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BLOG

Crypto Tax Update: New Tax Rules on the Horizon?

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KEY TAKEAWAYS FROM THE PRESIDENT'S WORKING GROUP RECOMMENDATIONS AND PROPOSALS

On July 30, President Trump's Working Group on Digital Assets released its comprehensive "Strengthening American Leadership in Digital Financial Technology" report (the Report). The 160-plus-page report sets forth a series of recommendations seeking to "ensure crypto becomes a hallmark of the new American Golden Age" while outlining a proposed framework for regulating digital assets. A key section of the Report focuses on the taxation of digital assets and sets forth proposals on the modernization of the tax framework to better align with the realities of the digital asset ecosystem. The proposals address a range of substantive tax issues, including the classification of digital assets for tax purposes, the timing and character of income from mining and staking activities, and the tax treatment of stablecoins, and also recommends updates to taxpayer and third-party reporting requirements.

President Donald Trump established the President's Working Group on Digital Asset Markets earlier this year through Executive Order 14178 (the Executive Order), with senior officials from the Treasury Department, Department of Justice, Department of Homeland Security, and other federal agencies delegated to evaluate current regulations and to recommend legislative and regulatory reform for the digital asset sector. The Report represents a mandate of the Executive Order to provide recommendations promoting innovation, protecting consumers, and positioning the United States to assert leadership in the digital asset space.

Below is a brief summary of some of the major tax proposals affecting taxpayers.

RECOMMENDATIONS

- *Making Crypto a New Asset Class* — the Report recommends that Congress enact legislation to treat digital assets as a new asset class for federal tax purposes, rather than categorizing digital assets as securities or commodities under existing classes. To that end, the Report recommends digital assets be subject to modified tax rules applicable to securities or commodities, reflecting their unique characteristics. Specifically, the Report recommends that certain Code provisions, including those governing mark-to-market elections (Section 475), trading safe harbors (Section 864(b)), securities loans (Section 1058) and wash sale rules (Section 1091), should be expanded to apply specifically to actively traded fungible digital assets. Alternatively, the Report recommends that legislation should clarify the circumstances under which a digital asset is treated as a security or a commodity for federal income tax purposes.

- *Legislation for Stablecoin Treatment Needed* — the Report recommends Congress enact legislation to clearly characterize payment stablecoins for federal income tax purposes, as current law does not address their classification. The Report suggests that treating payment stablecoins as debt may be most appropriate but also emphasizes the need for careful consideration of which existing tax rules—including wash sale and anti-bearer bond rules—which would apply to stablecoins.

- *Application of Wash Sale Rules* — the Report recommends Congress amend the wash sale rules to explicitly include digital assets. Current law only applies these rules to securities and not to digital assets. The proposal is intended to address tax planning strategies otherwise unavailable in other asset classes where taxpayers sell digital assets at a loss and quickly repurchase substantially identical assets, thereby claiming a tax loss while maintaining their economic position.

Importantly, the Report advises that payment stablecoins should be excluded from the application of the wash sale rules. Payment stablecoins are widely used as cash equivalents in digital asset transactions and applying the wash sale rules to them would create significant administrative burdens with little tax benefit, especially given the high volume and low value of many stablecoin transactions.

- *Tax Treatment of Crypto Lending Transactions* — the Report highlights the significant uncertainty surrounding the tax treatment of crypto lending transactions, noting that Section 1058, which allows for nonrecognition of gain or loss on loans of securities, does not currently apply to loans of digital assets unless those assets qualify as securities for federal income tax purposes. The Report notes that stakeholders have requested that similar nonrecognition treatment be extended to loans of actively traded fungible digital assets. To address this issue, the Report recommends that Congress enact legislation to amend Section 1058 to extend non-recognition treatment to cover loans of such digital assets, provided the loan terms are substantially similar to those required for securities loans under current law. The Report further recommends that the Treasury Secretary be granted authority to determine when a digital asset is "actively traded" for purposes of the amended Section 1058; this authority would allow Treasury to clarify the differences between standard securities loans and crypto loans.

- *Mark-to-Market Tax Treatment for Digital Assets* — the Report recommends amending Section 475 to include actively traded fungible digital assets, thereby allowing traders in such assets to elect mark-to-market tax treatment similar to that available for securities and commodities. The mark-to-market election under Section 475 is not currently available for digital assets unless those assets qualify as securities or commodities for federal income tax purposes. The Report notes that many digital assets share key characteristics with securities and commodities. To address these concerns, the Report recommends that Congress amend Section 475 to explicitly include actively traded fungible digital assets within its scope.

- *Trading in Securities and Commodities Safe Harbor for Digital Assets* — the Report highlights a significant gap in the current federal tax framework regarding the treatment of digital asset trading by non-U.S. persons. Under existing law, Section 864(b)(2) of the Internal Revenue Code provides a "trading safe harbor" for non-U.S. traders in securities and commodities, which allows non-U.S. persons to trade in securities or commodities through a U.S.-based agent or for their own account without being deemed to be engaged in a U.S. trade or business. As a result, these non-U.S. traders are generally not subject to U.S. federal income tax on gains from such trading activities. The lack of explicit inclusion with regard to digital assets creates uncertainty for non-U.S. persons who wish to trade digital assets through U.S. agents or platforms.

Accordingly, the Report recommends amending Section 864(b)(2) to include actively traded fungible digital assets, thereby extending the trading safe harbors, currently available for securities and commodities, to digital asset transactions. The Report notes that many digital assets exhibit economic characteristics similar to securities and commodities.

The legislative change would allow non-U.S. traders to engage in trading digital assets through U.S. agents or for their own account without being treated as engaged in a U.S. trade or business, while providing needed clarity and consistency.

- *De Minimis Digital Asset Receipts* — the Report recommends that Treasury and the IRS issue administrative guidance addressing *de minimis* receipts of digital assets, such as small-value airdrops, staking, hard forks, and mining rewards for taxpayers who do not operate a node or engage in digital asset mining. Current IRS rules require taxpayers to include the fair market value of these assets in income when they gain control over them, regardless of the asset's value or whether the receipt was solicited. This can result in significant recordkeeping and valuation burdens, often disproportionate to the actual economic benefit, particularly given the rapid fluctuation and frequent loss of value in such assets.

To address these issues, the Report recommends that Treasury and the IRS issue administrative guidance to provide relief for *de minimis* digital asset receipts. This guidance could establish thresholds or simplified reporting for small-value digital asset rewards, reducing compliance burdens for taxpayers who are not engaged in mining or node operation.

- *Timing of Income from Mining and Staking* — current IRS guidance requires taxpayers to include the fair market value of digital assets received from mining or staking as ordinary income at the time they gain dominion and control over the rewards. The Report notes that stakeholders have requested clarification, modification, or reversal of this guidance, arguing that the timing of income recognition for mining and staking rewards should be reconsidered. The Report highlights that stakeholders have raised concerns about the current rules, noting that the existing rules can create tax liabilities before the assets are liquidated and may not reflect the economic reality for taxpayers, especially given the volatility and evolving nature of digital asset markets.

While acknowledging that several legislative proposals that would affect income inclusion have been introduced in Congress, including proposals to defer income inclusion for mining and staking rewards until the year of sale or disposition, or to provide *de minimis* exceptions, the Report recommends that Treasury and the IRS review and consider updating their guidance on the timing of income from mining and staking.

Section 6038D Digital Asset Reporting — Section 6038D, enacted as part of the Foreign Account Tax Compliance Act (FATCA), requires individuals who hold interests in specified foreign financial assets with an aggregate value exceeding $50,000 during a taxable year to report detailed information on a Form 8938. Since Section 6038D does not explicitly reference digital asset accounts, the Report notes that closing that potential loophole is needed to ensure that digital assets held offshore are subject to the same transparency and reporting standards as traditional financial assets. Accordingly, the Report accordingly recommends that legislation be enacted requiring the reporting of foreign digital asset accounts, which would include custodial accounts holding digital assets maintained by a foreign digital asset exchange or other foreign digital asset service provider.

The Report also emphasizes the importance of coordinating these requirements with international standards like the Crypto-Asset Reporting Framework (CARF).[1] If the United States implements CARF, U.S. taxpayers would be required to report accounts with foreign crypto-asset service providers that are obligated to report information on U.S. customers to non-U.S. tax authorities. This coordination would enable the IRS and other taxing authorities to cross-check taxpayer disclosures with information received from foreign digital asset exchanges.

The Report also addresses the issue of duplicative reporting burdens, as information required under Section 6038D (reported on IRS Form 8938) often overlaps with information required in Foreign Bank Account Report (FBAR) reporting filed with the Treasury's Financial Crimes Enforcement Network (FinCEN). The Report recommends streamlining the reporting obligations by allowing a single filing to satisfy both Section 6038D and FBAR filing requirements.

CONCLUSION

The Report's tax proposals reflect a broad recognition that the current federal tax framework is not fully equipped to address the complexities and rapid evolution of digital assets. The overarching conclusion is that comprehensive legislative and regulatory updates are needed to provide clarity, consistency, and administrative efficiency in the taxation of digital assets. With certain Congress leadership appearing to eye a second reconciliation bill affecting tax later this calendar year, stakeholders should closely monitor legislative developments, as significant changes to the tax treatment, reporting, and compliance obligations for digital assets may be on the horizon.

For further information or to discuss how these changes may affect your organization, please contact any member of the Tax Controversy group at Winston & Strawn LLP.

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[1] Crypto-Asset Reporting Framework (CARF) is an emerging international tax transparency standard that requires digital asset service providers to report certain transactions to their home tax authorities, which then exchange information with other participating jurisdictions.

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