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Tax

International coalition investigating cryptocurrency tax evasion, money laundering

By **David Rotfleisch**

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(July 31, 2018, 8:43 AM EDT) -- The Wild West days of cryptocurrency and tax evasion are on the wane. Bitcoin, ethereum, dash and other digital currencies are now firmly in the crosshairs of worldwide tax authorities: the burning issue, of course, is the loss of tax revenue occurring from unreported cryptocurrency transactions.

The latest tax salvo occurred on July 3, 2018, when the Canada Revenue Agency (CRA) along with the Joint Chiefs of Global Tax Enforcement (J5) launched a joint, five-country international initiative aimed at investigating and combating cryptocurrency-related tax evasion and money laundering. If that iconic J5 acronym sounds a bit James Bond, I'm sure it was intended, perhaps inspired by Canada's own JTF 2 elite special forces.

The J5 comprises some pretty big guns: the Internal Revenue Service Criminal Investigation (IRS-CI) in the U.S. and the largest tax authority in the Western world; Her Majesty's Revenue & Customs (HMRC) in the U.K.; the Dutch Fiscal Information and Investigation Service (FIOD); the Australian Criminal Intelligence Commission (ACIC) and Australian Taxation Office (ATO); and, of course, the CRA.

The J5 was formed in response to a request from the Organisation for Economic Co-operation and Development (OECD) that member countries increase measures against the enablers of tax evasion. The group's directive includes sharing information and joint investigations with a view to fight the risk from bitcoin and similar cryptocurrencies on tax administration and collection. Specifically, the initiative intends to uncover unreported income and assets stemming from holdings in cryptocurrencies.

The CRA's director general, Johanne Charbonneau, commented on the requirement for a group with the J5's mandate and alluded to the technological advancements and assistance from professionals that may be aiding tax evaders:

"The formation of the J5 demonstrates the serious commitment of governments around the globe in enhancing international co-operation in fighting serious international tax and financial crimes, money laundering and cybercrime through the use of cryptocurrencies. The J5 complements the important international work of the OECD through operational collaboration. Our collective efforts and experience will be shared to jointly identify and address the increasingly sophisticated and global schemes and the professional enablers that facilitate such schemes."

Similarly, the chief of IRS Criminal Investigations, Don Fort, pointed out the need for transparency among tax authorities and law enforcement when combating tax evaders, who previously benefited from non-co-operation and bureaucratic bumbling among tax departments of different nations:

"We cannot continue to operate in the same ways we have in the past, siloing our information from the rest of the world while organized criminals and tax cheats manipulate the system and exploit vulnerabilities for their personal gain. The J5 aims to break down those walls, build upon individual best practices and become an operational group that is forward-thinking and can pressurize the global criminal community in ways we could not achieve on our own."

I expect that the formation of the group will result in increased focus by worldwide tax departments to gain insights into digital currency transactions.

For example, different tax authorities might simultaneously and strategically demand account information from providers of cryptocurrency wallets. This has precedent since earlier this year, the IRS succeeded in forcing the digital wallet provider, Coinbase, to turn over the account information of more than 14,000 users who dealt in bitcoin.

So, requests for digital wallet providers to release information simultaneously to the tax authorities of Canada, the United States, Australia, the Netherlands and the United Kingdom will be forthcoming.

The formation of the J5 group should serve as a warning to users of ethereum, bitcoin and other cryptocurrencies about the need to educate themselves on the tax compliance requirements in their jurisdiction of residence and of the U.S. if they are American citizens.

Not surprisingly, the formation of the J5 has elicited pushback from users of cryptocurrencies, citing privacy and confidentiality infringement. No surprise there.

The "benefits" of cryptocurrencies as marketed to users include:

- no identification is needed to set up a digital wallet;
- decentralized and not controlled by any central bank;
- completely digital, meaning not encumbered by physical assets that need to be moved physically at some point;
- transactions are irrefutable, meaning they cannot be reversed;

- transactions are very scalable, meaning you can process thousands of transactions at the same time;
- high levels of cryptography provide high levels of cybersecurity; and
- converting cryptocurrency to cash is easy and akin to trading forex.

All these “benefits” combined make cryptocurrencies — hiding among the electrons — the perfect money laundering and tax evasion tool.

Some cryptocurrency users think that cryptocurrency is entirely anonymous and that tax authorities cannot track transactions. This is wrong since the blockchain records every owner of the cryptocurrency.

Other cryptocurrency participants believe, wrongly, that they need not worry about tax liability until they convert their digital coins into fiat (conventional currency). This is false in Canada, since the CRA takes the position that cryptocurrency is similar to a commodity. Any transaction between different cyrptocurrencies gives rise to a tax liability.

There may also be asset reporting requirements for holdings of cryptocurrency in excess of $100,000.

My earlier article about how cryptocurrencies are taxed in Canada in *The Lawyer's Daily* can be read here.

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