you expect future IRS guidance to...



Crypto Reporting

Most investors will need to report their crypto using traditional tax forms like the 1099. How they should accomplish this varies depending on the type of form they receive from crypto businesses, if they receive one at all.

Takeaways for this section:

- **Forms 1099 are necessary for aiding tax professionals and crypto investors in annual income tax return preparation and overall reporting compliance.**
- **Forms 1099 issued for crypto transactions are often issued inaccurately or not at all.**
- **1099 returns filed by crypto payers are creating challenges for tax preparers and crypto investors.**
- **Managing cryptocurrency cost basis for large volumes of transactions is complex.**

The 1099 form is essential to reporting income for cryptocurrencies, but data consistently indicates underreporting. Cryptocurrency exchanges account for the bulk of crypto transactions, yet many say they do not have a legal obligation to report 1099s for crypto transactions. In Notice 2014-21, the IRS indicated crypto is considered property and the related tax rules apply. However, the IRS did not specify that those transactions are generally reported on Form 1099-B. Even in the most recent guidance in Revenue Ruling 2019-24, the IRS failed to address the confusion surrounding 1099 forms and crypto reporting.

The importance of recordkeeping

Tax preparers and investors rely on Form 1099 information in the traditional markets. Crypto is no different. Without it, the burden of responsibility shifts to the investor, requiring them to keep track of all of their crypto activity for the year. This includes tracking every crypto-related transaction, like fair market value based on the date of purchase or sale of assets. All of this information is vital for preparers to determine cost basis and properly calculate gains and losses. According to crypto tax preparers, therein lies the primary challenge.

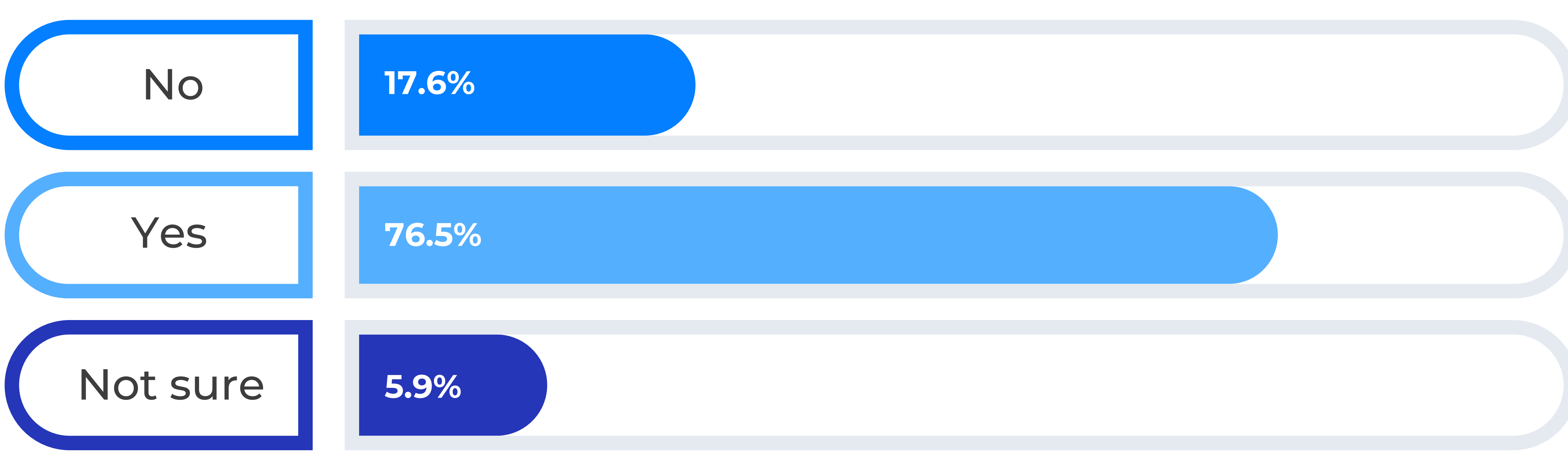
One respondent put it best when they said, “The biggest obstacle as a crypto accountant has been the lack of recordkeeping that a lot of the clients have. Many clients do not keep track of their transactions, exchanges, ICOs, etc... making it more difficult for accountants to trace and properly account for transactions.”

It doesn’t help that the IRS guidance to date has been less than clear. Since the majority of cryptocurrency transactions are related to asset trading, the IRS needs to issue clear guidance related to the 1099 reporting requirements for these transactions in order to combat underreporting of income by investors.

Missing 1099 information

When asked whether a 1099 was issued to their clients for crypto transactions, more than **76 percent** of professionals indicated their clients should be receiving them.

If your clients are not receiving 1099 forms, do you think they should be?

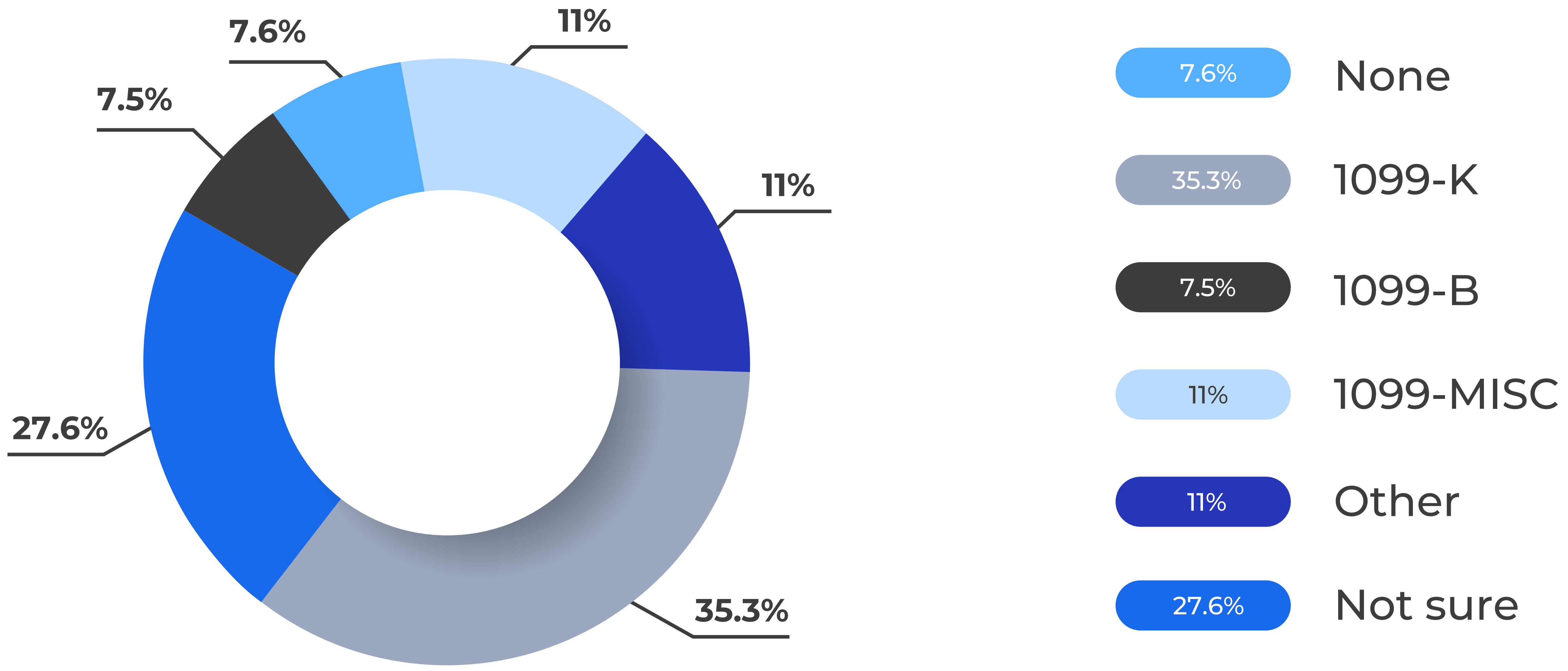


In the traditional markets, investors are accustomed to receiving detailed tax information on stocks and bonds in order to calculate gains and losses. Crypto investors deserve the same treatment. Forms 1099 help taxpayers prepare returns and enable the IRS to automate the enforcement process.

1099-K vs. 1099-B

For those investors that did receive 1099s, a little more than **35 percent** of respondents indicated the information was provided on Form 1099-K, while only a few respondents indicated their clients received Form 1099-B.

What 1099 forms do your clients receive for crypto trades?



Internal Revenue Code (IRC) §6050W states the 1099-K is intended for reporting goods and services transactions for payments made via payment cards and electronic payment platforms. However, many crypto exchanges are using this form to report property-related transactions. This is confusing to tax professionals and investors because investments in other asset classes result in Forms 1099-B being issued.

As one respondent said, "These forms [1099-K] do not take basis into consideration, typically only aggregating the amount that a taxpayer has realized in the transactions without subtracting their adjusted basis in the assets being sold, to determine what gain or loss is recognized."

So, why do some crypto payers choose to issue this form? Some believe there is no obligation to report Form 1099-B. This is likely because IRC §6045 specifies broker reporting for stocks and securities transactions, but that specificity may not eliminate the requirement to at least issue Form 1099-B for gross proceeds amounts.

Another reason some crypto payers opted for the 1099-K was to align with Coinbase. When Coinbase's information was sent to the IRS, it included information for accounts that had received the threshold amounts of at least $20,000 paid over 200 transactions in a calendar year. This is also the threshold for a Third Party Settlement Organization (TPSO) payer reporting Form 1099-K. **In general, filers in all industries want to ensure they are reporting tax information consistently.** So, it is reasonable other crypto exchanges would take this stance given the lack of clarity from the IRS.

Another reason payers opt to report the 1099-K is that it is often far less burdensome than the 1099-B. Form 1099-B is required to be reported for every transaction no matter if it is the same investor, which could result in millions of 1099-Bs that must be issued. Form 1099-K reports the aggregate of transactions by a single recipient. And only when they meet the above thresholds. Fewer forms means less burden.

Impacts of incorrect 1099s

The details on Forms 1099 are necessary for accurately reporting taxable income associated with crypto assets. **However, more than half of the reports CPAs believe their clients do not receive accurate 1099 forms with the data needed for preparing tax returns.**

If your clients are receiving 1099 forms, do you believe they're being accurately prepared?

This could be attributed to the issues that Form 1099-K has created for taxpayers trying to calculate gains and losses associated with crypto. Traditionally, Form 8949 is used to calculate gains and losses from traditional securities transactions. It directs the taxpayer to use information from Form 1099-B that should have been received from the payer. In fact, this form and its instructions were included as guidance material in the IRS enforcement Letters 6173, 6174 and 6174-A sent to crypto investors last fall.

The link between Form 8949 and 1099-B isn't just found in the IRS forms and instructions. **When a Form 8949 is filed and a corresponding Form 1099-B is not also filed to confirm those details, it triggers IRS mismatch notices and penalties to be issued to the crypto investor.** The IRS sends CP2000 letters to the taxpayer to notify them of the mismatch and associated penalty. Shortly after the IRS issued the initial wave of enforcement letters last fall, some crypto investors also received this penalty notice.

Many crypto investors do not possess the proper 1099 information necessary to calculate gains and losses. Therefore the IRS is missing out on a large portion of the information they need to enforce tax compliance. This is similar to what drove the adoption of cost-basis reporting rules in 2008.

Inexperienced and beginner investors

Unfortunately, inexperienced crypto investors and professionals may neglect their reporting burdens until they come of an age where they feel more accountable. With so many millennials and younger generations having instant access to purchase crypto assets, the age of investors is dropping to new lows.[7]

Inexperienced and beginner crypto investors can be more skeptical of governments and may skew the reporting numbers by failing to disclose their assets. Additionally, many of these investors and those uneducated in the trade, may not even realize a tax obligation exists.[1]

Data from Blockchain Capital[8] states that about **30 percent** of people ages 18 to 34, prefer to invest in Bitcoin rather than stocks or bonds. **42 percent** of millennials know of Bitcoin, while only **15 percent** of those 65 and older know of it. Unsurprisingly, 18-to-34-year-olds are the same segment responsible for the rise of digital banks and the fintech industry.

These inexperienced and beginner investors lack the resources and knowledge to properly account for their crypto holdings, which could lead to penalties and other issues. This demonstrates the need for crypto reporting education and training for entry-level crypto investors and holders.

Do-it-yourself reporting

Young investors are not alone. Seasoned investors are also unsure how to account for their crypto assets. Crypto reporting is difficult for investors at all levels. Before they meet with an advisor, investors must retrieve their exchange data and crypto activity for the year. Retrieval has become easier now that exchanges are more forthcoming with user records. However, according to the participants in this report, many investors do not know how to retrieve data from crypto exchanges, and some are not aware they need to retrieve data at all.

Hiring a professional to handle cryptocurrency accounting and tax is an expensive solution. Not only can tax liabilities be exceptionally high, but the fees are often costly. It is also difficult to find a reputable professional with the right knowledge and resources. Untangling complex webs of crypto activity and transactions in multiple accounts and portfolios makes it a daunting task. Even the act of calculating cost basis for approximately 100 crypto transactions can take days.

Firms will charge clients hundreds and sometimes thousands of dollars to handle their annual tax filings. This is an expensive option that is not feasible for many. That is why professionals always recommend investors of any kind stay informed and seek professional support.

However, investors and funds are starting to investigate other alternatives for personal income tax calculation, like software and online services. These new options leverage technology to meet the demands of crypto accounting and tax compliance. These solutions are cheaper alternatives, but are not yet perfect. Research already indicates that lack of crypto accounting technology is a major industry challenge. In the meantime, crypto businesses and exchanges already have access to automation, regulatory and reporting solutions to ensure compliance and protect them and their customers from risk – if they choose to leverage the technology available to them.

> **Seek advice from professionals who have a wide range of crypto accounting and tax experience and who are thought leaders in the space indicating they understand the industry.**
>
> Jagruti Solanki, Technology & Blockchain Partner, Aprio

Crypto Accounting and Tax

The industry is ripe for expansion, but crypto professionals experience several challenges that threaten even further expansion.

The top five challenges for crypto accounting and tax professionals:

1 Missing Client Data

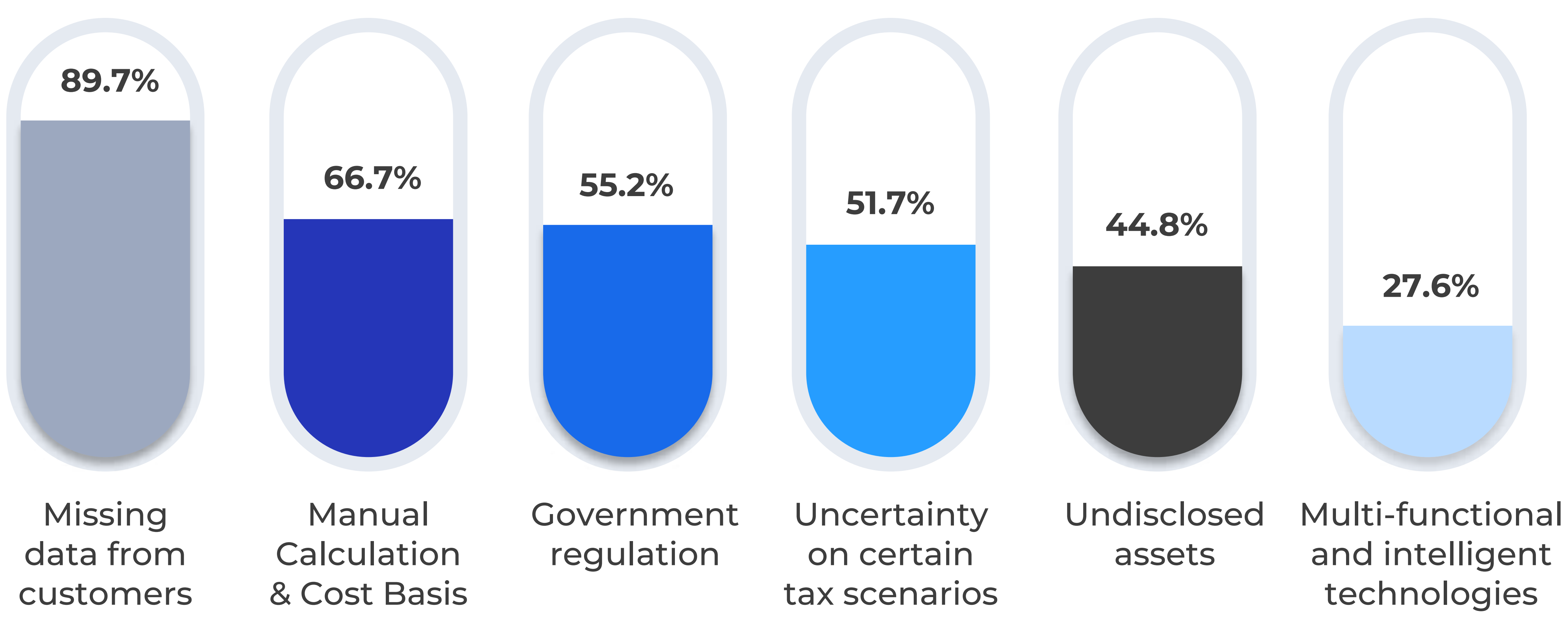
2 Manual Calculations and Cost Basis

3 Government Regulation

4 Uncertainty On Tax Scenarios

5 Undisclosed Assets

As a crypto tax expert or accountant, select any of the following that create your biggest day-to-day challenges? *



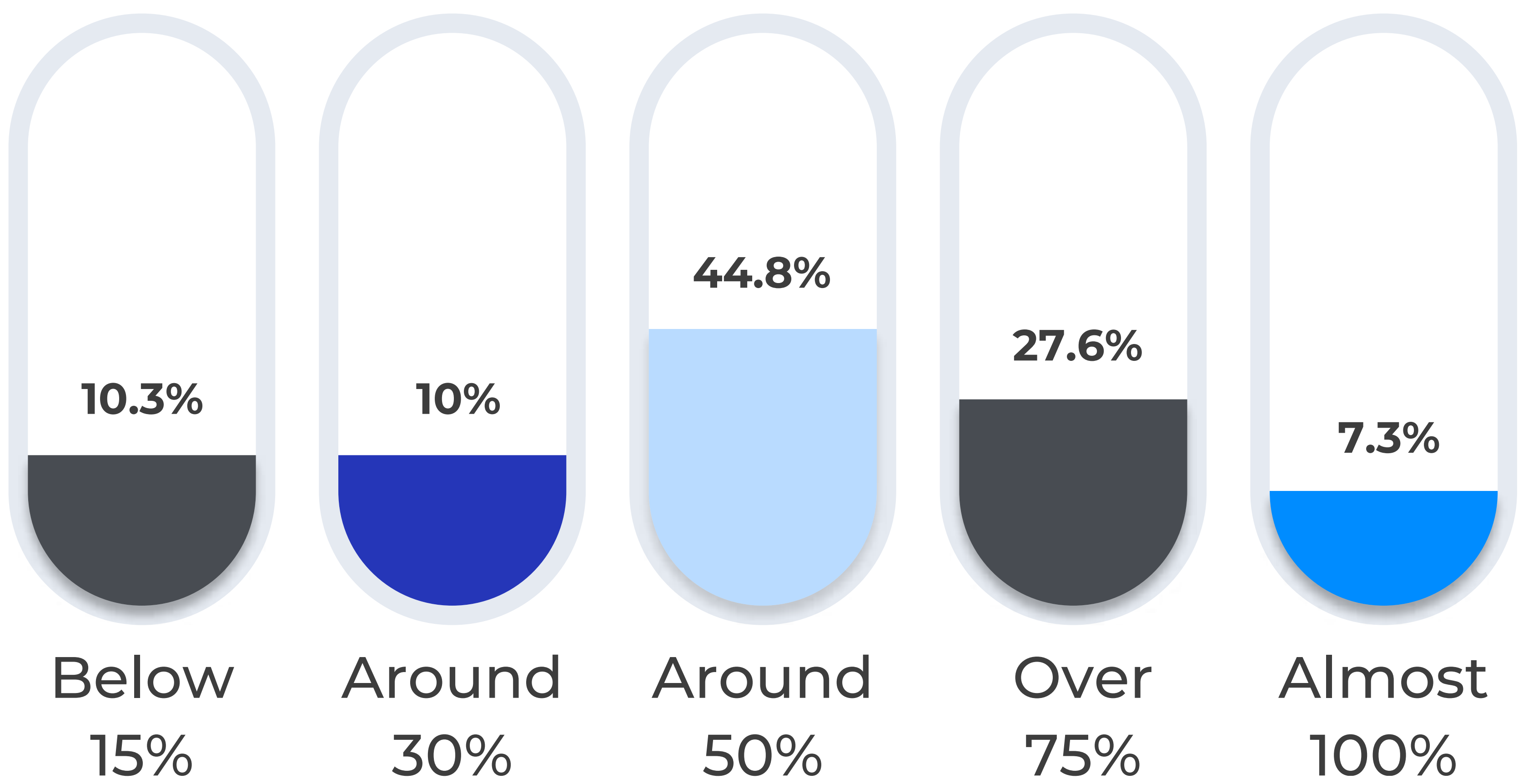
*Respondents could choose multiple selections

Missing data and undisclosed assets

Today's professionals need the most up-to-date and complete historical data of all cryptocurrency transactions, across every wallet and exchange. In order for firms to properly calculate cost basis and effectively assist clients, clients must produce a crypto transaction history directly from the source.

Many professionals believe that less than 50 percent of their clients have access to their full crypto transaction data. This means there is still a significant gap to fill. Crypto exchanges have tried making it easier for users to obtain these essential records. However, many exchanges have succumbed to hacks, legal scrutiny and internal finance troubles. This indicates it is still difficult for many users to retrieve personal crypto records.

What percentage of your clients have access to their full crypto transaction history?



Crypto calculations are inherently complex given the volume and intricacy of transaction activity. **When professionals operate without all the necessary information, they are effectively powerless, which may create higher than normal tax liabilities.**

Professionals claim that most undisclosed assets and activity remain undisclosed because investors know that disclosing them will create an expensive tax liability. Report participants ranked undisclosed assets the fifth biggest challenge at almost **45 percent**. Without a complete crypto history, including all digital assets and transactions, it is impossible to gather accurate reporting calculations.

With investors constantly triggering taxable events and the IRS increasing enforcement, data completeness is imperative. For example, when calculating cost basis, one byte of data can cost a business thousands and even millions of dollars.

Failing to report assets is increasingly problematic, but not just for accounting professionals and tax practitioners. The IRS has ramped up its efforts[9] to zero in on the culprits that refrain from reporting their transaction activity. Failing to disclose assets will likely not lead to jail time, but it could lead to penalties of up to $250,000 and in some cases, a legal investigation. For payers, failure to report 1099 penalties can reach $3.3 million USD for large businesses, and, in some cases, no maximum cap if intentional disregard of the requirements is discovered. In other words, being safe is less expensive than being sorry.

Realized and unrealized gains

Tax loss harvesting can serve investors well should they leverage the strategy. Crypto investors can use underwater crypto assets currently at a loss and apply that loss to other gains from their stock portfolio, reducing investors' annual tax bills.

> **Businesses and investors should sit down at least once a year and analyze their total portfolio to better optimize it for tax purposes. This can include strategies like tax loss harvesting, making a donation to offset some gains or creating a charitable trust.**
>
> Alex Wilson, CPA, Co-Founder of The Giving Block

This highlights the importance of realized versus unrealized gains. During the great hype of cryptocurrencies in 2017 and 2018, many investors sold some of their Bitcoin capital, at a high-value, to purchase inexpensive Altcoins, which quickly became worthless. Due to the lack of tax guidance, investors engaged in hundreds of transactions without ever considering the tax implications. When reporting years later, these investors incurred a confusing and expensive tax obligation. **Many tax professionals believe that if the IRS and government had acted sooner, businesses and investors could have saved millions of dollars.**

In January 2020, the IRS issued further clarity for investors and businesses on tax-exempt charitable donations and organizations. The onus falls on charity organizations to report virtual currency-based donations on Form 990. If these organizations receive virtual currency donations exceeding $5,000 in value, they must also sign Form 8283, to acknowledge receipt of the contribution. But because cryptocurrency is treated as property, all donations are considered non-taxable events. Charities are still required to report the donation and follow the acceptable rules based on the length of time for which the cryptocurrency was held. Holding cryptocurrency for longer than one year would allow them to deduct the fair market value at the moment of donation. Should it be within one year, they would likely deduct the cost basis at the moment of donating.

There is no longer any justification for investors and businesses that fail to report. The IRS is meeting ignorance and negligence with a firm hand. The best way to circumvent punishment is to be prudent, proactive and transparent with crypto activities. Honest, accurate reporting will build trust between crypto investors and tax authorities.

Manual calculations and cost basis

When individuals file annual taxes, some will use their family accountants or large firms to handle their business accounts. This is similar for cryptocurrencies, except when calculating crypto cost basis. The basis calculation is an exceptionally difficult and time-consuming task, even for a seasoned tax professional. Conversations with participating tax professionals found that many of their clients came to them because their existing accountants were not familiar with crypto tax practices.

The process is laborious and is only reliable with complete historical data of transactions and crypto activities to define the basis of a digital asset. It often takes days to correctly calculate the basis of 100 transactions. For funds, exchanges and large transaction volume clients, this could require an entire team to complete the basis across millions of transactions.

> **Cutting out the menial tasks is the most important part of the crypto reporting world right now.**
>
> Michael Ryan, CPA, MBA, President at Grey Stone

Today's tax professionals are demanding more from technology. They need software solutions capable of accurately calculating the basis of digital assets quickly and for large volume clients. Traditional stock, securities and other instruments requiring basis have access to a variety of existing software. This demand has ignited a race for companies to compete in building the best technology, capable of meeting the industry's needs.

Government regulation and uncertain tax scenarios

One of the core pillars of cryptocurrencies are their independence from institutions and governments. In some ways, however, the success of crypto is tied to its ability to tap into existing infrastructure and ecosystems. **When crypto is connected to the real world, it becomes infinitely more usable.** But to enter the mainstream, crypto needs to be validated and accepted by the government. Two of the leading crypto challenges according to tax professionals are government and regulation (**55 percent**) and uncertainty on tax scenarios (**55 percent**).

> **The biggest obstacle has been advising clients on how to navigate through the current regulatory environment for cryptocurrency. There is a lot of uncertainty with respect to how to handle specific tax matters for digital assets and we don't have historical precedent to refer to.**
>
> Curt Mastio, CPA, Founder of Founder's CPA

Without government regulation, crypto companies and blockchain businesses can't open a bank account or operate with their crypto funds. Cryptocurrencies and their businesses need to be approved by governments. Without regulation, the industry will be extremely limited.

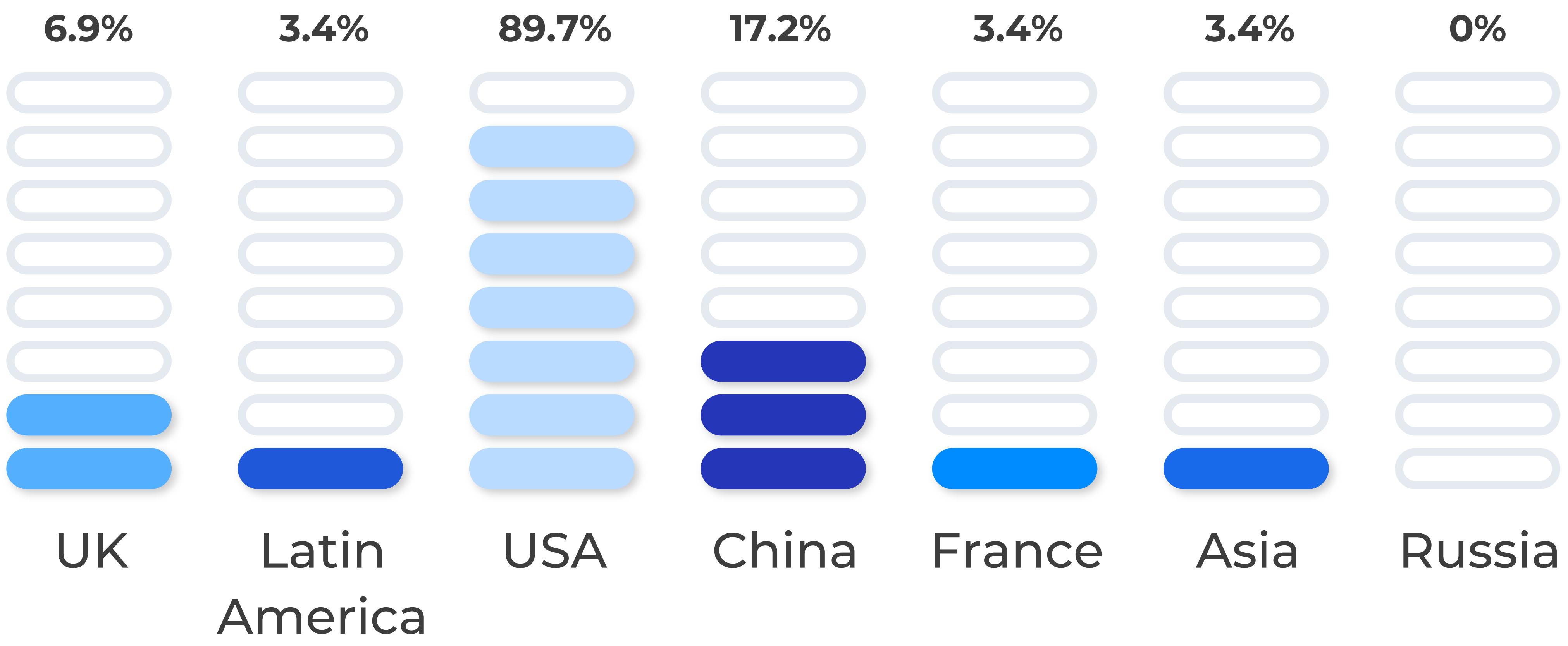
Multi-functional and intelligent technology

Traditional accounting and tax have many software-as-a-service (SaaS) options that cater to individuals, small businesses and even corporations. In the world of cryptocurrencies, the apps and services have left professionals needing more. 2020 is expected to usher in the highest crypto reporting numbers ever, and software will help to increase those numbers and their accuracy.

In 2019, the Crypto Accounting Insights Report confirmed that digital tools are improving productivity and revitalizing tax software for digital assets. The potential is endless. Tools are being built to help auditors track cryptocurrency activity to the source. And platforms are making it easier to reconcile transactions in an automated fashion. The entire industry can benefit from the advantages of automation, synchronization, big data, artificial intelligence and machine learning.

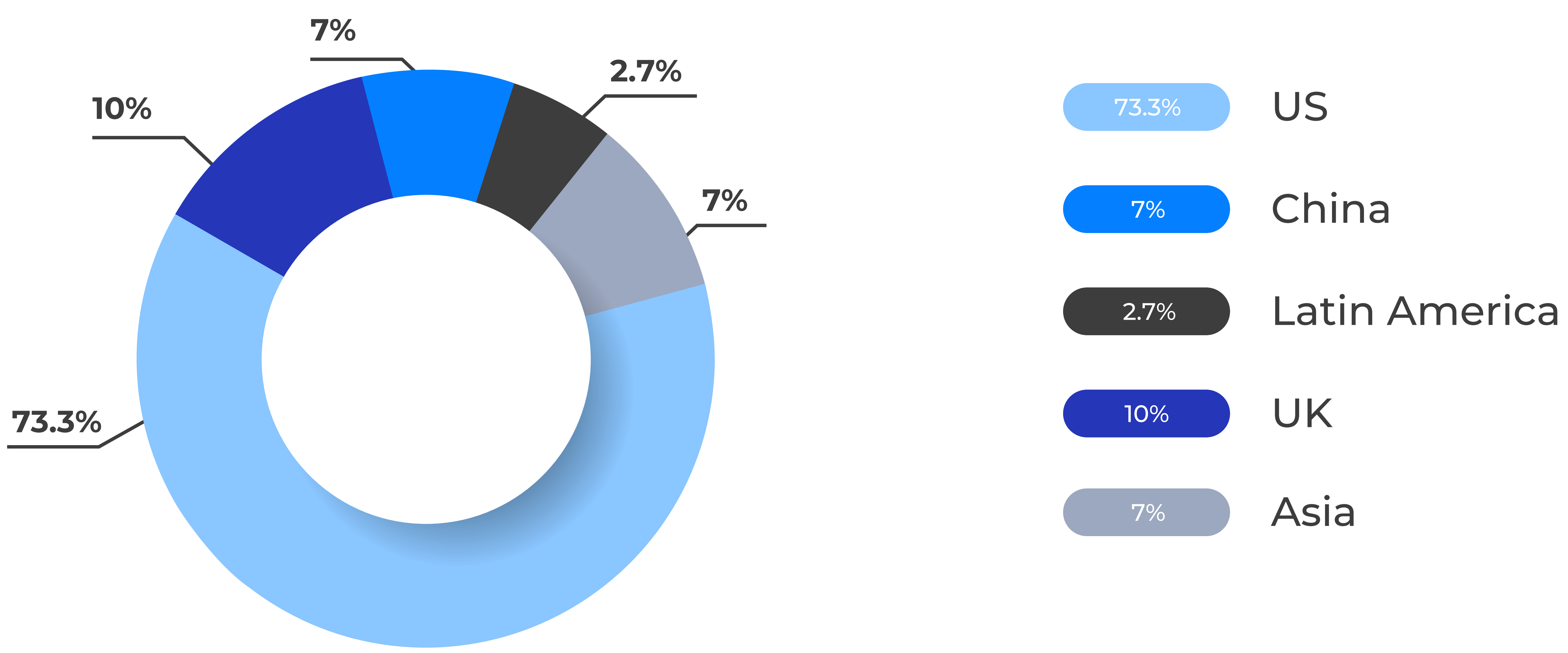
Almost 90 percent of tax professionals believe that in the next year, the U.S. will undergo the toughest crackdown on crypto taxes. There is a chance the IRS will be lenient with those who cannot access their transaction records. While no official regulation has been set in stone, crypto accounting and tax professionals agree that it is imperative to start disclosing and reporting all crypto assets immediately, to avoid potential penalties and staying in the good graces of the IRS.

Which country do you expect will have the toughest crack down on crypto taxes in the next 12-months?



The United States is considered the most advanced when it comes to handling complex cryptocurrency solutions and best practices. It's not hard to see why; there are millions of tax dollars at stake. The U.S. is home to some of the most prominent and thriving blockchains (Ripple, Stellar), crypto exchanges (Coinbase, Kraken), investors, professionals (Winklevoss brothers, Vitalik Buterin) and hundreds of operations.

Which market do you think is the most advanced when it comes to complex accounting solutions and best practices for digital assets?



The United Kingdom has distinguished itself with its thriving fintech ecosystem, but that system is far more aligned with traditional finance. And it has produced little legal guidance for cryptocurrencies. Instead, the U.K. has decided to wait and see how the U.S. will execute its cryptocurrency tax guidance strategy. It is highly likely the U.S will set the standard for cryptocurrency accounting and tax for the rest of the world.

> **When it comes to crypto accounting and taxation, don't alter your businesses purpose or goals just to have a better result. Instead, investors should engage with the best and most experienced digital asset service providers to work through the obstacles.**
>
> Mark Li, BPM LLP, Partner - Blockchain & Digital Asset Practice Leader

Crypto Tax Technology

All professionals depend on the technology at their disposal to help them complete tasks quickly, efficiently and effectively. The rapid growth of cryptos means tax and accounting professionals, as well as governments, have had to quickly adapt and catch up.

Tax technology providers cannot wait for the much anticipated legal framework needed to better clarify how businesses and investors should report tax information. The IRS is enforcing tax compliance and businesses and investors need solutions that can help them comply now.

Takeaways for this section:

The rising demand for better crypto reporting technology started the race to an all-in-one solution.

Tax professionals still rely on outdated, manual tools for cryptocurrency cost basis, reporting, calculations and other complex tasks.

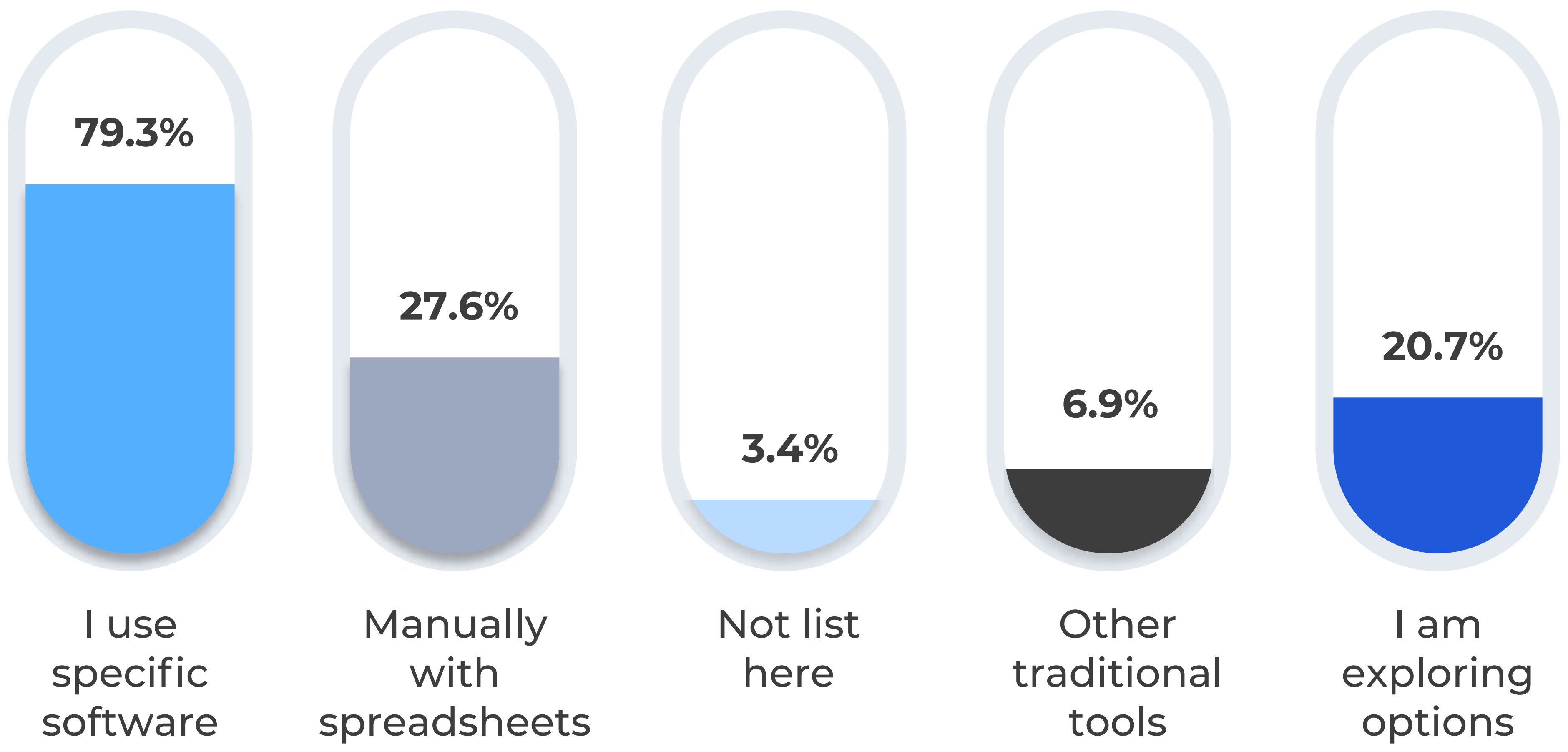
Crypto tax technology must be automated, accurate and trustworthy.

Crypto accounting technology is still in its infancy. Today, most tax professionals use multiple software and a combination of automated and manual operations, with the most prominent being spreadsheets. In time, crypto software will automate the most challenging tasks, like the calculation of crypto cost basis.

Calculating cryptocurrency cost basis is generally considered the most sought after feature for crypto professionals. It has become a benchmark among crypto accounting software companies. Blox asked report participants how they calculate cost basis for their crypto clients and gave them the option of making multiple selections.

Our report found approximately **80 percent** of professionals reported they use crypto-specific software. Yet, **27 percent** continue to manually calculate cost basis using spreadsheets. This spreadsheet method is almost impossible to scale, and it often leads to inaccurate results, sometimes through human error, but typically through incomplete data. Many crypto professionals are exploring new options in order to mitigate this risk.

How do you calculate cost basis for your clients? *



*Respondents could choose multiple selections

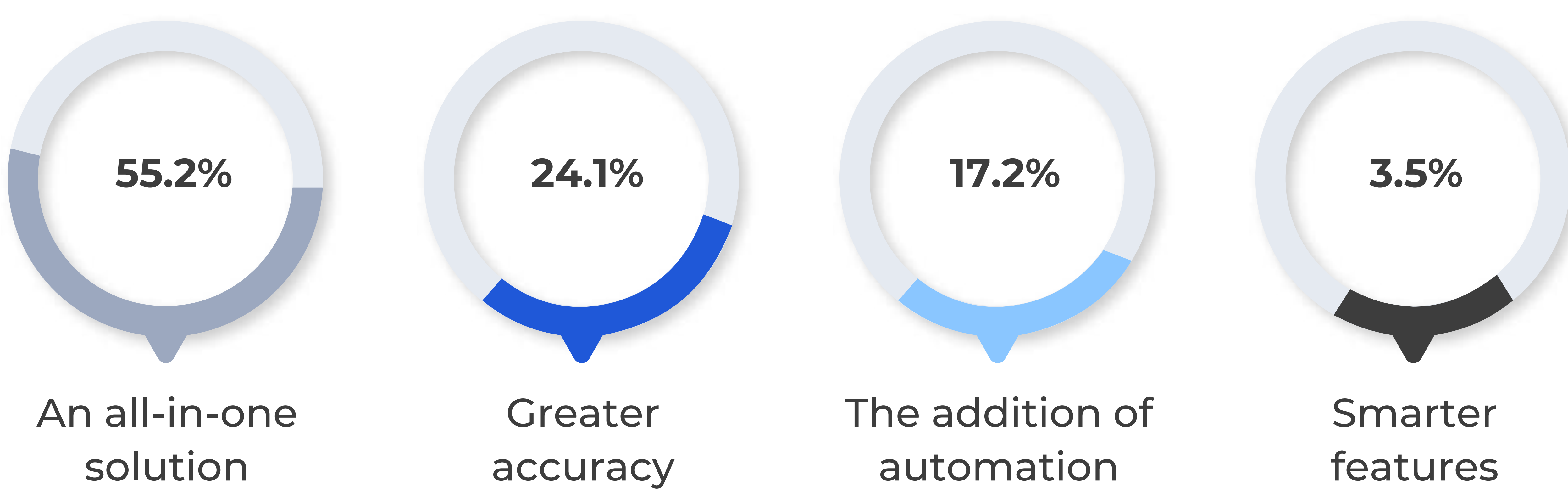
20 percent of professionals are exploring new crypto tax software solutions, indicating there is still a large sector of the industry that is yet to settle on a long-term software solution. There are many competing companies producing crypto accounting and tax software, but none of the incumbents possesses a perfect solution. While some may have one or two essential features, they may lack in accuracy or speed, or vice versa. Moreover, these professionals spend hours on spreadsheets and calculations everyday. They may also rely on several tools or platforms to get their job done faster, but this often creates fatigue and can be inefficient or even lead to inaccurate results.

More than half of professionals want an all-in-one solution that blends the abilities of crypto tax and crypto accounting software. This end-to-end solution would incorporate automation, security and greater accuracy into one robust platform. Unfortunately, today there is no all-in-one platform available.

Crypto payers also desire a modern tax information reporting solution because the IRS and states require a variety of tax information details to be filed in numerous formats. Exchanges and other payers want an end-to-end tax solution that can collate data across multiple platforms and place it in the required outputs no matter the tax jurisdiction.

Every crypto company has unique needs for handling its accounting operations, and those needs can change. Each day crypto exchanges need to track and analyze thousands of transactions and keep records for auditing purposes. Crypto mining operations must be able to track profits and assets for hundreds of cloud-hosted mining rigs. Crypto family funds need access to real-time Net Asset Value in order to provide daily, weekly and monthly reports for investors. Accounting firms and tax professionals may have a variety of these crypto clients in different sectors. The solutions that work for one client, may not work for another.

What do crypto accounting and tax professionals seek from their software/technology to assist them?



However, while tax professionals want an all-in-one solution, their top priority is accuracy. **This report found that 24 percent of professionals are seeking greater accuracy from their crypto accounting and tax technology.** Accuracy is the key differentiator that divides the crypto tax software space. Few platforms provide accurate results when importing, exporting, reporting and calculating. When reconciling transactions or verifying results, accuracy becomes the most important element for professionals. Many professionals and firms use technology to ensure the solution's final numbers match their own results. Conflicting results create a worrisome scenario.

Technology is the best tool the industry has to untangle the wild web of crypto activities and handle large volume activity. Professionals will soon find themselves relying on the automation, speed and accuracy of their software of choice.

Today's crypto professionals may face a daunting set of challenges, but technology is already beginning to respond to their needs. Compliance, bookkeeping, cost basis and tax reporting are becoming more digitized, with more companies and service providers offering smarter services. In 2020, there is no longer a reason to be non-compliant or re-active when it comes to crypto tax and reporting.

Afterword

The convergence of cryptocurrencies and real-world use brought forth a new generation of accounting, tax and finance professionals who must learn to navigate a new digital asset class. Their endeavours continue to be interrupted by shaky legal framework for crypto taxation, which remains scarce and indecisive. Accountants, tax professionals and crypto investors are clamoring for government guidance on reporting, compliance, bookkeeping, cost basis and more. While 2019 saw significant response from the IRS related to individual taxpayer enforcement, guidance in fundamental accounting and tax reporting obligations is still widely unknown for both payers and investors of crypto transactions alike.

As the industry matures, businesses are attempting to set themselves apart by offering tax solutions for their clients. Technology solutions are emerging for accountants and crypto investors, and there are a variety of solutions to aid in trading, forecasting and reporting transactions for tax purposes. The industry is also leaning toward more end-to-end solution concepts to add value to their clients - offerings that track relevant details, provide easy-to-understand information, and calculate cost-basis for purposes of income tax reporting (without the need for external spreadsheets).

Despite the enthusiasm in providing tax information solutions to crypto accounting and crypto investors, crypto businesses continue to neglect to issue and report Forms 1099. In some cases, reporting is inconsistent from exchange to exchange. The IRS and states use Form 1099 information to triangulate income and expenses reported on the crypto investor tax return, and accountants, tax professionals and investors rely on this information to ensure compliance in that process.

While significant progress has been made in crypto accounting & taxation over the past year, there is still a long way to go. Professionals, investors, society and governments need to continue to work together with the mutual understanding that this digital asset class will continue to grow, resulting in the need for agile tax regulatory processes and technical solutions. Collaboration and education can help clarify outstanding industry questions. We look forward to tracking progress in next year's report.

Afterword and Report Authored by Wendy Walker & Michael Soussan

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Blox

Blox is an industry-leading platform for tracking, managing and accounting for cryptocurrency assets. The web-based platform provides crypto accounting professionals with automated and accurate tools to increase productivity and efficiency, while reducing costs, time and resources.

The Blox API engine powers the platform and enables Blox to build rich, flexible and efficient features like a versatile transaction table, automated importing and exporting and an automated and accurate cost basis calculator for reporting, compliance, auditing, taxation and general accounting.

This report was developed with our friends at Sovos and the Accounting Blockchain Coalition. A special thank you to Sovos and the hardworking industry professionals that made this report possible.

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Sovos is a leading global provider of software that safeguards businesses from the burden and risk of modern transactional taxes. As tax goes digital, businesses face increased risks, costs and complexity. The Sovos Intelligent Compliance Cloud is the the first complete solution for modern tax, giving businesses a global solution for tax determination, e-invoicing compliance and tax reporting. Sovos supports more than 7,000 customers, including half of the Fortune 500 and major crypto organizations, including Binance.us, BlockFi, Gemini and Paxos. The company integrates with a wide variety of business applications and has offices throughout North America, Latin America and Europe.

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Accounting Blockchain Coalition

The Accounting Blockchain Coalition has created a forum for CPAs, technology providers, and other industry experts to engage and navigate issues related to the accounting and taxation of digital assets. Over the last two years, ABC has quickly become the go-to source for guidance in the crypto/blockchain space. Through regular working group meetings, webinars, and in-person events, our members are developing frameworks and best practices in the areas of Audit & Accounting, Internal Controls, and Taxation to move the industry forward.

Join ABC to:

- Position your organization as an industry thought leader across our many platforms, including webinars, newsletters, blogs, and events;
- Join our working groups to discuss the latest trends and produce relevant materials and best practices to guide the industry when it comes to accounting for digital assets;
- Priority speaking opportunities and discounted registration for our annual conference that attracts hundreds of accounting blockchain enthusiasts from tech, finance, academia, and the startup community;
- Become a sponsor and get your brand in front of our members and the broader accounting community at events and meet-ups.

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Michael Soussan is the senior marketing and communications manager at Blox.io, an industry leading platform for crypto accounting, tax and asset management. Michael has over ten years of experience in the world of marketing, advertising, PR, social media and content distribution. He is an expert at building co-marketing partnerships, utilizing high-level strategy planning and execution. Before joining Blox, Michael was involved in the Israeli startup sector, and is an active ambassador for cryptocurrencies and blockchain technologies. By employing his decade of cumulative industry experience, Michael continues to leverage his personal insights to spearhead a diverse range of successful marketing projects, with some of the industry's most notable brands.

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