Bitcoin and Virtual Currency: What happens if my company decides to accept it?

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Agenda

What happens if my company decides to accept it?

• Increasing use in the marketplace
• How do I Account for it
• How do I Tax it
• How do I Reduce the Risk
Virtual Currency: Rapid Increase in the Marketplace
Virtual Currency: Current Market Cap

Bitcoin’s Market Cap is 14x Larger Than the Next Altcoin, up 6x from End of 2014

<table>
<thead>
<tr>
<th>Rank</th>
<th>Name</th>
<th>Market Cap</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Bitcoin</td>
<td>$3,428,547,561</td>
</tr>
<tr>
<td>2</td>
<td>Ripple</td>
<td>$245,984,620</td>
</tr>
<tr>
<td>3</td>
<td>Litecoin</td>
<td>$62,695,671</td>
</tr>
<tr>
<td>4</td>
<td>Dash</td>
<td>$20,785,772</td>
</tr>
<tr>
<td>5</td>
<td>BitShares</td>
<td>$16,084,946</td>
</tr>
<tr>
<td>6</td>
<td>Dogecoin</td>
<td>$12,518,429</td>
</tr>
<tr>
<td>7</td>
<td>Stellar</td>
<td>$12,222,510</td>
</tr>
<tr>
<td>8</td>
<td>Nxt</td>
<td>$9,887,171</td>
</tr>
<tr>
<td>9</td>
<td>MaidSafeCoin</td>
<td>$8,090,823</td>
</tr>
<tr>
<td>10</td>
<td>Paycoin</td>
<td>$7,683,946</td>
</tr>
</tbody>
</table>

Data source: CoinMarketCap, data as of 1st Apr 2015
Virtual Currency: Increase in Trading Volume

Bitcoin’s Price Decline Has Not Stopped Exchange Trading Volume From Trending Up

Monthly Bitcoin Trading Volume

Data sources: Blockchain, CoinDesk, Bitcointy

State of Bitcoin Q1 2015

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Virtual Currency: Increase in Daily Transactions

Bitcoin Transactions Have Been Rising; Average of 10,000 Daily Transactions by Popular Addresses*

- The milestone of 100,000 daily transactions by ‘addresses excluding popular ones’ was reached in February, which is two months later than total transactions.

Source and note: Blockchain.info, * 100 most popular addresses.
Virtual Currency: Increase in Corporate Acceptance

Growth of New Bitcoin-Accepting Merchants Remained Slow in Q1

Number of New Bitcoin-Accepting Businesses Added Each Quarter

Sources: CoinDesk, CoinBase, BitPay, International Business Times

State of Bitcoin Q1 2015

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Virtual Currency: Increase in Corporate Acceptance

More than 88,000 Merchants Now Accept Bitcoin, up from 82,000 in Q4 (+7%)

Data sources: Coinbase, BitPay

State of Bitcoin Q1 2015
Virtual Currency: Increase in Corporate Acceptance

Blockchain’s Quarterly New Wallet Growth Rate Has Been Remarkably Consistent

No. of New Wallets Added Each Quarter

Data Source: Blockchain.info
Virtual Currency:
Larger Companies now accepting Bitcoin

Companies Representing >$180 Billion in Annual Revenue Now Accept Bitcoin

Top 10 Largest Bitcoin-Accepting Retailers

<table>
<thead>
<tr>
<th>Rank</th>
<th>Company</th>
<th>Annual Revenue ($bn)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Microsoft</td>
<td>86.8</td>
</tr>
<tr>
<td>2</td>
<td>Dell</td>
<td>56.9</td>
</tr>
<tr>
<td>3</td>
<td>Dish Network</td>
<td>13.9</td>
</tr>
<tr>
<td>4</td>
<td>Expedia</td>
<td>5.0</td>
</tr>
<tr>
<td>5</td>
<td>Intuit</td>
<td>4.5</td>
</tr>
<tr>
<td>6</td>
<td>Monprix*</td>
<td>4.3</td>
</tr>
<tr>
<td>7</td>
<td>Time Inc.**</td>
<td>3.4</td>
</tr>
<tr>
<td>8</td>
<td>NewEgg</td>
<td>2.8</td>
</tr>
<tr>
<td>9</td>
<td>Overstock</td>
<td>1.3</td>
</tr>
<tr>
<td>10</td>
<td>TigerDirect*</td>
<td>1.0</td>
</tr>
</tbody>
</table>

Total $179.9

*Monprix is a private company; most recent revenue data is from 2005. TigerDirect estimate provided by parent company investor relations. Other divisions that are part of a larger parent organization, but do not break out individual divisional revenues, are excluded.

**The revenue is Time Inc. FY 2013 revenue

Sources: CoinDesk, Coinbase, BitPay, companies’ annual reports
Bitcoin & Virtual Currency: How do I Account for it?
How do I Account for it?

The Five Types of Bitcoin User

1. People who want a cheap, fast, global online payment experience

2. People who want access to a new suite of consumer payment applications

3. People who want to connect to the global economy for the first time

4. People who believe bitcoin is an attractive investment

5. People who value financial privacy

Sources: CoinDesk, Coinbase Blog
How do I Account for it?

• Is it as a Capital Asset or Inventory Item?
• How do I Value It?
• How do I prove its Existence?
Bitcoin & Virtual Currency: How do I Tax it?
Federal Government Notice 2014-21

How is virtual currency treated for federal tax purposes?

For Federal Tax Purposes, virtual currency is treated as property, and general tax principles applying to property transactions apply to virtual currency transactions.
What is the basis of virtual currency received as payment for goods or services?

The basis of virtual currency that a taxpayer receives as payment for goods or services is the fair market value of the virtual currency in U.S. dollars as of the date of receipt.

See Publication 551, Basis of Assets, for more information on the computation of basis when property is received for goods or services.
Does a taxpayer have gain or loss upon an exchange of virtual currency for other property?

Yes. If the fair market value of property received in exchange for virtual currency exceeds the taxpayer’s adjusted basis of the virtual currency, the taxpayer has taxable gain. The taxpayer has a loss if the fair market value of the property received is less than the adjusted basis of the virtual currency.
What type of gain or loss does a taxpayer realize on the sale or exchange of virtual currency?

The character of the gain or loss generally depends on whether the virtual currency is a capital asset in the hands of the taxpayer. A taxpayer generally realizes capital gain or loss on the sale or exchange of virtual currency that is a capital asset in the hands of the taxpayer. (e.g., stocks, bonds) A taxpayer generally realizes ordinary gain or loss on the sale or exchange of virtual currency that is not a capital asset in the hands of the taxpayer. Inventory and other property held mainly for sale to customers in a trade or business.
Bitcoin Virtual Currency: How do I tax it at the State Level?
Virtual Currency: States Providing Guidance
The measure of tax is the total amount of the sale, lease or rental price as the case may be, valued in U.S. dollars, whether received in U.S. dollars or otherwise.

The measure of tax from a barter or exchange transaction includes any amount allowed by a retailer to the customer for property or services of any kind:

• When a sale is made where the consideration is virtual currency, the measure of tax from the sale of the product is the amount allowed by the retailer in exchange for the virtual currency (generally, the retailer's advertised selling price of the product).
Example: A restaurant sells a taxable meal to a customer with an advertised menu price of $50. The customer pays the restaurant 0.065 Bitcoin for the meal. The measure of tax from the sale of the meal is $50, which is the amount allowed by the retailer for the 0.065 Bitcoin at the time of the sale. Similarly, the restaurant sells a taxable meal to a customer with the menu price of $50. The customer pays the restaurant 1 Bitcoin for the meal. The measure of tax from the sale of the meal is still $50. The restaurant should retain a copy of the menu in its records to document the measure of tax from its virtual currency transactions.
Retailers accepting virtual currencies as payment should retain documentation on the amount for which they regularly sell the same or similar property to their customers when payment is made in U.S. dollars.
For Kentucky sales and use tax purposes, Bitcoins are the “consideration” provided by the purchaser in the transaction. Any business that accepts Bitcoins as a form of payment must convert the Bitcoin into U.S. dollars, and charge 6 percent Kentucky sales and use tax on any taxable transaction for which Bitcoin represents the financial instrument of consideration. Documentation must be maintained to verify the value of Bitcoin at the time of the transaction.
ISSUE:
– Is Applicant required to collect and remit sales or use tax upon the transfer of Bitcoins through Applicant's ATM?

RESPONSE:
– No. Applicant is not required to collect and remit sales or use tax upon the transfer of Bitcoins through Applicant's ATM.
The New Jersey Division of Taxation issued the following guidance regarding virtual currency and cryptocurrencies:

- Sale is treated as a barter transaction;
- Sales tax is due based on the amount allowed in exchange for the virtual currency;
- the customer owes tax based on the market value of the virtual currency at the time of the transaction in US Dollars; and
- for purposes of Corporation Business tax and Gross Income tax, taxpayer will realize gain or loss on the sale or exchange.
A seller making sales in New York State that accepts convertible virtual currency in exchange for taxable goods or services must:

- register for sales tax purposes;
- record in its books and records the value of the convertible virtual currency accepted at the time of each transaction, converted to U.S. dollars;
- record in its books and records the amount of sales tax collected at the time of each transaction, converted to U.S. dollars; and
- report such sales and remit any sales tax due in U.S. dollars when filing its periodic sales tax returns.
Example 1:
An online retailer registered for NYS sales tax purposes accepts virtual currency from a customer as payment for home décor items that will be delivered in New York State. In effect, the customer has purchased the home décor items in exchange for the virtual currency, and the retailer has purchased the virtual currency in exchange for the home décor items. Because home décor items are taxable, the customer owes sales tax based on the taxable receipt for the purchase of the items. The taxable receipt is the fair market value of the virtual currency in U.S. dollars at the time of the transaction.
Example 2:
A vendor in New York State that accepts convertible virtual currency as payment creates custom computer software for sale to a client. The custom software is delivered to a New York location. Since the sale of custom software is not subject to sales tax, this barter transaction is an exchange of a non-taxable product for non-taxable convertible virtual currency. No sales tax is due on this transaction.
Example 3:

A NYS resident sends her watch to be repaired at a NYS repair shop that accepts virtual currency for its services. Since watch repair services are subject to sales tax, the resident owes sales tax based on the taxable receipt for the purchase of the service. The taxable receipt for the repair service is the fair market value of the virtual currency at the time of the sale. The repair shop must collect the sales tax and must separately state the tax on any receipt provided to the customer. The repair shop must also record in its books and records the amount of the sale and the sales tax collected in U.S. dollars, and report the sale and remit the sales tax due in U.S. dollars.
• How does tax apply? Tax applies to sales of Tangible Personal Property, Digital Products and Services provided in exchange for virtual currency in the same way as any other sale.

   – Example: Your business sells a taxable widget to a customer. The advertised price is $50. The customer pays you 0.134 bitcoin for the widget. The measure of tax is $50. This is the amount you sell for the 0.134 Bitcoin at the time of sale.

• What if the virtual currency value fluctuates before the business redeems it? It doesn't matter. The measure of the tax is not affected by virtual currency fluctuation.
The sales price from the sale of virtual currency is not subject to Wisconsin sales and use tax because the virtual currency represents an intangible right. When the virtual currency is redeemed for a taxable product, the transaction is completed and the retailer’s tax liability accrues at that time. The tax is computed on the value of the consideration received by the seller, measured in U.S. dollars, as of the date the virtual currency is received.
Bitcoin and Virtual Currency: How do I reduce the risk?
How do I reduce the Risk?

- Controls over Currency Conversion.
- Ensuring Compliance with existing Regulations (SOX).
- Accounting Policies for tracking Crypto currency, specifically around areas where current guidance is silent.
How do I reduce the Risk?

• Policies and procedures to govern dynamic pricing of items that are offered in exchange for Crypto Currency
• What is the impact to systems
• Ensure compliance with State Regulatory Requirements
• Ensure transactions do not violate the FCPA, UK Bribery Act or Bank Secrecy Act
• Data Privacy
Bitcoin and Virtual Currency: Review
Review

• Use is becoming common in the Marketplace
• Tax issues both Fed and State
  – Income, Sales, Property
• How do I Account for it
  – Company's intended Use
• How do I Reduce the Risk
  – Internal Controls
  – Regulatory
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