



Tax Insights
from Financial Services

Proposed digital asset legislation signals evolving tax framework

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In brief

What happened?

Two recently proposed bills--the Virtual Currency Tax Fairness Act (S. 4171) and the Digital Asset PARITY Act-- would significantly reshape the US federal income tax treatment of digital assets. Together, they signal continued bipartisan interest in modernizing the tax framework for cryptocurrencies, stablecoins, and related activities. The proposals address longstanding issues, including de minimis transactions, stablecoin treatment, wash sale rules, staking, lending, and trader elections, and could materially affect both individual and institutional taxpayers.

Why is it relevant?

These proposals reflect a policy shift toward integrating digital assets into the existing tax framework rather than treating them as an outlier. While the proposed de minimis rule in the Virtual Currency Tax Fairness Act addresses usability concerns, the broader PARITY Act underscores congressional intent to close perceived gaps (e.g., wash sales) while enabling institutional participation.

Actions to Consider

Taxpayers engaged in digital asset transactions should begin evaluating how these proposals could affect compliance processes, transaction tracking, and tax planning strategies. Taxpayers should monitor whether these provisions are included in broader tax legislation, what role Treasury could play in issuing guidance if enacted, and how the proposals would interact with existing IRS digital asset reporting rules.

In detail

Virtual Currency Tax Fairness Act

The Virtual Currency Tax Fairness Act (S. 4171) would introduce a targeted change to the US tax treatment of digital assets by excluding certain small-value (de minimis) transactions from gross income. The proposal is intended to reduce administrative burdens associated with tracking and reporting gains or losses on routine personal transactions involving virtual currency. The provision would apply to transactions entered into after December 31, 2026.

The bill would create new Section 139K of the Internal Revenue Code to provide that gain or loss from the sale or exchange of virtual currency is excluded from gross income, subject to specified limitations.

Observation: This approach represents a departure from current law, under which all dispositions of digital assets are generally taxable events, regardless of size.

The bill defines 'virtual currency' as a digital representation of value that functions as a medium of exchange, store of value, or unit of account, and is not denominated in US dollars or foreign currency

Observation: This definition broadly aligns with existing IRS guidance but excludes fiat currency.

The exclusion would apply only if both of the following thresholds are satisfied:

- The total value of the transaction does not exceed \$200, and
- The total gain or loss that otherwise would be recognized does not exceed \$200.

If either threshold is exceeded, the entire transaction would remain fully taxable. Beginning in tax years after 2027, the \$200 threshold would be indexed for inflation, with adjustments rounded to the nearest \$10.

To prevent abuse, the bill includes an aggregation rule under which multiple transactions that are part of the same transaction, or a series of related transactions, are treated as a single transaction for purposes of applying the \$200 threshold.

Observation: This provision is intended to limit taxpayers' ability to fragment larger transactions into smaller amounts to qualify for the exclusion.

The exclusion would not apply to transactions involving cash or cash equivalents, property used in a trade or business, and property held for the production of income (investment property). As a result, the provision is primarily targeted at personal-use transactions, such as using cryptocurrency to purchase goods or services.

Observation: The proposed legislation reflects a policy effort to distinguish between investment use and consumer use of digital assets. While the \$200 threshold may improve usability, its relatively low amount and the inclusion of aggregation rules could limit its practical impact.

Digital Asset PARITY Act

The proposed Digital Asset PARITY Act represents a comprehensive effort to modernize the US federal income tax treatment of digital assets. The bill introduces new rules addressing stablecoins, trading,

lending, staking, wash sales, mark-to-market elections, and charitable contributions, while also providing definitions and clarifications for key digital asset concepts.

Observation: The Digital Asset PARITY Act reflects a legislative intent to integrate digital assets into the existing tax system, rather than treat them as a separate category. While the proposal introduces helpful clarity in several areas and more closely aligns the digital asset rules with the rules regarding trading in securities and commodities, it also signals increased scrutiny and a move toward closing perceived gaps in compliance and enforcement. If enacted, taxpayers would need to carefully analyze their current trading activity in digital assets to avoid any potential foot faults created by the new rules.

The bill proposes the following changes:

Regulated payment stablecoins transactions: The bill would establish specific provisions for regulated payment stablecoins, generally providing nonrecognition of gain or loss on disposition unless the taxpayer's basis falls below 99% of the redemption value and assigning a deemed \$1 basis in certain exchanges, effectively aligning qualifying stablecoins more closely with cash-like instruments.

Trading safe harbor for digital assets: The bill would expand existing Section 864(b) trading safe harbor rules to digital assets, allowing non-US taxpayers to trade digital assets through US brokers or agents, and trading for a taxpayer's own account without creating a US trade or business (with certain limitations for dealers).

Tax treatment of digital asset lending agreements: The bill would amend Section 1058 to extend securities lending rules to certain eligible digital assets, define qualifying digital assets and exchanges, require substitute payments (such as staking rewards) to be included in gross income, and clarify that the rules do not affect securities law classification. Treasury also would be granted authority to issue guidance, including how the rules are intended to apply to forks and airdrops.

Application of wash sale rules: The proposal would expand wash sale rules to include digital assets by redefining covered property as 'specified assets.' This change would prevent taxpayers from recognizing losses and reacquiring substantially identical positions in digital assets during the 61-day period around the sale.

Mark-to-market election: The bill would allow dealers and traders in actively traded digital assets to elect mark-to-market accounting, similar to rules applicable to securities and commodities traders.

Application of constructive sale rules: Existing constructive sale rules (Section 1259) would be expanded to include digital assets, potentially accelerating gain recognition in certain hedging transactions.

Treatment of digital assets acquired through passive validation activities: The bill would create a new subchapter governing digital assets acquired through passive validation, under which newly created digital assets generally would be included in gross income at fair market value upon receipt with a corresponding basis increase, but taxpayers could elect to defer income and capitalize related costs, resulting in ordinary income or loss during the election period and capital gain or loss upon disposition after the election period.

Charitable contributions and qualified appraisals: The bill would enhance rules for charitable contributions of digital assets, imposing stricter substantiation and valuation requirements, particularly for non-actively traded assets, limiting deductions in certain cases to the proceeds received upon sale, and introducing penalties for fraudulent acknowledgments by donee organizations.

Tax treatment of certain digital asset activity: The bill would amend Section 7701 to clarify that passive staking does not constitute a trade or business and to provide that certain trustee powers related to staking, liquidity management and responding to technological changes in digital asset investment trusts would not be treated as varying the investments or otherwise jeopardizing the trust's classification as a non-business investment trust.

Definitions: The bill would amend Section 7701 to add definitions for 'digital assets' including defining a digital asset broadly as a value recorded on a distributed ledger, establishing criteria for 'actively traded digital assets,' based on fungibility, trading volume, market capitalization, and ownership thresholds (with inflation adjustments), and defining 'staking' as the use of digital assets to support transaction validation on blockchain or similar technologies.

Let's talk

For a deeper discussion of how these proposals might affect your business, please contact:

Taxation of Digital Assets

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