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TAKING BACK BITCOIN

*Zachary Segal**

INTRODUCTION

Regardless of age, everyone these days is talking about cryptocurrencies.¹ To some, it is the scam of the century and should be criminalized.² To others, it is the best thing since sliced bread because it allows users to spend with *something* outside government control.³ Cryptocurrencies, like Bitcoin, are slowly attracting more and more government attention, but no concrete national policy has

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¹ Alexavier Guzman, *The Ripple Effect of Cryptocurrencies Forbes*, FORBES (Jan. 11, 2018, 2:40 PM), <https://www.forbes.com/sites/forbesproductgroup/2018/01/11/the-ripple-effect-of-cryptocurrencies/#568574b66080>.

² See Joe Manchin III, *Press Release: Manchin Demands Federal Regulators Ban Bitcoin*, JOE MANCHIN, Feb. 26, 2014, <https://www.manchin.senate.gov/newsroom/press-releases/manchin-demands-federal-regulators-ban-bitcoin>; see also Eric Engle, *Is Bitcoin Rat Poison? Cryptocurrency, Crime, and Counterfeiting (CCC)*, 16 J. HIGH TECH. L. 340, 345 (2016).

The anonymity cryptocurrencies offer enables criminality such as arms sales, drug dealing, human trafficking, murder-for-hire, money laundering, sale of child porn, and sanctions busting. Such a network of anonymity and criminality would also be ideal for state sponsored terrorism. Frankly speaking, the social costs and dangers posed by cryptocurrency far outweigh any potential use of cryptocurrency to fund U.S. or allied intelligence operations secretly as part of the CIA's "black" budget, which is the only potential upside to these facts that one could imagine from a governmental perspective.

Id. (footnotes omitted).

³ Nicolas Wenker, *Online Currencies, Real-World Chaos: The Struggle to Regulate the Rise of Bitcoin*, 19 TEX. REV. L. & POL. 145, 146 (2014) ("Bitcoin's creation and growth may eventually come to be regarded as one of the most fascinating and influential developments of the early twenty-first century."); Vishal Gupta, *#8 Reasons Why Bitcoin is Better than Conventional Currency*, ENTREPRENEUR INDIA (Mar. 29, 2017), <https://www.entrepreneur.com/article/292103>.

been promulgated to regulate them.⁴ While some government agencies, such as the Internal Revenue Service (hereinafter “IRS”),⁵ Federal Election Commission (hereinafter “FEC”),⁶ Securities Exchange Commission (hereinafter “SEC”),⁷ and some federal courts⁸ have addressed it, none have done so in a uniform way.⁹

The looming questions among Bitcoin owners, however, are how will the government define cryptocurrencies and how will the government regulate them.¹⁰ Historically, government regulation and interference with property raise questions as to whether the government act constitutes a taking under the Fifth Amendment’s

⁴ Michael E. McKenney, *As the Use of Virtual Currencies in Taxable Transactions Becomes More Common, Additional Actions Are Needed to Ensure Taxpayer Compliance*, TREASURY INSPECTOR GEN. FOR TAX ADMIN., Sept. 21, 2016, at 7, <https://www.treasury.gov/tigta/auditreports/2016reports/201630083fr.pdf> (“The IRS should prepare a comprehensive virtual currency strategy that will assist taxpayers lawfully engaged with virtual currencies to voluntarily comply with the tax laws while seeking to identify individuals unlawfully engaged in their use.”); *see also* Christopher Burks, *Bitcoin: Breaking Bad or Breaking Barriers?*, 18 N.C. J.L. & TECH. 244 (2017).

For nearly the past decade, Bitcoin has found itself in a state of non-regulation, ambiguous regulation, and conflicting regulation, with several interested agencies vying for effective regulation of an often misunderstood technology. . . . There is no better time than now for federal agencies to align their stances and policies relating to this technology, establish consistent criminal and civil regulation, and allow Bitcoin to reach its fullest potential: as a form of security.

Id. at 244.

⁵ I.R.S. Notice 2014-21, 2014-16 I.R.B. 938 (“This notice describes how existing general tax principles apply to transactions using virtual currency. The notice provides this guidance in the form of answers to frequently asked questions.”).

⁶ Lee E. Goodman, *Bitcoin Contributions and Disbursements*, AO 2014-02, FED. ELECTION COMMISSION, May 8, 2014, <https://www.fec.gov/data/legal/advisory-opinions/2014-02/>; *see also* Byron Tau, *FEC May OK Bitcoin donations*, POLITICO (Nov. 7, 2013, 7:17 PM), www.politico.com/story/2013/11/bitcoin-campaign-donations-draft-rule-99566.html.

⁷ Tony Romm, *Bitcoin Could Face New Regulations in the U.S. After Top Financial Cops and Lawmakers Raise New Fears About Virtual Currency*, RECODE (Feb. 6, 2018), <https://www.recode.net/2018/2/6/16979498/bitcoin-regulation-sec-cftc-congress>.

⁸ *United States v. Faiella*, 39 F. Supp. 3d 544 (S.D.N.Y. 2014); *United States v. 50.44 Bitcoins*, No. CV ELH-15-3692, 2016 WL 3049166, at *1 (D. Md. May 31, 2016); *United States v. Murgio*, No. 15-CR-769 (AJN), 2016 WL 5107128 (S.D.N.Y. Sept. 19, 2016); *United States v. Coinbase, Inc.*, No. 17-CV-01431-JSC, 2017 WL 5890052 (N.D. Cal. Nov. 28, 2017).

⁹ *See* Burks, *supra* note 4.

¹⁰ Jay Adkisson, *Bitcoin, Cryptocurrency and the Government Regulation Paradox*, FORBES (Jan. 29, 2018, 12:47 PM), <https://www.forbes.com/sites/jayadkisson/2018/01/29/bitcoin-cryptocurrency-and-the-government-regulation-paradox/#466b4ee53531>; Joseph Lawler, *Will the Government Start Regulating Bitcoin?*, WASH. EXAMINER (Jan. 16, 2018), <https://www.washingtonexaminer.com/will-the-government-start-regulating-bitcoin>.

Takings Clause.¹¹ Considering the idea of preventing government intrusion into the lives of Americans is enshrined in both constitutional¹² and natural law,¹³ this article will undertake a Takings Clause analysis evaluating whether government, in particular the IRS, regulation of cryptocurrencies constitutes a taking.

The Takings Clause is embedded in the Fifth Amendment to the Constitution: “[N]or shall private property be taken for public use, without just compensation.”¹⁴ It is generally accepted that conducting an analysis under the Takings Clause requires a court to answer four questions: (1) is there a taking?; (2) is it property?; (3) is the taking for public use?; and (4) is just compensation paid?¹⁵ The third question does not require much analysis because the Supreme Court has been consistent in deferring to the government’s decision as to what public use is.¹⁶ The first, second, and fourth prongs, however, are not as simple.

On the property prong, the IRS classified cryptocurrencies as property for income tax purposes.¹⁷ Similarly, in criminal forfeiture proceedings, courts have auctioned off confiscated Bitcoin instead of converting them as it would if the proceeds of the forfeiture were foreign cash.¹⁸ Finally, numerous experts in the field of trusts and

¹¹ See *Horne v. Dep’t. of Agric.*, 135 S. Ct. 2419, 2426-29 (2015) (recounting the history of the Takings Clause in order to justify its later holding that the Takings Clause applies to both personal and real property); Bill Funk, *CPR Perspective: The Takings Clause of the Fifth Amendment*, CTR. FOR PROGRESSIVE REFORM, <http://www.progressivereform.org/perspectives/takings.cfm> (last visited Oct. 23, 2018).

¹² U.S. CONST. amend. V.

¹³ *Horne*, 135 S. Ct. at 2426.

The principle reflected in the Clause goes back at least 800 years to Magna Carta, which specifically protected agricultural crops from uncompensated takings. Clause 28 of that charter forbade any “constable or other bailiff” from taking “corn or other provisions from any one without immediately tendering money therefor, unless he can have postponement thereof by permission of the seller.”

Id. (citations omitted).

¹⁴ U.S. CONST. amend. V.

¹⁵ ERWIN CHEMERINSKY, *CONSTITUTIONAL LAW* 670-671 (5th ed. 2017).

¹⁶ *Berman v. Parker*, 348 U.S. 26, 32 (1954).

¹⁷ I.R.S. Notice 2014-21, 2014-16 I.R.B. 938.

¹⁸ See Daniel Oberhaus, *Why Doesn’t the US Government HODL Seized Bitcoins?*, MOTHERBOARD (Jan. 18, 2018), https://motherboard.vice.com/en_us/article/wjpkx/doj-bitcoin-seizure-marshals-auction; see also Joon H. Kim, *Acting Manhattan U.S. Attorney Announces Forfeiture of \$48 Million From Sale of Silk Road Bitcoins*, U.S. DEP’T JUST., Sept. 29, 2017, <https://www.justice.gov/usao-sdny/pr/acting-manhattan-us-attorney-announces->

estates concluded Bitcoin could constitute the res of a trust so long as the encryption key is available to the beneficiary.¹⁹

A regulation constitutes a taking when the government action has gone “too far.”²⁰ The final determination regarding whether a regulatory taking has occurred is evaluated pursuant to the three part *ad hoc* approach delineated by *Penn Central Transportation Company v. New York City*²¹: (1) the economic impact of regulation on the claimant; (2) the extent to which the government regulation interferes with investment back expectation; and (3) the character of government action.²²

In this article, the author will argue Bitcoin is property for Takings Clause purposes because the federal government has classified it and treated it as such. However, this article focuses on the IRS classification because Bitcoin involves interstate commerce and thus should be regulated by the federal government instead of the individual states. The IRS classification serves as the regulation, which gives rise to a regulatory taking. Specifically, under the *Penn Central* test, the regulation constitutes a taking because (1) the economic impact on the claimant is both the volatility of Bitcoin and potential fines resulting from non-compliance; (2) the extent to which the government classification interferes with the investment backed expectation is significant in that it frustrates holders of Bitcoin from using it as a currency by requiring that each transaction be recorded for capital gains purposes; and (3) the character of the government action is unduly burdensome because it is arbitrary and capricious in that the

forfeiture-48-million-sale-silk-road-bitcoins; *For Sale Approximately 3,813.0481935 Bitcoins*, U.S. MARSHALS SERV., <https://www.usmarshals.gov/assets/2018/bitcoinauction/> (last visited Oct. 23, 2018).

¹⁹ See generally Jeff Vandrew, Jr., *5 Things Bitcoin Owners Must Do When Estate Planning*, COINDESK (Jul. 28, 2015), <https://www.coindesk.com/5-things-bitcoin-owners-must-do-when-estate-planning/>; Jeff John Roberts, *What Happens to Cryptocurrency When You Die?*, FORTUNE (Sept. 26, 2017), <http://fortune.com/2017/09/26/cryptocurrency-bitcoin-death/>; Nate Lanxon, *Bitcoin Industry Grapples With Age-Old Problem of Inheritance*, BLOOMBERG (Feb. 13, 2018), <https://www.bloomberg.com/news/articles/2018-02-13/bitcoin-industry-grapples-with-age-old-problem-of-inheritance>.

²⁰ *Pennsylvania Coal Co. v. Mahon*, 260 U.S. 393, 415 (1922) (“The general rule at least is that while property may be regulated to a certain extent, if regulation goes *too far* it will be recognized as a taking.” (emphasis added)). A regulatory taking is distinguishable from a possessory taking, which are per se unconstitutional because it, generally, involves physical appropriations of real property. *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419, 426 (1982).

²¹ 438 U.S. 104 (1978).

²² *Id.* at 124.

federal government, by way of the IRS, disproportionately treats Bitcoin compared to other non-state issued currencies. Proof of the disproportionate treatment is the IRS's treatment of international currencies not formally recognized by the United States, such as Taiwan, insofar that, as will be further explained below, persons using Taiwanese dollars in the United States are not subject to the same reporting obligations as those using Bitcoin.

Although the Court has previously held taxes are not reviewable under the Takings Clause,²³ scholars suggest, and cases confirm, challenging a classification is reviewable.²⁴ Therefore, owners of Bitcoin likely could challenge the IRS classification under the Takings Clause seeking just compensation or injunctive relief in the form of a currency classification.

Part I will briefly explain what cryptocurrencies are by looking at how they work, and what they are used for. Part II is divided into two parts: it commences by examining the framework for defining property followed by explaining why Bitcoin is property for Takings Clause purposes. Similarly, Part III starts by discussing the jurisprudence that lays out the tests for determining whether a taking occurred. This Part concludes by applying *Penn Central's ad-hoc* approach to Bitcoin. Part IV explores why *Horne* permits a request for equitable relief, instead of just compensation in monetary form. Specifically, a Bitcoin holder could contest the IRS classification of Bitcoin as property if the IRS brings an action against him or her for failing to report a capital gain resulting from a transaction where Bitcoin was used as the mode of purchase. Part V concludes by summarizing the findings and suggesting the appropriate form of relief is not just compensation, but rather classifying Bitcoin as currency instead of property.

²³ *Koontz v. St. John's River Water Mgmt. Dist.*, 570 U.S. 595, 615 (2013) ("It is beyond dispute that '[t]axes and user fees . . . are not "takings."'" (citations omitted)); *see also* *City of Mobile v. Kimball*, 102 U.S. 691 (1881); *United States v. Sperry Corp.*, 493 U.S. 52, 62 n.9 (1989); *A. Magnano Co. v. Hamilton*, 292 U.S. 40, 44 (1934); *Dane v. Jackson*, 256 U.S. 589, 599 (1921); *Henderson Bridge Co. v. City of Henderson*, 173 U.S. 592, 614-15 (1899).

²⁴ *See* Thomas W. Merrill, *Anticipatory Remedies for Takings*, 128 HARV. L. REV. 1630, 1650 (2015) ("I would also include within the category of anticipatory remedies petitions for review of agency action, either under the agency's organic act or under the APA, in which a party claims the agency's action violates the Takings Clause."); *see also* *Wensmann Realty, Inc. v. City of Eagan*, 734 N.W.2d 623 (Minn. 2007) (explaining the City's refusal to re-classify land challenged as taking).

I. WHAT IS BITCOIN?

Bitcoin is a virtual currency that was developed by Satoshi Nakamoto through the infamous White Paper.²⁵ According to the White Paper, Bitcoin is a purely peer-to-peer version of electronic cash that would allow online payments to be sent directly from one party to another without going through a financial institution.²⁶ In the same way the United States Dollar is the official currency for the United States, Bitcoin was intended to serve as the official currency on the Internet.²⁷ Instead of going through financial institutions, however, Nakamoto envisioned a system whereby individuals take control insofar that they can perform peer-to-peer transactions monitored by other individuals.²⁸

These “other individuals,” frequently referred to as “miners,” verify the transactions that are entered into blocks on a public ledger, known as the block chain, which keeps track of all Bitcoin transactions.²⁹ Unlike banks, for example, miners are ordinary people with an Internet connection who dedicate their computers to the Bitcoin network and attempt to unravel a “puzzle” through trial and error.³⁰ Once a block is uncovered, the miner’s work is “audited” by other miners to ensure its reliability.³¹ If the majority of miners accept the discovery, the miner receives a number of Bitcoins, the transaction is approved, and a new block is added to the block chain.³² By placing the validity of transactions into the hands of ordinary people, instead of centralized institutions, Bitcoin is almost like a credit union for the Internet that is owned and controlled by those with a stake in it.

²⁵ Satoshi Nakamoto, *Bitcoin: A Peer-to-Peer Electronic Cash System*, BITCOIN, <https://bitcoin.org/bitcoin.pdf> (last visited Oct. 23, 2018).

²⁶ *Id.*

²⁷ *Id.*

²⁸ *Id.*

²⁹ *Id.*

³⁰ Noelle Acheson, *How Bitcoin Mining Works Coin Desk*, COINDESK, <https://www.coindesk.com/information/how-bitcoin-mining-works/> (last updated Jan. 29, 2018).

³¹ *The Rise of Bitcoin: Understanding the Ins and Outs of this Cryptocurrency*, NAT'L CREDIT UNION ADMIN., <https://www.ncua.gov/newsroom/Pages/ncua-report/2017/fourth-quarter/rise-bitcoin-understanding-cryptocurrency.aspx> (last modified Sept. 20, 2018).

³² *Id.*

II. BITCOIN FALLS WITHIN THE TAKINGS CLAUSE DEFINITION OF PROPERTY

Prior to 2015, the Takings Clause was generally applied to takings of real property; but that changed with the Court's decision in *Horne v. Department of Agriculture*.³³ In *Horne*, the Court held personal property is also subject to a taking: "The Government has a categorical duty to pay just compensation when it takes your car, just as when it takes your home."³⁴

Although the Court has not prescribed a specific test to evaluate whether something is property for Takings Clause purposes, the Takings Clause jurisprudence provides enough guidance to make this determination.³⁵ In *Lucas v. South Carolina Coastal Council*,³⁶ the Court explained property hinges on the state's definition of property or the reasonable expectations of the property owner.³⁷ *Drye v. United States*,³⁸ moreover, confirms that looking at the state's definition is

³³ 135 S. Ct. 2419 (2015).

³⁴ *Id.* at 2426. *Horne* was a case in which a family in California—the Hornes—invoked the Takings Clause as a defense in an enforcement action to collect unpaid fees pursuant to an act that required raisin handlers to set aside a portion of their crop during years of excess production for the government to divert those raisins from the open market to non-competitive markets in order to stabilize the raising crop market. *See generally id.*

³⁵ *See* LAWRENCE H. TRIBE, AMERICAN CONSTITUTIONAL LAW § 9-7, at 609 (2d ed. 1988) ("The Court's conception of property in its takings analysis, however, has often rested too heavily on whether a given stick in a bundle of property rights resembles the Justices' collective hunch as to what 'traditional' property is all about." (footnote omitted)); *see also* D. Benjamin Barros, *Defining "Property" in the Just Compensation Clause*, 63 FORDHAM L. REV. 1853, 1853-54 (1995) ("'Property,' however, has remained largely undefined. This lack of definition poses a serious problem, because defining the terms of the Just Compensation Clause is critical to devising a coherent test for regulatory takings." (citation omitted)).

³⁶ 505 U.S. 1003 (1992).

³⁷ *Id.* at 1078 n.7.

The answer to this difficult question may lie in how the owner's reasonable expectations have been shaped by the State's law of property—*i.e.*, whether and to what degree the State's law has accorded legal recognition and protection to the particular interest in land with respect to which the takings claimant alleges a diminution in (or elimination of) value. In any event, we avoid this difficulty in the present case, since the "interest in land" that Lucas has pleaded (a fee simple interest) is an estate with a rich tradition of protection at common law, and since the South Carolina Court of Common Pleas found that the Beachfront Management Act left each of Lucas's beachfront lots without economic value.

Id.

³⁸ 528 U.S. 49 (1999); *see also* *Carpenter v. United States*, 138 S. Ct. 2206, 2270 (2018) (Gorsuch, J., dissenting) ("In the context of the Takings Clause we often ask whether those

appropriate in determining whether something is property.³⁹ *Ruckelshaus v. Monsanto Co.*,⁴⁰ although decided before *Lucas*, suggests something that is either assignable or can constitute the res of a trust falls within the definition of property.⁴¹

Therefore, the existing jurisprudence permits finding that an item can be considered property for purposes of a regulatory taking based on: (1) state’s law of property;⁴² (2) reasonable expectations of property owners,⁴³ and (3) whether it can constitute the res of a trust.⁴⁴ The following section will explain why the government’s treatment and classification of Bitcoin—along with its ability to constitute the res of a trust— enables the conclusion that Bitcoin is property.

state-created rights are sufficient to make something someone’s property for constitutional purposes.”).

³⁹ *Drye*, 528 U.S. at 57.

⁴⁰ 467 U.S. 986 (1984).

⁴¹ *Id.* at 1002 (“Trade secrets have many of the characteristics of more tangible forms of property. . . . A trade secret can form the res of a trust.” (citations omitted)); *see also* Mark S. Levy, *Holding the FBI Accountable For Hacking Apple’s Software Under the Takings Clause*, 66 AM. U. L. REV. 1293, 1312 (2017).

Moreover, the Supreme Court has recognized other forms of intangible property as “property” for Takings Clause purposes. In *Ruckelshaus v. Monsanto Co.*, for example, the Court established that trade secrets constitute property, comparing trade secrets to “more tangible forms of property” because a “trade secret is assignable” and “can form the res of a trust.”

Id.

⁴² Steven C. Begakis, *Stop the Reach: Solving the Judicial Takings Problem by Objectively Defining Property*, 91 NOTRE DAME L. REV. 1197, 1213 (2016) (quoting *Drye v. United States*, 528 U.S. 49 (1999)) (“We look initially to state law to determine what rights the taxpayer has in the property the Government seeks to reach, then to federal law to determine whether the taxpayer’s state-delineated rights qualify as ‘property’ or ‘rights to property’ within the compass of the federal tax lien legislation.” (citation omitted)).

⁴³ Barros, *supra* note 35, at 1866.

Thus, between the opinion of the Court and Justice Kennedy’s concurring opinion, there are three possible definitions of property, as the term relates to regulatory takings: (1) Property is defined by the background principles of the state’s property and nuisance law; (2) Property is defined as the property owner’s reasonable expectations as shaped by the state’s law of property; and (3) Property is defined as the property owner’s reasonable expectations, no matter what their source.

Id.

⁴⁴ *See supra* note 41.

A. How the Federal Government Has Classified Bitcoin

In 2014, the IRS classified Bitcoin and other cryptocurrencies as property for income tax purposes.⁴⁵ Similarly, the SEC regulates Bitcoin and other cryptocurrencies in the same way it regulates other securities.⁴⁶ Finally, the FEC concluded, in an advisory opinion, that Bitcoin is “money or anything of value.”⁴⁷ Thus, the federal government classifications would appear to suggest Bitcoin could be considered property.

B. How the Federal Government Has Treated Bitcoin

The federal government has treated Bitcoin and other cryptocurrencies as property by auctioning it following a criminal or civil forfeiture.⁴⁸ In criminal forfeiture, the government seizes assets obtained as part of the criminal scheme.⁴⁹ When the proceeds of the forfeiture are currency, the government deposits it into the asset forfeiture fund.⁵⁰ If, however, the currency is foreign, the government converts it into U.S. dollars before depositing it into the fund.⁵¹ By contrast, forfeited real or personal property is auctioned off with the proceeds following the same route as cash.⁵²

⁴⁵ See *supra* note 17.

⁴⁶ See *supra* note 7.

⁴⁷ See *supra* note 6; see also Nick Corasaniti, *Election Commission Votes to Allow Bitcoin Donations*, N.Y. TIMES (May 8, 2014), <https://www.nytimes.com/2014/05/09/us/politics/election-commission-votes-to-allow-bitcoin-donations.html>.

⁴⁸ See Oberhaus, *supra* note 18; see also Kim, *supra* note 18; Aaron Mak, *Prosecutors Are Planning to Sell Millions of Dollars Worth of Seized Bitcoin*, FUTURE TENSE (Dec. 15, 2017), http://www.slate.com/blogs/future_tense/2017/12/15/bitcoin_seized_by_the_u_s_government_during_an_arrest_can_be_sold_a_judge.html; *For Sale*, *supra* note 18.

⁴⁹ Dick Thornburgh, *9-118.000 - AG Guidelines On Seized And Forfeited Property*, U.S. DEP'T JUST., July 31, 1990, <https://www.justice.gov/usam/usam-9-118000-ag-guidelines-seized-and-forfeited-property>.

The Attorney General has the authority to retain any civilly or criminally forfeited property for official use by any federal agency. No seized property shall be placed into official use until a final determination of forfeiture has been made and the request to place the property into official use has been approved by the appropriate official.

Id. at 9-118.400.

⁵⁰ Oberhaus, *supra* note 18.

⁵¹ Oberhaus, *supra* note 18.

⁵² Oberhaus, *supra* note 18.

Bitcoin, ironically, although referred to as a virtual currency, is being auctioned in the same manner, for example, as gold or a house.⁵³ In fact, in January 2018, the United States Marshals Service invited interested buyers to submit a \$200,000 minimum bid to purchase 3,813.0481935 Bitcoins.⁵⁴ Similarly, in September 2017, the United States District Court for the Southern District of New York successfully auctioned 144,336 Bitcoins for a whopping \$48,238,116.⁵⁵ The Bitcoins being auctioned off by the federal government were forfeited pursuant to criminal, civil, and administrative cases.⁵⁶ The federal courts treat Bitcoin in the same way as the Department of Justice.

In *United States v. 50.44 Bitcoins*,⁵⁷ the District Court for the Western District of Maryland held Bitcoin was property for the purposes of a forfeiture following a criminal conviction.⁵⁸ The Bitcoins were seized pursuant to a search warrant when one of the defendants showed officers her personal computer, where the Bitcoins were stored, followed by transferring them to the officers.⁵⁹ The court held, “Because the United States has established a substantial connection between the *property* to be forfeited and a criminal offense, 50.44 Bitcoins are subject to forfeiture”⁶⁰

C. Res of a Trust

In *Monsanto*, the Court noted a trade secret could constitute property because it can form the res of a trust.⁶¹ The question facing the Court in *Monsanto* was whether a trade secret was property for purposes of the Taking Clause.⁶² The Court explained that “[t]rade secrets have many of the characteristics of more tangible forms of property. A trade secret is assignable. A trade secret can form the res of a trust.”⁶³ Bitcoin, like a trade secret, is not tangible property in the

⁵³ Oberhaus, *supra* note 18.

⁵⁴ *For Sale*, *supra* note 18.

⁵⁵ Kim, *supra* note 18.

⁵⁶ *See supra* note 18.

⁵⁷ No. ELH-15-3692, 2016 WL 3049166, at *1 (D. Md. 2016).

⁵⁸ *Id.* at *2.

⁵⁹ *Id.*

⁶⁰ *Id.* (emphasis added).

⁶¹ *Ruckleshaus v. Monsanto Co.*, 467 U.S. 986, 1002 (1984).

⁶² *Id.* at 1003.

⁶³ *Id.* at 1002 (citations omitted).

traditional sense, but rather exists by virtue of the laws willingness to recognize an exclusive ownership interest in it.

Trusts and estates attorneys have remarked that Bitcoin can in fact be left in a trust.⁶⁴ However, the testator must give either the executor, or someone else, the private key required to access the Bitcoin wallet.⁶⁵ Without the private key, the Bitcoin cannot be accessed.⁶⁶ Therefore, in order for Bitcoin to constitute the res of a trust, an owner must simply ensure that a beneficiary can access the Bitcoin via the key.

Bitcoin meets the criteria to be considered property under the Takings Clause because its character and government treatment are concomitant with the Court's definition for this purpose.⁶⁷ The expectation created by the State, in this context, is the treatment by the federal government because, as mentioned above, Bitcoin involves interstate commerce insofar that the expectations created by the federal government carry more weight than any State classification. However, there is an irony in Bitcoin being classified and treated as property: the classification is the regulation that gives rise to a Takings Clause claim.

III. CLASSIFYING BITCOIN AS PROPERTY CREATES THE REGULATORY TAKING

The Court has outlined two different types of takings: possessory and regulatory takings.⁶⁸ A possessory taking occurs when the government physically occupies or confiscates property for public use.⁶⁹ This implicates a *per se* rule requiring the government to pay

⁶⁴ See generally Vandrew Jr., *supra* note 19; Roberts, *supra* note 19; Lanxon, *supra* note 19.

⁶⁵ See generally Vandrew Jr., *supra* note 19; Roberts, *supra* note 19; Lanxon, *supra* note 19.

⁶⁶ See generally Vandrew Jr., *supra* note 19; Roberts, *supra* note 19; Lanxon, *supra* note 19.

⁶⁷ Justice Gorsuch explained in his dissenting opinion in *Carpenter v. United States* that the state created rights can serve as the basis for a property right. 138 S. Ct. 2206, 2270 (2018) (Gorsuch, J., dissenting) (“In the context of the Takings Clause we often ask whether those state-created rights are sufficient to make something someone’s property for constitutional purposes.”). Given that Bitcoin is an online currency, however, this article argues State classifications are irrelevant and thus the expectation of a property right should reflect expectations created by federal authorities.

⁶⁸ See *supra* note 20.

⁶⁹ *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419, 426 (1982) (“A ‘taking’ may more readily be found when the interference with property can be characterized as a physical invasion by government, than when interference arises from some public program

just compensation.⁷⁰ Conversely, a regulatory taking occurs when a government regulation goes “too far” insofar that, while the government does not appropriate the property in its entirety, the property owner’s use is frustrated.⁷¹ Unless the regulation leaves no economically viable use of the property, regulatory takings are evaluated using the three-part test prescribed by the Court in *Penn Central*.⁷²

The following sections will first explain why the IRS classification is a regulation, then elaborate on the two types of takings and the tests used to determine whether one has occurred. The section will conclude by explaining why classifying Bitcoin as property constitutes a regulatory taking.

A. Classifying Bitcoin as Property is a Regulation

The IRS’s classification of Bitcoin as property is the regulation that enables a Takings Clause analysis in that the regulation itself both permits the inference that Bitcoin is property and serves as the justification for taking Bitcoin upon failing to comply with it. According to the Administrative Procedure Act (hereinafter “APA”), federal agencies can issue two types of rules⁷³: legislative and interpretive.⁷⁴ Unlike interpretive rules, legislative rules must undergo a three-step process.⁷⁵ Before a federal agency issues a legislative rule,

adjusting the benefits and burdens of economic life to promote the common good.”); *see also* *Horne v. Dep’t. of Agric.*, 135 S. Ct. 2419, 2443 n.3 (2015) (“In other words, only when a law requires forfeiture of *all* rights in property does it effect a *per se* taking regardless of whether the law could be avoided by a different use of the property.” (emphasis in original)).

⁷⁰ *Loretto*, 458 U.S. at 426.

⁷¹ *See supra* note 20.

⁷² *Lucas v. S.C. Coastal Council*, 505 U.S. 1003, 1015 (1992) (“The second situation in which we have found categorical treatment appropriate is where regulation denies all economically beneficial or productive use of land.”).

⁷³ *Perez v. Mortg. Bankers Ass’n*, 135 S. Ct. 1199, 1203 (2015) (“‘Rule,’ in turn, is defined broadly to include ‘statement[s] of general or particular applicability and future effect’ that are designed to ‘implement, interpret, or prescribe law or policy.’” (citing 5 U.S.C. § 551)).

⁷⁴ *Id.*

⁷⁵ *Id.*

Section 4 of the APA, 5 U.S.C. § 553, prescribes a three-step procedure for so-called “notice-and-comment rulemaking.” First, the agency must issue a “[g]eneral notice of proposed rule making,” ordinarily by publication in the Federal Register. § 553(b). Second, if “notice [is] required,” the agency must “give interested persons an opportunity to participate in the rule making through submission of written data, views, or arguments.” § 553(c). An agency must consider and respond to

it must go through what is known as the notice-and-comment rulemaking procedures.⁷⁶ Rules that follow the notice-and-comment procedure are considered legislative rules because they can be enforced through law.⁷⁷

An interpretive rule, which does not require modification through the notice-and-comment procedure, is “issued by an agency to advise the public of the agency’s construction of the statutes and rules which it administers.”⁷⁸ As such, while interpretive rules are easier to issue, it does not “have the force and effect of law and are not accorded that weight in the adjudicatory process.”⁷⁹ It follows that federal agencies can contradict a previously issued interpretive rule without notifying the public.⁸⁰

In March 2017, the IRS issued Notice 2014-21 (hereinafter “Notice”).⁸¹ According to the Notice, “virtual currency is treated as property for U.S. federal tax purposes. General tax principles [that apply] to property transactions apply to transactions using virtual currency.”⁸² A Bitcoin user who inaccurately reports a payment using Bitcoin is subject to penalty in the same way an individual taxpayer would be penalized for failing to report a capital gain made from

significant comments received during the period for public comment. *See Citizens to Preserve Overton Park, Inc. v. Volpe*, 401 U.S. 402, 416, 91 S. Ct. 814, 28 L. Ed. 2d 136 (1971); *Thompson v. Clark*, 741 F.2d 401, 408 (C.A.D.C. 1984). Third, when the agency promulgates the final rule, it must include in the rule’s text “a concise general statement of [its] basis and purpose.” § 553(c). Rules issued through the notice-and-comment process are often referred to as “legislative rules” because they have the “force and effect of law.” *Chrysler Corp. v. Brown*, 441 U.S. 281, 302-303, 99 S. Ct. 1705, 60 L. Ed. 2d 208 (1979) (internal quotation marks omitted).

Id.

⁷⁶ *Id.*

⁷⁷ *Id.* at 1204 (citing *Chrysler Corp. v. Brown*, 441 U.S. 281, 302-03 (1979)) (“Rules issued through notice-and-comment process are often referred to as legislative rules because they have the force and effect of law.”) (internal ellipsis omitted); *see also Supreme Court Makes It Easier for Administrative Agencies to Change “Interpretive Rules”*, SPENCER FANE LLP (Mar. 17, 2015), <https://www.spencerfane.com/publication/supreme-court-makes-it-easier-for-administrative-agencies-to-change-interpretive-rules/> (“This development is concerning because it is now easier for administrative agencies to change longstanding interpretations of ambiguous labor and employment regulations without giving warning to, or getting input from, private employers.”).

⁷⁸ *Shalala v. Guernsey Mem’l Hosp.*, 514 U.S. 87, 99 (1995).

⁷⁹ *Id.*

⁸⁰ *See supra* note 77.

⁸¹ I.R.S. Notice 2014-21, 2014-16 I.R.B. 938.

⁸² *Id.*

stock.⁸³ Accuracy related penalties, for example, are twenty percent of the portion of the underpayment attributable to the taxpayer's negligence or disregard of rules or regulation.⁸⁴

The Notice, however, despite having a comment section, did not follow the typical notice-and-comment procedure required for legislative rules.⁸⁵ The IRS's failure in doing so has resulted in criticism by the Treasury Inspector General for Tax Administration in a 2016 report.⁸⁶ According to that report, although the IRS has been clearer in interpreting other provisions of the Notice, it is focusing its enforcement on tax compliance without any guidance to taxpayers.⁸⁷ As a result, taxpayers using Bitcoin to "buy a cup of coffee each day for one week" lack the guidance to properly record the transaction, which makes them susceptible to violation.⁸⁸ In fact, the Inspector General's prediction is not far off from what is occurring.

⁸³ *Id.*

⁸⁴ 26 U.S.C. § 6662(a), (b)(1) (2018).

(a) Imposition of penalty.—If this section applies to any portion of an underpayment of tax required to be shown on a return, there shall be added to the tax an amount equal to 20 percent of the portion of the underpayment to which this section applies.

(b) Portion of underpayment to which section applies.—This section shall apply to the portion of any underpayment which is attributable to 1 or more of the following:

(1) Negligence or disregard of rules or regulations. . . .

Id.

⁸⁵ As of this writing, Notice 2014-21 is the only action taken by the IRS. Nothing has been published expanding on the Notice in the Federal Register.

⁸⁶ McKenney, *supra* note 4.

⁸⁷ *Id.* at 7-8, 12.

⁸⁸ *Id.* at 9.

Based on this general guidance, when a portion of a bitcoin is used to make a purchase, taxpayers will have to treat the transaction as property and determine their tax basis for the bitcoin on the day of the purchase. For example, if a taxpayer uses a portion of a bitcoin to buy a cup of coffee each day for one week, he or she will have to determine what portion of the bitcoin was used to make the purchase based on the daily exchange rate, convert it into U.S. dollars, and keep a record of each transaction so that the gain or loss from his or her virtual currency property can be properly reported. Notice 2014-21 does not provide taxpayers with guidance on what records should be kept and how the records should be maintained.

Id.

In November 2017, a United States district court granted an IRS motion to enforce a summons⁸⁹ requiring Coinbase, Inc.⁹⁰ to disclose its customer information to the IRS.⁹¹ The IRS argued the purpose was to investigate whether Coinbase customers were complying with the Notice requirements for reporting transactions made with virtual currency.⁹² Moreover, in March 2018, the IRS

⁸⁹ As a corollary to the general issues discussed herein, the statutes governing summons enable the government to delve into the records of those ordered to comply with the summons. In other words, questions arise vis-à-vis the government's ability to investigate a Bitcoin holder's financial records based on an error, deemed by the TIGTA Report, as inevitable. See 26 U.S.C. § 7402(b) (2018), which provides:

(b) To enforce summons.—If any person is summoned under the internal revenue laws to appear, to testify, or to produce books, papers, or other data, the district court of the United States for the district in which such person resides or may be found shall have jurisdiction by appropriate process to compel such attendance, testimony, or production of books, papers, or other data.

See also 26 U.S.C. § 7602(a) (2018), which provides:

(a) Authority to summon, etc.—For the purpose of ascertaining the correctness of any return, making a return where none has been made, determining the liability of any person for any internal revenue tax or the liability at law or in equity of any transferee or fiduciary of any person in respect of any internal revenue tax, or collecting any such liability, the Secretary is authorized—

- (1) To examine any books, papers, records, or other data which may be relevant or material to such inquiry;
- (2) To summon the person liable for tax or required to perform the act, or any officer or employee of such person, or any person having possession, custody, or care of books of account containing entries relating to the business of the person liable for tax or required to perform the act, or any other person the Secretary may deem proper, to appear before the Secretary at a time and place named in the summons and to produce such books, papers, records, or other data, and to give such testimony, under oath, as may be relevant or material to such inquiry; and
- (3) To take such testimony of the person concerned, under oath, as may be relevant or material to such inquiry.

⁹⁰ See *About Coinbase*, COINBASE, <https://www.coinbase.com/about> (last visited Oct. 23, 2018) (“Founded in June of 2012, Coinbase is a digital currency wallet and platform where merchants and consumers can transact with new digital currencies like bitcoin, ethereum, and litecoin. We’re based in San Francisco, California. Bitcoin is the world’s most widely used alternative currency with a total market cap of over \$100 billion. The bitcoin network is made up of thousands of computers run by individuals all over the world.”).

⁹¹ *United States v. Coinbase, Inc.*, No. 17-CV-01431-JSC, 2017 WL 5890052 (N.D. Cal. Nov. 28, 2017).

⁹² *Id.* at *1.

[T]he IRS “is conducting an investigation to determine the identity and correct federal income tax liability of United States persons who

issued IR-2018-71.⁹³ IR-2018-71 is a reminder to taxpayers that failure to comply with the Notice requirements for reporting transactions made with Bitcoin can result in audits, penalties, and even criminal prosecutions for tax evasion and filing false tax returns.⁹⁴ The criminal prosecutions carry prison terms between three to five years and fines up to \$250,000.⁹⁵

The IRS's failure to follow the required procedure for legislative rules creates the presumption that it is an interpretive rule.⁹⁶ However, both the Notice and IR-2018-71 are enforceable by law, which permits the inference that the former has the "force and effect of law" required to be a legislative rule.⁹⁷ As will be further discussed in Part IV, the Takings Clause was used as a defense in *Horne* when the government sought collection of unpaid fees resulting from a violation of a statute.⁹⁸ Therefore, if the IRS can bring suit against Bitcoin holders for failing to comply with the Notice, the Notice constitutes a regulation insofar that a defendant can raise a Takings Clause defense. Considering this regulation does not deprive Bitcoin owners of all economically viable use of it, the subsequent subsections will explain why the *Penn Central* three-part test applies.

conducted transactions in a convertible virtual currency . . . for the years ended December 31, 2013, 2014, and 2015." . . . The IRS believes that virtual currency gains are underreported. . . . Based upon an IRS search, only 800 to 900 persons electronically filed a Form 8949 that included a property description that is "likely related to bitcoin" in each of the years 2013 through 2015.

Id. (alteration in original) (citations omitted).

⁹³ I.R.S. News Release IR-2018-71 (Mar. 23, 2018).

⁹⁴ *Id.*

⁹⁵ *Id.*

⁹⁶ See *supra* note 78; Professor Merrill, later on in the article justifies his proposition that the Takings Clause can be used as a defense by citing to *Horne*: "*Horne v. Department of Agriculture*, in which the Court held that a takings claim could be raised defensively in a judicial review proceeding in a court of general jurisdiction without the claimant's first seeking compensation from the CFC." Merrill, *supra* note 24, at 1636.

⁹⁷ *Perez v. Mortgage Bankers Ass'n.*, 135 S. Ct. 1199, 1203 (2015) (citing *Chrysler Corp. v. Brown*, 441 U.S. 281, 302-03 (1979)).

⁹⁸ See *supra* note 24.

B. Regulatory Takings

Initially, *Pennsylvania Coal Co. v. Mahon*,⁹⁹ held that a taking occurs when a government regulation goes too far.¹⁰⁰ Thus, when a regulation rendered the interest of the property owner “commercially impracticable,” a taking occurred.¹⁰¹ Subsequently, however, in *Penn Central*, the Court prescribed a three-part test to determine whether a regulatory taking has occurred: (1) the economic impact of regulation on the claimant; (2) the extent to which the government regulation interferes with the claimant’s investment back expectation; and (3) the character of the government action.¹⁰²

In *Penn Central*, the plaintiff applied to New York City asking to add a fifty-story extension to Grand Central Station.¹⁰³ The city denied the permit citing the Landmarks Law, which protected structures that were historically important and retained their ability to be used as a landmark.¹⁰⁴ The plaintiff argued the law constituted a taking because it was deprived of using the air rights on top of the building.¹⁰⁵ The Court rejected this argument holding the plaintiffs had not been deprived of using its property as initially intended.¹⁰⁶ In other words, the plaintiff intended to use the terminal as a train station with concession stands, and the Landmark Law had not deprived them of using it for that purpose.¹⁰⁷ Therefore, because the plaintiffs were still able to obtain a return on their investment (i.e., from using the property as a train station that is also rented out for commercial use), the

⁹⁹ 260 U.S. 393 (1922).

¹⁰⁰ *Id.* at 415 (“The general rule at least is that while property may be regulated to a certain extent, if the regulation goes *too far* it will be recognized as a taking.” (emphasis added)).

¹⁰¹ *Id.* at 414 (“To make it commercially impracticable to mine certain coal has very nearly the same effect for constitutional purposes as appropriating or destroying it.”).

¹⁰² *Penn Cent. Transp. Co. v. City of N.Y.*, 438 U.S. 104, 124 (1978).

¹⁰³ *Id.* at 136-37.

¹⁰⁴ *Id.* at 115-16.

¹⁰⁵ *Id.* at 130.

¹⁰⁶ *Id.* at 136.

Its designation as a landmark not only permits but contemplates that appellants may continue to use the property precisely as it has been used for the past 65 years: as a railroad terminal containing office space and concessions. So the law does not interfere with what must be regarded as Penn Central’s primary expectation concerning the use of the parcel.

Penn Cent. Transp. Co. v. City of N.Y., 438 U.S. 104, 136 (1978).

¹⁰⁷ *Id.* at 136.

economic impact was deemed insufficient for Takings Clause purposes.¹⁰⁸

Courts continue to use the *Penn Central* three-part test to evaluate regulatory takings claims, unless the taking deprives the owner of economically viable use of the property.¹⁰⁹ Subsequent cases, however, suggest the first two prongs are reviewed together¹¹⁰ while the third—the character prong—is balanced against the first two.¹¹¹

1. The Economic Impact of the Regulation Interferes With Investment Backed Expectations

The government regulation significantly interferes with the investment-backed expectation of Bitcoin holders because the classification virtually disables owners from using it as currency. As

¹⁰⁸ *Id.* at 138.

¹⁰⁹ See *Palazzolo v. Rhode Island*, 533 U.S. 606, 617 (2001).

Where a regulation places limitations on land that fall short of eliminating all economically beneficial use, a taking nonetheless may have occurred, depending on a complex of factors including the regulation's economic effect on the landowner, the extent to which the regulation interferes with reasonable investment-backed expectations, and the character of the government action.

Id.; see also *Lingle v. Chevron U.S.A. Inc.*, 544 U.S. 528, 538 (2005) (“Outside these two relatively narrow categories . . . regulatory takings challenges are governed by the standards set forth in *Penn Central Transp. Co. v. New York City*, 438 U.S. 104, 98 S. Ct. 2646, 57 L. Ed. 2d 631 (1978).”).

¹¹⁰ See Michael Lewyn, *Character Counts: The “Character of the Government Action” in Regulatory Takings Actions*, 40 SETON HALL L. REV. 597 (2010).

Considering that the minimal economic impact of the Pennsylvania law affected both the Court's “reasonable investment-backed expectations” discussion and its “economic harm” discussion, *Keystone* suggests that these two *Penn Central* factors are intertwined: both relate to the degree of economic harm suffered by a takings plaintiff.

Id. at 604.

By mentioning the purposes and effects of government action, Justice O'Connor's concurrence [in *Palazzolo*] suggested that courts should continue to consider the importance of the purpose animating that action, as well as the relationship between that purpose and the action's economic effects; in short, whether the government's action effectively furthered an important purpose.

Id. at 607.

¹¹¹ *Id.* (“Between 2002 (when *Tahoe-Sierra* was decided) and 2005 (when *Lingle* was decided), lower courts generally agreed that the *Penn Central* “character” factor required them to balance the public interest favoring regulation against the impact regulation had on property owners.”).

mentioned above, Satoshi Nakamoto released the White Paper in January 2009.¹¹² According to the White Paper, Bitcoin is a means by which individuals can engage in commerce online without a third party using “electronic cash.”¹¹³ Even politicians and online handymen service startups are seeking to take advantage of using Bitcoin as a currency.¹¹⁴

Unlike currency, Bitcoin is subject to capital gains because it is classified as property.¹¹⁵ This regulation, therefore, economically impacts Bitcoin owners because it requires them to record every transaction, which exposes them to penalties for failing to do so.¹¹⁶ If, however, a Bitcoin owner fails to properly record the capital gains, a more direct impact results in the form of IRS fines of up to \$250,000.¹¹⁷

Another economic impact of the regulation is Bitcoin’s decreased value.¹¹⁸ Some market analysts attribute the recent decline

¹¹² Nakamoto, *supra* note 25.

¹¹³ Nakamoto, *supra* note 25.

¹¹⁴ See Meghan Keneally, *Bitcoin Is Gaining Currency in Political Campaign Donations*, ABC NEWS (Feb. 7, 2018), <http://abcnews.go.com/Politics/bitcoin-popular-political-campaign-donations/story?id=52873921>; see also Anna Irrera, *Lamborghini, Long Lines Welcome Crypto Fans at ‘Blockchain Week’*, REUTERS (May 15, 2018, 10:09 AM), <https://www.reuters.com/article/us-crypto-currencies-consensus/lamborghini-long-lines-welcome-crypto-fans-at-blockchain-week-idUSKCN1IG24B> (“‘It’s packed; it’s amazing,’ Frideric Prandecki, co-founder and CEO of Las Vegas-based Bob’s Repair, told Reuters at the event. His startup, which is building a blockchain-based website that lets users find handymen online, raised money by issuing its own cryptocurrency.”).

¹¹⁵ See *supra* note 4.

¹¹⁶ See *supra* note 4.

¹¹⁷ See *supra* note 92.

¹¹⁸ See Aaron Hankin, *Can Falling Bitcoin Prices Really Be Blamed on the Tax Man?*, MARKETWATCH (Apr. 6, 2018, 11:07 AM), <https://www.marketwatch.com/story/can-falling-bitcoin-prices-really-be-blamed-on-the-tax-man-2018-04-06>.

With lofty tax bills to pay, digital currency owners had to come up with the funds. “Odds are very high that if they made a bunch of realized money [meaning you bought and sold it in the same year] in crypto in 2017, they are still heavily weighted in crypto,” said Tim Enneking, founder and managing director of Crypto Asset Management. Enneking added that many investors re-entered their crypto longs as the price fell in early 2018, meaning, as their tax payments come due in early April, they are short U.S. dollars and are having to sell crypto to pay Uncle Sam.

Id.; see also Avi Salzman, *Bitcoin: Where’s That Post-Tax Price Boom We Were Promised?*, BARRON’S (Apr. 19, 2018, 12:00 PM), <https://www.barrons.com/articles/bitcoin-wheres-that-post-tax-price-boom-we-were-promised-1524153620>.

Bitcoin bulls have argued that tax season was a bummer for the digital coin, because owners were forced to sell their coins for cash and hand it over to the government. . . . It’s not clear if taxes induced one of the biggest currency owners to sell \$50 million in Bitcoin on Tuesday just before the

in Bitcoin's value to the regulation.¹¹⁹ These analysts explain that the IRS classification forces Bitcoin owners to sell their Bitcoin in order to pay the capital gains they made using the Bitcoin.¹²⁰ For example, the IRS requires people using Bitcoin to record any capital gains or losses measured by the buying price against the selling price.¹²¹ Assume the owner purchased his Bitcoin at \$1,000. If a Bitcoin owner buys a cup of coffee for \$10 using a unit of Bitcoin originally valued at \$5, the owner must record the \$5 capital gain.¹²² Thus, according to the analysts, if the Bitcoin owner does not have the cash on hand, he must sell his Bitcoin to pay the hypothetical \$5 capital gain.¹²³ Given the fact that Bitcoin is divisible by eight decimal points, such simple calculations will seldom occur.¹²⁴ The result of the mass selling,

deadline. That sale helped force the price of Bitcoin down by \$200 in less than 20 minutes.

Id.; Kellie Ell, *Bitcoin Makes a Comeback Now That Tax Season is Nearly Over: Venture Capitalist*, CNBC (Apr. 12, 2018, 7:20 PM), <https://www.cnbc.com/2018/04/12/tax-selling-is-behind-bitcoin-declines-crypto-investor.html> (noting a small increase days before taxes were due and predicting an increase despite that “[p]eople realiz[ing] way more tax gains in 2017 than they expected to . . . with crypto prices down 50 percent from their highs, people have to sell twice as much crypto to cover those taxes.” (internal quotations marks omitted)).

¹¹⁹ See *supra* note 118.

¹²⁰ See *supra* note 118. Others, like Ryan Taylor, CEO of Dash Core, argue the brief dip in Bitcoin's value was offset by those who were able to buy more Bitcoin due to favorable tax returns. Aaron Smith, *Bitcoin Surges 10% In an Hour Ahead of Tax Day*, CNN MONEY (Apr. 12, 2018, 1:23 PM), <https://money.cnn.com/2018/04/12/technology/bitcoin-rally-tax-day/index.html>.

¹²¹ McKenney, *supra* note 4, at 9 (“Notice 2014-21 requires a taxpayer who receives virtual currency as payment for goods or services to compute gross income using the fair market value of the virtual currency, measured in U.S. dollars, as of the date that the virtual currency is received.”).

¹²² McKenney, *supra* note 4, at 9.

For example, if a taxpayer uses a portion of a bitcoin to buy a cup of coffee each day for one week, he or she will have to determine what portion of the bitcoin was used to make the purchase based on the daily exchange rate, convert it into U.S. dollars, and keep a record of each transaction so that the gain or loss from his or her virtual currency property can be properly reported.

McKenney, *supra* note 4, at 9.

¹²³ See *supra* note 118.

¹²⁴ McKenney, *supra* note 4, at 9.

However, because bitcoins are divisible to eight decimal places, this means that each bitcoin can be divided up into 100 million pieces. . . . Due to the potential complexity of reporting otherwise simple retail purchase transactions related to virtual currencies, further guidance is needed to help taxpayers voluntarily comply with their tax obligations.

prompted to ensure IRS compliance, is more Bitcoin in circulation, which decreases its value.¹²⁵

Like the plaintiffs in *Pennsylvania Coal*, the regulation makes using Bitcoin as a currency commercially impracticable.¹²⁶ Unlike the plaintiffs in *Penn Central*, the IRS classification interferes with a Bitcoin owner's investment backed expectations because lawfully using it as a currency is virtually impossible given the lack of guidance from the IRS.¹²⁷ While the classification does not deprive a Bitcoin owner of using it as currency, doing so exposes the owner to IRS penalty, which, as illustrated in the IRS action against Coinbase, can be severe.¹²⁸ Although diminution in value, according to *Penn Central*, is insufficient by itself to justify a taking,¹²⁹ here the impact is both diminution in value and fines resulting from the impracticable requirement to record every transaction using Bitcoin. Balancing the economic impact on the investment-backed expectation against the character of government action further demonstrates why the IRS regulation constitutes a regulatory taking.

2. *The Character of the Government Action Unfairly Burdens Bitcoin Owners Because it is Arbitrary and Capricious*

Conflicting views exist regarding how courts determine the “character of government action” prong.¹³⁰ Some continue to balance the public versus private interests, while others confine the prong to

¹²⁵ See *supra* note 118.

¹²⁶ See *supra* note 101.

¹²⁷ McKenney, *supra* note 4, at 11 (“Because the IRS has determined that virtual currency is treated as property, the public may not understand that each purchase of consumer goods with a virtual currency could result in a reportable transaction.”).

¹²⁸ See *supra* note 91.

¹²⁹ *Penn Cent. Transp. Co., v. City of N.Y.*, 438 U.S. 104, 131 (1978).

¹³⁰ Lewyn, *supra* note 110, at 610.

Post-*Lingle* cases generally agree that lower courts must apply *Penn Central* to partial regulatory takings cases, but are divided as to the application of the *Penn Central* “character” factor. These cases fall into three categories: (1) cases reaffirming the “private harm/public interest” balancing test, (2) cases holding that the “character” factor is limited to physical invasions and similar situations, and (3) cases redefining the “character” factor as an inquiry into whether a small number of property owners have been unfairly burdened by a government regulation.

Lewyn, *supra* note 110, at 610.

physical invasions.¹³¹ A third approach inquires into whether the government regulation unfairly burdens some property owners.¹³² Considering there is no physical invasion, the following discussion focuses on the private harm versus public interest balance and the unfair burden approaches.

Under the private harm versus public interest approach to the character prong, the Bitcoin owner likely would carry his burden. The obvious public interest is to ensure currency has legal tender status in a given jurisdiction.¹³³ While this interest is certainly understandable, it lacks consistency; Taiwan, for example, is neither formally recognized by the United States, nor the United Nations.¹³⁴ Nonetheless, commercial transactions made using a bank account containing New Taiwan Dollars need not be recorded because the

¹³¹ Lewyn, *supra* note 110, at 610.

¹³² Lewyn, *supra* note 110, at 612.

A third group of cases focuses on whether “the burden of the regulation falls disproportionately on the relatively few property owners.” For example, in *Wensmann Realty v. City of Eagan*, a landowner sought to build houses on property zoned for a golf course and filed a lawsuit after the city rejected its application for rezoning.

Lewyn, *supra* note 110, at 612 (citation omitted).

¹³³ I.R.S. Notice 2014-21, 2014-16 I.R.B. 938.

In some environments, it operates like real currency—i.e., the coin and paper money of the United States or of any other country that is designated as legal tender, circulates, and is customarily used and accepted as a medium of exchange in the country of issuance—but it does not have legal tender status in any jurisdiction.

Id. at 9 (emphasis added).

¹³⁴ See *U.S. Relations with Taiwan*, U.S. DEP’T ST., Aug. 31, 2018, <https://www.state.gov/r/pa/ei/bgn/35855.htm>.

The United States and Taiwan enjoy a robust unofficial relationship. The 1979 U.S.-P.R.C. Joint Communique switched diplomatic recognition from Taipei to Beijing. In the Joint Communique, the United States recognized the Government of the People’s Republic of China as the sole legal government of China, acknowledging the Chinese position that there is but one China and Taiwan is part of China.

Id.; see also Sigrid Winkler, *Taiwan’s UN Dilemma: To Be or Not To Be*, BROOKINGS (June 20, 2012), <https://www.brookings.edu/opinions/taiwans-un-dilemma-to-be-or-not-to-be/>.

Taiwan is not a member of the United Nations (UN) or its suborganizations, but it aspires to participate. China opposes this. It argues, correctly, that only sovereign states can enjoy membership in the UN; any state that manages to enter into the UN system as a full member in its own right is seen by the other member states as a fully-fledged independent country.

Id.

purchaser is not deriving any income.¹³⁵ The classification of Bitcoin when compared to the New Taiwanese Dollar, therefore, is unduly burdensome because it is arbitrary and capricious¹³⁶ in that it allows someone to buy a cup of coffee in the United States using his Taiwanese bank account and not forcing him to pay a capital gain on whatever gain he obtains on the New Taiwanese Dollar, but a Bitcoin owner must record the same kind of capital gain.¹³⁷ Although the arbitrary and capricious standard—deriving from the APA—is applied when reviewing challenges to federal agency decisions,¹³⁸ the IRS classification serves as the regulation and thus applying this standard, in conjunction with an unfairly burdensome standard, is appropriate.

Under the preferable approach, which looks at whether the government regulation unfairly burdens some property owners, the character of the government action is arbitrary and capricious, which makes it unduly burdensome. This analysis emerged following a city's refusal to amend its zoning laws that classified a particular area as "Parks, Open Space, and Recreation."¹³⁹ In *Wensmann Realty, Inc. v. City of Eagan*, the plaintiff owned a golf course, which was subject to

¹³⁵ *Taxable and Nontaxable Income*, Publication 525, I.R.S., at 31, <https://www.irs.gov/pub/irs-pdf/p525.pdf>.

¹³⁶ *U.S. Postal Serv. v. Postal Regulatory Comm'n*, 785 F.3d 740 (D.C. Cir. 2015).

Even if the statute is ambiguous and does not foreclose the Commission's interpretation, however, the Commission's exercise of its authority must be "reasonable and reasonably explained" in order to survive *arbitrary and capricious* review under the Administrative Procedure Act. Furthermore, we review the Commission's interpretation of its own regulations with "substantial deference," allowing that interpretation to control unless "plainly erroneous or inconsistent with the regulation."

Id. at 750 (emphasis added) (citations omitted). See 5 U.S.C. § 706 (2018), which provides:

To the extent necessary to decision and when presented, the reviewing court shall decide all relevant questions of law, interpret constitutional and statutory provisions, and determine the meaning or applicability of the terms of an agency action. The reviewing court shall—

- (1) compel agency action unlawfully withheld or unreasonably delayed; and
- (2) hold unlawful and set aside agency action, findings, and conclusions found to be—
 - (A) arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law.

¹³⁷ See *supra* note 131.

¹³⁸ See *supra* note 136.

¹³⁹ *Wensmann Realty, Inc. v. City of Eagan*, 734 N.W.2d 623 (Minn. 2007).

this classification.¹⁴⁰ The golf course could not keep up with local competition, forcing the plaintiff to sell it to a real-estate developer.¹⁴¹

The sale could not go through, however, unless the city reclassified the golf course because residential houses could not be built on a lot with its current classification.¹⁴² The city denied plaintiff's request to reclassify arguing traffic and school overcrowding would ensue if more houses were built.¹⁴³ The plaintiff challenged the city's denial as a taking¹⁴⁴ arguing the denial was "arbitrary and capricious."¹⁴⁵ The Minnesota Supreme Court—although rejecting the arbitrary and capricious argument without explanation—held the city's reasons for denial, balanced against the harm incurred by the plaintiff, could constitute a taking if the plaintiff could no longer use the golf course as such.¹⁴⁶

Here, the character of the government action is unduly burdensome. Although a Bitcoin owner can still use his currency, doing so exposes him to penalties because it is virtually impossible to record each transaction.¹⁴⁷ This exposure, as the Inspector General of the Treasury Department seems to believe, is unwarranted when considering the complexity of Bitcoin.¹⁴⁸ Specifically, Bitcoin is divisible to eight decimal places meaning it can be divided up into 100 million pieces.¹⁴⁹ Expecting a Bitcoin owner to undergo this process merely in order to use it as a currency is unduly burdensome.

¹⁴⁰ *Id.* at 628.

¹⁴¹ *Id.*

¹⁴² *Id.*

¹⁴³ *Id.* at 629.

¹⁴⁴ *Wensmann*, 734 N.W.2d at 631-32 ("The language of the Takings Clause in the Minnesota Constitution is similar to the Takings Clause in the U.S. Constitution. *Zeman v. City of Minneapolis*, 552 N.W.2d 548, 551-52 (Minn.1996). We have therefore relied on cases interpreting the U.S. Constitution's Takings Clause in interpreting this clause in the Minnesota Constitution.").

¹⁴⁵ *Id.* at 627.

¹⁴⁶ *Id.* at 641-42.

The citizens of Eagan clearly value the open space that the golf course provides, but if the property owner is forced to leave the property undeveloped for the benefit of neighboring landowners without an opportunity to pursue a reasonable use of the property, the city is, in essence, asking the property owner to carry a burden that in all fairness should be borne by the entire community.

Id.

¹⁴⁷ McKenney, *supra* note 4, at 9.

¹⁴⁸ McKenney, *supra* note 4, at 9.

¹⁴⁹ McKenney, *supra* note 4, at 9.

Like the plaintiff in *Wensmann*, moreover, the IRS classification unfairly treats Bitcoin owners in comparison to people using New Taiwan Dollars. The government interest, therefore, cannot be reconciled so long as individuals making purchases with bank accounts containing New Taiwan Dollars are not taxed on the gains like Bitcoin owners. Thus, Bitcoin owners are unduly burdened due to the IRS's disproportionate treatment compared to those using New Taiwan Dollars.

Unlike the plaintiff in *Wensmann*, however, a Bitcoin owner likely could demonstrate the classification is arbitrary and capricious because it is neither reasonable, nor reasonably explained.¹⁵⁰ In *United States Postal Serv. v. Postal Regulatory Comm'n*, the D.C. Circuit held the Postal Regulatory Commission's regulation, which reclassified mail causing an increase for persons sending mail, was arbitrary and capricious.¹⁵¹ The D.C. Circuit explained that the Commission's failure to "reasonably explain" why it promulgated such an ambiguous regulation enabled it to conclude the decision was arbitrary and capricious.¹⁵² Unless the IRS can reasonably explain why it is classifying Bitcoin as property, given the uncertainty in the regulation, the Notice could be found arbitrary and capricious.

Finally, companies exchanging Bitcoin into conventional currency must register as money transmitters.¹⁵³ Charlie Shrem,

¹⁵⁰ See *supra* note 146.

¹⁵¹ 785 F.3d 740, 750 (D.C. Cir. 2015).

We hold that the statute and regulations are ambiguous and that, contrary to the Postal Service's arguments, the "plain language" does not forbid regulation of mail preparation requirement changes with rate effects. We hold, however, that the Commission's decision is *arbitrary and capricious* because it is not "reasonably explained."

Id.

¹⁵² *Id.* The Postal Service amendment disabled mailers from obtaining an automatic discounted rate previously available to mailers who used technology that reduced Postal Service costs.

¹⁵³ *United States v. Faiella*, 39 F. Supp. 3d 544 (S.D.N.Y. 2014).

The Financial Crimes Enforcement Network ("FinCEN") has issued guidance specifically clarifying that virtual currency exchangers constitute "money transmitters" under its regulations. See FinCEN Guidance at 1 ("[A]n administrator or exchanger [of virtual currency] is an MSB [money services business] under FinCEN's regulations, specifically, a money transmitter, unless a limitation to or exemption from the definition applies to the person." (emphasis in original)).

Id. at 546.

FinCEN has further clarified that the exception on which defendant relies for its argument that Faiella is not a "money transmitter," 31 C.F.R. §

founder of BitInstant, was prosecuted and convicted of operating an unlicensed money transmitting business in violation of 18 U.S.C. § 1960.¹⁵⁴ The Southern District of New York explained, “Bitcoin clearly qualifies as ‘money’ or ‘funds’ under these plain meaning definitions. Bitcoin can be easily purchased in exchange for ordinary currency, acts as a denominator of value, and is used to conduct financial transactions.”¹⁵⁵ In the same way someone must register as a money transmitter before converting New Taiwan Dollars, so must someone converting Bitcoin.

Thus, under both approaches, the character of the government action can be labeled as unduly burdensome because it is arbitrary and capricious. Although ensuring currency is government backed is a legitimate interest, the government’s treatment of currency from unrecognized countries undermines the public interest in favor of the private harm. The IRS, it appears, is trying to have its cake and eat it too. But, the Fifth Amendment might present a bulwark against the IRS’s regulation considering that, while a Bitcoin owner likely cannot secure monetary just compensation for this taking, he could obtain what Professor Thomas W. Merrill terms an Anticipatory Remedy.¹⁵⁶

IV. JUST COMPENSATION CAN BE RECLASSIFICATION

A trend is emerging among courts whereby injunctive relief replaces monetary relief on takings claims.¹⁵⁷ Professor Merrill argues this approach avoids undue delay in litigating Takings Clause cases.¹⁵⁸ He explains that although the Tucker Act requires plaintiffs to bring Takings Clause actions in D.C. based Court of Federal Claims, this

1010.100(ff)(5)(ii)(F), is inapplicable. *See* FinCEN Guidance at 4 (“It might be argued that the exchanger is entitled to the exemption from the definition of ‘money transmitter’ for persons involved in the sale of goods or the provision of services. . . . However, this exemption does not apply when the only services being provided are money transmission services.”).

Id. at 546-47.

¹⁵⁴ *Id.* at 545 (explaining that Shrem operated under the pseudonym Robert Faiella).

¹⁵⁵ *Id.* (citing *SEC v. Shavers*, 2013 WL 4028182, at *2 (E.D. Tex. Aug. 6, 2013) (“It is clear that Bitcoin can be used as money. It can be used to purchase goods or services. . . . [I]t can also be exchanged for conventional currencies. . . .” (alteration in original))).

¹⁵⁶ *See* Merrill, *supra* note 24.

¹⁵⁷ Merrill, *supra* note 24, at 1631 (“On other occasions however—and usually without acknowledging the inconsistency—the Court has reviewed takings claims without requiring that they first be submitted to the court having authority to award just compensation.”).

¹⁵⁸ Merrill, *supra* note 24, at 1631.

process is overly time consuming considering plaintiffs seeking injunctive or declaratory relief can only do so in Article III courts.¹⁵⁹ Anticipatory relief, Professor Merrill explains, can be grounded in a challenge to a federal agency rule that the rule is arbitrary and capricious.¹⁶⁰ The following section will argue the Takings Clause can be raised as a defense in an IRS action against a Bitcoin owner who did not comply with the Notice.

In 2015, the Court modified the Fifth Amendment definition of property to include personal property.¹⁶¹ What it also did, however, was create a precedent for asserting the Takings Clause as a defense in a judicial review proceeding before seeking compensation.¹⁶² In *Horne*, the petitioners were fined for failing to comply with the Agriculture Marketing Agreement Act of 1937 (hereinafter “AMAA”).¹⁶³ The AMAA required raisin handlers to set aside a portion of their raisin crop for the government, which it “sells, allocates, or otherwise disposes of [them] in ways [the government]

¹⁵⁹ Merrill, *supra* note 24, at 1643-44.

With respect to the federal government, the APA contains a general waiver of sovereign immunity for actions seeking relief other than “money damages.” Thus, insofar as one can seek declaratory or equitable relief for takings, the APA clears the way for suits in federal courts of general jurisdiction. The Tucker Act, which authorizes suits against the United States founded “upon the Constitution,” has been held to constitute a waiver of sovereign immunity for claims seeking compensation for takings.

Merrill, *supra* note 24, at 1643-44 (footnotes omitted).

¹⁶⁰ Merrill, *supra* note 24, at 1630, 1632.

[C]laimants who wish to advance claims enforced by injunctions or declaratory judgments (for example, that the government action was arbitrary and capricious) must seek relief in an Article III court.

...

A petition for review of federal agency action under the agency’s authorizing statute or the Administrative Procedure Act (APA) could provide the basis for such a determination.

Merrill, *supra* note 24, at 1630, 1632.

¹⁶¹ *Horne v. Dep’t. of Agric.*, 135 S. Ct. 2419, 2426 (2015) (“The Government has a categorical duty to pay just compensation when it takes your care, just as when it takes your home.”).

¹⁶² Although Professor Merrill discusses *Horne I*, the Court’s subsequent holding in 2015 confirms that the Takings Clause can be used as a defense. See Merrill, *supra* note 24, at 1636 (“*Horne v. Department of Agriculture*, in which the Court held that a takings claim could be raised defensively in a judicial review proceeding in a court of general jurisdiction without the claimant’s first seeking compensation from the CFC.”).

¹⁶³ *Horne*, 135 S. Ct. at 2425.

determines are best suited to maintain an orderly market.”¹⁶⁴ During the petitioners’ first trip to the Court, in *Horne I*, they raised a takings defense arguing they were producers, and not handlers, within the definition of the AMAA to avoid paying the handler fine.¹⁶⁵ The Court, in *Horne I*, held the Ninth Circuit erred in ruling the petitioners could not raise a takings claim defensively, i.e., the Hornes were not obligated to bring their Takings Clause claim in the Court of Federal Claims before raising it as a defense.¹⁶⁶

The Takings Clause defense was that AMAA itself was a taking because it allowed the government to take the Hornes raisin crop without providing them with just compensation.¹⁶⁷ Thus, on remand the petitioners argued the Ninth Circuit erred again in denying their Takings Clause defense.¹⁶⁸ The Ninth Circuit once again rejected this argument and held that no taking occurred because petitioners retained an interest in the raisins the government did not sell.¹⁶⁹ As a corollary, the Ninth Circuit explained the reserve requirement was analogous to a condition on participating in the raisin market.¹⁷⁰

The Court disagreed and held, instead, that the retention of some interest does not abrogate the taking because the Hornes were deprived of making the ultimate decision vis-à-vis the raisins.¹⁷¹ This inability, according to the Court, constituted a *per se* taking like that in

¹⁶⁴ *Id.* at 2424.

¹⁶⁵ *Id.* at 2425.

¹⁶⁶ *Horne v. Dept. of Agriculture*, 569 U.S. 513, 528-29 (2013) [hereinafter “*Horne II*”].

In the case of an administrative enforcement proceeding, when a party raises a constitutional defense to an assessed fine, it would make little sense to require the party to pay the fine in one proceeding and then turn around and sue for recovery of that same money in another proceeding. . . . Petitioners were therefore free to raise their takings-based defense before the USDA. And, because § 608c(14)(B) allows a handler to seek judicial review of an adverse order, the district court and Ninth Circuit were not precluded from reviewing petitioners’ constitutional challenge. The grant of jurisdiction necessarily includes the power to review any constitutional challenges properly presented to and rejected by the agency. We are therefore satisfied that the petitioners raised a cognizable takings defense and that the Ninth Circuit erred in declining to adjudicate it.

Id.

¹⁶⁷ *Horne*, 135 S. Ct. at 2425.

¹⁶⁸ *Id.*

¹⁶⁹ *Id.*

¹⁷⁰ *Id.* (“The court instead viewed the reserve requirement as a use restriction, similar to a government condition on the grant of a land use permit.”).

¹⁷¹ *Id.* at 2428.

Loretto because the Hornes lost “the entire bundle of property rights in the appropriated raisins.”¹⁷² Conditioning participation in the raisin market on a forty-seven percent contribution of the owner’s crop, moreover, was likewise rejected.¹⁷³

Now, the Court could not have reached this conclusion without holding that the AMAA provided a scheme whereby a disgruntled handler could seek relief—thus removing the Tucker Act requirement.¹⁷⁴ In this vein, Professor Merrill argues the Court could have just said, given that the claim is for anticipatory relief, it could be raised in federal court.¹⁷⁵ In other words, considering a CFC claim cannot be heard while an administrative claim is pending, allowing the suit to be brought in an Article III court makes sense because the claims are the same in both courts, but injunctive relief can only be obtained in the Article III court.¹⁷⁶

On this line, *Wensmann* and *U.S. Postal Service* should permit a suit challenging a classification in an Article III court instead of first raising it in an administrative proceeding or the CFC. So, if the IRS

¹⁷² *Horne*, 135 S. Ct. at 2428 (internal quotations marks omitted).

The reserve requirement imposed by the Raisin Committee is a clear physical taking.

. . .

Raisin growers subject to the reserve requirement thus lose the entire bundle of property rights—the rights to possess, use and dispose of them—with the exception of the speculative hope that some residual proceeds may be left when the Government is done with the raisins.

Id. (internal citations omitted).

¹⁷³ *Id.* at 2430-31.

In one of the years at issue here, the Government insisted that the Hornes turn over 47 percent of their raisin crop, in exchange for the “benefit” of being allowed to sell the remaining 53 percent. . . . Selling produce in interstate commerce . . . is similarly not a special governmental benefit that the Government may hold hostage, to be ransomed by the waiver of constitutional protection.

Id.

¹⁷⁴ *Id.* at 2431 (“But we held in *Horne I* that the Hornes may, in their capacity as handlers, raise a takings-based defense to the fine levied against them. We specifically rejected the contention that the Hornes were required to pay the fine and then seek compensation under the Tucker Act.”).

¹⁷⁵ Merrill, *supra* note 24, at 1659 (“Justice Thomas’s opinion in *Horne* would have been more persuasive if he had simply recognized that the case was one in which anticipatory review of the takings issue by a court of general jurisdiction was appropriate.”).

¹⁷⁶ See *supra* note 159; see also Merrill, *supra* note 24, at 1659-60 (“Moreover, given that the takings claim was based on the same operative facts as the APA claim, and the APA action was filed first, there is authority suggesting that the CFC could not consider the takings claims as long as the APA challenge remained pending.”).

brings an action against a Bitcoin holder for non-compliance, the defendant can raise the Takings Clause as a defense. Instead of seeking judicial review of the fines, however, the Bitcoin holder should rely on *Wensmann Realty* and challenge the classification itself as a taking with a prayer for injunctive relief in the form of re-classification of Bitcoin from property to currency.

V. CONCLUSION

At least one commentator has argued *Horne* created a *per se* rule of unconstitutionality when a taking of personal property occurred.¹⁷⁷ Should this in fact be the case, challenging the IRS regulation as a taking would be far simpler because the *Penn Central* test would not be the appropriate approach.¹⁷⁸ In other words, if the Notice is evaluated as a possessory taking, the subsequent analysis would be far simpler than that described above because it will be presumptively unconstitutional.¹⁷⁹ However, given the Court's general inconsistency regarding the Takings Clause, evaluating the Notice as

¹⁷⁷ *Takings Clause—Regulatory Takings—Horne v. Department of Agriculture*, 129 HARV. L. REV. 261 (2015).

Last Term, in *Horne v. Department of Agriculture*, the Court revisited this debate, this time in the context of personal property. In the process of holding that the Takings Clause categorically applies to certain personal property cases, the Court reflexively applied its “*per se*” approach to a regulatory scheme governing the national raisin market. In so doing, the Court dismissed as irrelevant valuable precedent discouraging the use of categorical rules in takings cases involving personal property.

Id. at 261 (footnote omitted).

¹⁷⁸ *Id.* at 270.

By applying a categorical rule to a regulation of personal property, the *Horne* Court not only eliminates this burden but deprives the government of the opportunity to defend its myriad regulations of personal property that might fall into this new category. This, in turn, seems to leave the government unable to argue on behalf of mandatory consumer product recalls, seizures of unsafe drugs, or an agency's demands for records. The holding in *Horne* thus threatens to stymie certain key functions of the government, leaving it unable to “go on” effectively without paying sweeping compensation.

Id. (footnotes omitted).

¹⁷⁹ *Id.* Arguing the Notice constitutes a possessory taking, however, would be a stretch because no physical taking of Bitcoin occurs as a result of the Notice. Rather, the Notice disables Bitcoin owners from using it as intended without any type of seizure. If, for example, the Notice compelled Bitcoin owners to forfeit their Bitcoin upon failure to comply with the reporting requirements, then perhaps a possessory taking would be arguable due to the impossibility of making accurate reports.

a regulatory taking under the *Penn Central* test is, if anything, prudent to ensure its success.¹⁸⁰

A more compelling reason to approach the Notice under the traditional regulatory takings framework, aside from the fact that no “physical” taking of Bitcoin occurs, is that such a claim is unique in the wake of *Horne*. To date, the constitutionality of the Notice has not been raised insofar as it is accepted as a legitimate exercise of the IRS’s rulemaking power.¹⁸¹ Nonetheless, the Notice, as demonstrated above, is a regulation in the traditional sense because it carries with it the force of law.¹⁸² Bitcoin, moreover, though intangible, satisfies the traditional requirements to be considered property.¹⁸³

The overall treatment of Bitcoin by the government creates an illusion that it is some sort of hybrid whereby the United States Marshals can auction it as if it were a boat,¹⁸⁴ but is also subject to money-transmitter restrictions.¹⁸⁵ The latter permits the inference that it is currency.¹⁸⁶ Granted, it could be argued the treatment is consistent insofar that it receives the same treatment as foreign currency—also classified as property for income tax purposes—because currency converters must report their capital gains.¹⁸⁷ However, this argument

¹⁸⁰ *Lucas v. S.C. Coastal Council*, 505 U.S. 1003 (1992).

¹⁸¹ *United States v. Coinbase, Inc.*, No. 17-CV-01431-JSC, 2017 WL 5890052, at *1 (N.D. Cal. Nov. 28, 2017) (“IRS Notice 2014-21 describes how the IRS applies U.S. tax principles to transactions involving virtual currency such as bitcoin.”).

¹⁸² *See supra* Part III.A.

¹⁸³ *See supra* Part II.

¹⁸⁴ *See supra* note 18.

¹⁸⁵ *United States v. Faiella*, 39 F. Supp. 3d 544, 547 (S.D.N.Y. 2014) (citing 18 U.S.C. § 1960(b)(1)) (“[A]n administrator or exchanger [of virtual currency] is an MSB [money services business] under FinCEN’s regulations, specifically a money transmitter, unless a limitation to or exemption from the definition applies to the person.”).

¹⁸⁶ *Id.* at 545-46.

Bitcoin clearly qualifies as “money” or “funds” under these plain meaning definitions. Bitcoin can be easily purchased in exchange for ordinary currency, acts as a denominator of value, and is used to conduct financial transactions.

. . .

Third, Faiella clearly qualifies as a “money transmitter” for purposes of Section 1960. The Financial Crimes Enforcement Network (“FinCEN”) has issued guidance specifically clarifying that virtual currency exchangers constitute “money transmitters” under its regulations.

Id. (emphasis in original).

¹⁸⁷ Currency converters must report capital gains because they are money transmitters for purposes of the Bank Secrecy Act. See 31 C.F.R. § 1010.100(e) (2018), which provides:

likely fails because while currency converters derive profit from the conversion, their customers need not report the capital gains should they buy a cup of coffee using the newly acquired currency.¹⁸⁸

Although it is conceded the United States can decide what currency to accept, an arbitrary and capricious regulation unduly burdening holders of one currency warrants an explanation.¹⁸⁹ Toll booths in Northern New York, for example, accept Canadian currency, but do not require the individual report a capital gains even if the loonie, at the time of payment, was worth more than when the owner acquired it.¹⁹⁰ The expected justification is that a recognized government, Canada, backs the loonie.¹⁹¹ However, as described above, the New Taiwanese Dollar enjoys similar treatment (albeit not at toll booths near the border) even though Taiwan is not recognized independently from China.¹⁹²

Whether the IRS's failure to provide a workable means for Bitcoin users to report transactions to ensure compliance is purposeful, however, is unknown. This article is not arguing that the IRS's failure is part of some conspiracy to undermine Bitcoin in general by exposing users to civil and criminal penalties to discourage the use of Bitcoin.

(e) Bank Secrecy Act. The Currency and Foreign Transactions Reporting Act, its amendments, and the other statutes relating to the subject matter of that Act, have come to be referred to as the Bank Secrecy Act. These statutes are codified at 12 U.S.C. 1829b, 12 U.S.C. 1951-1959, 18 U.S.C. 1956, 18 U.S.C. 1957, 18 U.S.C. 1960, and 31 U.S.C. 5311-5314 and 5316-5332 and notes thereto.

¹⁸⁸ See *supra* note 135.

¹⁸⁹ See *supra* note 151.

¹⁹⁰ *Thruway Authority Announces Updated Discount Rate for Canadian Currency at Toll Plazas*, N.Y. ST. THRUWAY AUTHORITY, Feb. 9, 2016, <http://www.thruway.ny.gov/news/pressrel/2016/02/2016-02-09-canadian-currency.html>.

The Thruway Authority today announced an updated discount rate of 35 percent for Canadian currency at all toll plazas along the Thruway beginning Saturday, Feb. 13. The Canadian dollar is now valued at 35 percent less than the U.S. dollar. For example, a toll of \$1 U.S. will be \$1.54 Canadian at Thruway toll plazas. This update will allow for a fair exchange rate in areas closer to the Canadian border. A toll paid with Canadian currency of any amount less than one dollar will be accepted without discount and any necessary change will be given in Canadian, if available. If one dollar or more of Canadian currency is tendered, it will be discounted at the current rate of the whole dollar amount (35 percent).

Id.

¹⁹¹ *Striking In Its Solitude—The 1-Dollar Coin, Familiarly Known As The 'Loonie'*, ROYAL CANADIAN MINT, <http://www.mint.ca/store/mint/about-the-mint/1-dollar-5300014#.WvNyNMvy8o> (last visited Oct. 23, 2018).

¹⁹² See *supra* note 135.

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Rather, the IRS, regardless of its motive, can be held accountable for its ambiguous treatment of Bitcoin by challenging the constitutionality of its regulatory scheme covering the issue. Thus, considering Bitcoin owners expected to use it as currency, and the Notice arbitrarily both impairs the value of Bitcoin and exposes owners to potential civil or criminal penalty when used as such, the Takings Clause is one route Bitcoin owners can pursue to re-classify it as currency.