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## Taxing Virtual Money: The Bitcoin and the CRA

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New business remains subject to the old taxes. Believing otherwise is wishful thinking. The latest tax topic in the world of technology is the Bitcoin. For those still using old-fashioned e-transfers and PayPal, the Bitcoin is the new currency. Unaffiliated with any country or bank, the Bitcoin works because the parties agree that it should. Bitcoins are accepted by an increasing number of online (and offline) vendors and service suppliers, and can even be converted into real money provided someone with real money agrees. It's like a barter system but without the bartering.

You might object that the Bitcoin has nothing to do with bartering since it is fundamentally liquid. It is fungible. A loonie is worth a loonie and a Bitcoin is worth a Bitcoin. There is no squabbling over how many of my chickens your cow is worth, or which service has the greater value. Fundamentally then, Bitcoins are money, but without the underwriting of a bank or national treasury which, given the experience of recent years, might not be such a bad thing. At least, that is what you might think. But for practical purposes, you would be wrong at least where taxes are concerned.

The CRA posted its position on the Bitcoin late last year and the news was grim for those who thought that only national currencies are taxed and that the Bitcoin heralded a return to a pre-war income tax free nirvana-that-never-was. The Bitcoin or more broadly, digital currency is, we are told, virtual money. It can be bought and sold like a commodity and the receipt of this virtual-money-that-is-sometimes-a-commodity is taxable in the same way as any other income. This is not to say that every Bitcoin transaction is taxable, only that Bitcoins do not make taxable transactions into non-taxable ones.

This is bad news for the wishful thinkers but validation for the champions of stateless money. The rub for the latter bunch,

however, is that the CRA did not bestow the status of money on the Bitcoin. That would have been unhelpful and a little meaningless since one cannot go onto the Bank of Canada website to check the Bitcoin's exchange rate. Instead, the CRA simply said that the Bitcoin is subject to the same rules as barter transactions, meaning that Bitcoins are to be valued according to the goods or services for which they are exchanged. Sadly, then, despite its fungibility, the Bitcoin leaves us still asking after the underlying value at tax filing time.

It must also be recognized that when Bitcoins are bought and sold like a commodity arbitrated like any other currency their disposition must give rise to income or capital gains according to whether they are traded on income, or held on capital, account.

The takeaway is this. First, tax has always applied to non-cash receipts, such as are realized upon share exchanges, stock dividends, dividends in kind, shareholder benefits, employee benefits and, yes, even barter transactions unless carefully structured to access a specific exemption or deferral. Whether you are paid in dollars, Bitcoins or ham sandwiches, there is a value to what you receive and you are taxed on that value. Were it otherwise, tax planning would be simple and tax planners could all retire comfortably financed by the tax-free accruing Bitcoin. Second, although the Bitcoin and its digital ilk may have the hallmarks of real money, the distinction is academic since, without a State-sanctioned exchange rate, the Bitcoin does not bestow a value upon the goods or services but instead must derive its value from those goods or services, which must then still be valued in old fashioned dollars. And, finally, when investing in Bitcoins, be prepared to recognize income or gains when you cash in.

There is also a more technological concern, which should speak to every early adopter and everyone who has ever lost data.



What happens when there is a bug in your Bitcoin, when problems with the software cause your digital bank to suspend operations until further notice? What is the value then? Just ask the clients of Mt. Gox, the Tokyo Based Bitcoin exchange that did exactly that in the days before this article was written.

### **Practice Groups:**

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Patrick Westaway is Tax Counsel to Sorbara, Schumacher, McCann LLP, a full service law firm based in Waterloo, Ontario. Patrick advises on a broad range of Canadian taxation issues such as corporate tax planning, structuring inbound investments, corporate reorganizations, cross-border financings, tax opinions for public disclosure documents, tax assessments, personal tax matters, wealth preservation, and on federal and provincial sales tax matters (HST/GST/PST). Patrick also practices corporate and commercial law with an emphasis on the implementation of matters related to his tax planning practice.