

## LIMITED-SCOPE AUDIT PROPOSAL

### Reviewing Issues Related to State Cryptocurrency Tax Policies

#### SOURCE

This audit proposal was requested by Senator Robert Olson.

#### BACKGROUND

Cryptocurrencies (also known as virtual currencies) are a digital form of currency that function as a medium of exchange or to store value. A University of Cambridge study estimated that in 2020 there were 101 million individuals using some form of cryptocurrency worldwide. Although there are several types of cryptocurrencies available, the most commonly used is Bitcoin. Like other forms of currency, cryptocurrencies can be used in exchange for various goods or services or can be used as an investment and held in anticipation of its value increasing. Although an individual may use a cryptocurrency to purchase items, it is not recognized as legal money and is not backed by a central bank or any government.

The increasing use of cryptocurrencies in recent years has required governments to create policies to determine how, and if, cryptocurrency transactions are taxable. For example, the federal government and some state governments have developed policies that do not allow cryptocurrencies to be treated as legal money. Others have policies regarding the use of cryptocurrencies as campaign donations or have policies that require sales tax when a cryptocurrency is used to purchase goods. Because cryptocurrencies have recently become popular, many states have only begun developing these policies.

Legislators have expressed concern about whether Kansas has tax policies regarding cryptocurrencies.

#### AUDIT OBJECTIVES AND TENTATIVE METHODOLOGY

*The audit objective listed below is the question we would answer through our audit work.*

*The steps listed for the objective convey the type of work we would do. These may change as we learn more about the audit issues.*

**Objective 1: How do Kansas's cryptocurrency tax rules compare to federal rules and best practices?** Our tentative methodology would include the following:

- Work with Department of Revenue officials to understand the tax rules (i.e. law, regulations, etc.) that apply to cryptocurrency in Kansas. Also work with them to determine how much tax revenue, if any, Kansas collected from cryptocurrencies in the most recent year.
- Review IRS documents and interview federal officials to understand the federal tax rules that pertain to cryptocurrencies.

- Work with federal and state officials to identify any best practices for how governments should tax cryptocurrencies. In the absence of best practices, talk with knowledgeable government officials, researchers, or others to gather their opinions on good practices regarding the taxation of cryptocurrencies.
- Compare Kansas' tax rules to federal rules and best practices (if possible) to identify areas where Kansas is significantly different.

#### **ESTIMATED RESOURCES**

We estimate this audit would require **100 staff hours** to complete.