

**SAN ANTONIO EPC**

**THE DIGITAL DOWNLOAD: A PRIMER ON  
PLANNING FOR AND ADMINISTERING DIGITAL  
ASSETS**

FEBRUARY 21, 2023 | ABIGAIL EARTHMAN & BRI LOUGHLIN

Please read important information at the end of the presentation.



## ABIGAIL EARTHMAN

500 N. Akard Street  
Suite 3300  
Dallas, TX 75201  
[AEarthman@perkinscoie.com](mailto:AEarthman@perkinscoie.com)  
D +1.214.965.7793

# Agenda

- I. Introduction**
- II. Types of Digital Assets
- III. Barriers to accessing Digital Assets
- IV. Pre- Death Advising Clients & Drafting Considerations
- V. Post-Death Advising Clients & Drafting Considerations
- VI. Taxation & Reporting
- VII. Takeaways
- VIII. Q&A



# @CRISTIANORONALDO

SOURCE:CRISTIANORONALDO.COM

# Introduction – Why Should We Care about Cryptocurrencies?

- **Total Number of Cryptocurrencies:** 22,222 (as of January 6, 2023)<sup>1</sup>
- **Total Market Cap:** Almost \$1.85 trillion (as of April 14, 2022) vs. \$814,360,064,944 (as of January 6, 2023 @9:18 CST)
- **Number of Users of Coinbase:** Over 108 million (as of January 6, 2023)<sup>2</sup>
- **Number of Blockchain.com Wallets:** Over 84 million (as of January 6, 2023)<sup>3</sup>
  - Compared to Users of Traditional Investment Accounts:
    - TD Ameritrade: 11 million accounts (as of January 6, 2023)<sup>4</sup>
    - Charles Schwab: 11.6 million active brokerage accounts (as of January 6, 2023)<sup>5</sup>
- **Percentage of Individuals Between Ages 24-38 Who either had \$50,000 of Investable Assets or Earned \$100,000+/Year and Owned Cryptocurrency:** 25% (as of November 1, 2019)<sup>6</sup>
- **Number of Businesses that Accept Cryptocurrency:** Approx. 100 (as of September 13, 2018) vs. Now nearly 36% of small business accept Bitcoin <sup>7</sup>
  - AT&T, Microsoft, and Burger King

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1. <https://www.coinmarketcap.com> (last visited January 6, 2023).

2. <https://www.coinbase.com/about> (last visited January 6, 2023).

3. <https://www.blockchain.com/charts/> (last visited January 6, 2023).

4. <https://www.tdameritrade.com/about-us.page> (last visited January 6, 2023).

5. U.S. SEC Form 10-K The Charles Schwab Corporation, found at:

[https://content.schwab.com/web/retail/public/about-schwab/YE\\_2018\\_Form\\_10-K.pdf](https://content.schwab.com/web/retail/public/about-schwab/YE_2018_Form_10-K.pdf) (last visited January 6, 2023).

6. See Megan Henney, *More Rich Millennials Are Investing in Cryptocurrencies*, found at

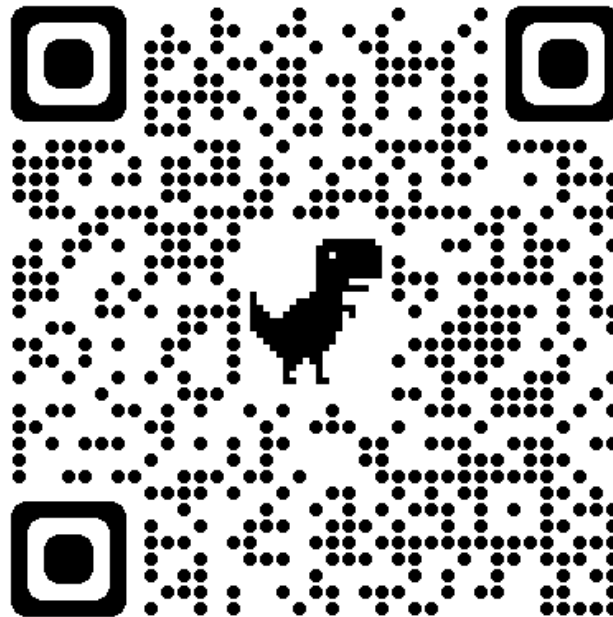
<https://www.foxbusiness.com/personal-finance/more-rich-millennials-are-investing-in-cryptocurrencies-heres-why.amp> (November 1, 2018).

7. See Jonas, Chokun, *Who Accepts Bitcoins*, found at:

<https://www.99bitcoins.com/who-accepts-bitcoins-payment-companies-stores-take-bitcoins/> (last updated September 13, 2018).

# Introduction - The Internet of Things (“IoT”)

Physical objects or “things” embedded with software, technology, or sensors with the purpose to connect or exchange information with other IoTs or systems over the internet.



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# Types of Digital Assets

## PERSONAL

- Photos and Documents
- Email accounts
- Bank accounts
- **Social media**
- Subscriptions
- Digital Wallets (not to be confused with financial wallets)\*

## FINANCIAL

- Assets stored on the Blockchain
- Cryptocurrency
- NFTs



# \*Digital Wallets vs. Electronic Payment



- Digital Wallet vs. Blockchain.com wallet
- Access to credit and bank accounts without a physical device
- Facilities digital financial transactions
- Added security and protection

# What is Blockchain?

- **A blockchain provides the means to record and store distributed ledger transactions.**
- **Blockchain is much more than Bitcoin**
  1. Bitcoin is the first “use case” for blockchain technology.
    - Satoshi Nakamoto’s Bitcoin “whitepaper”
    - Genesis Block (first Bitcoin) was mined on January 3, 2009.
  2. Ethereum project, for example, has its own blockchain capable of very different actions.
    - Smart contracts
  3. Other blockchain use cases:
    - Trusts and estates
    - Elections
    - Health records

# What is Blockchain? (continued)

## DEFINING FEATURES OF BLOCKCHAIN

1. Decentralized, peer-to-peer network
2. Transactions on blockchain are public
3. Immutable
4. Secure

## ADVANTAGES OF BLOCKCHAIN

1. Faster
2. Less costly
3. More secure

# Why Call It a Blockchain?

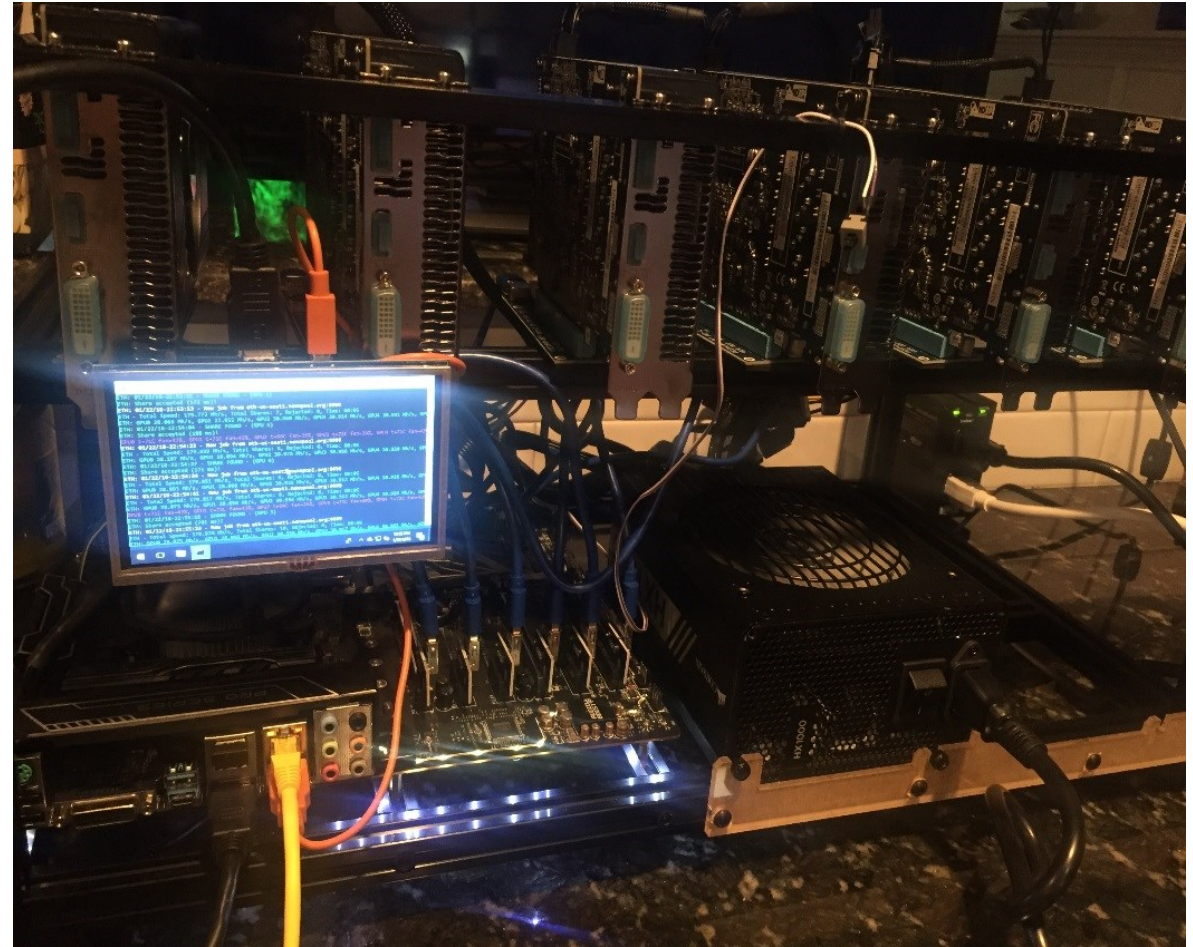
- **Pending transactions, once verified, are grouped into blocks of data. Blocks are linked sequentially by reference to the immediately preceding block, creating an unbreakable chain.**
- **Each block, once verified and incorporated into the ledger, is immutable.**
  - To reverse a transaction, one has to enter into a new transaction. No changes or erasures.
- **There is no running tally of one participant's transactions.**
  - Assets are traced, not asset owners.

# What Are Cryptocurrencies?

- **Cryptocurrency Is Not Fiat Currency**
- **Different Currencies**
  1. Digital
  2. Virtual
  3. Crypto
- **Why Care about Cryptocurrencies?**
  1. Market value
  2. User base

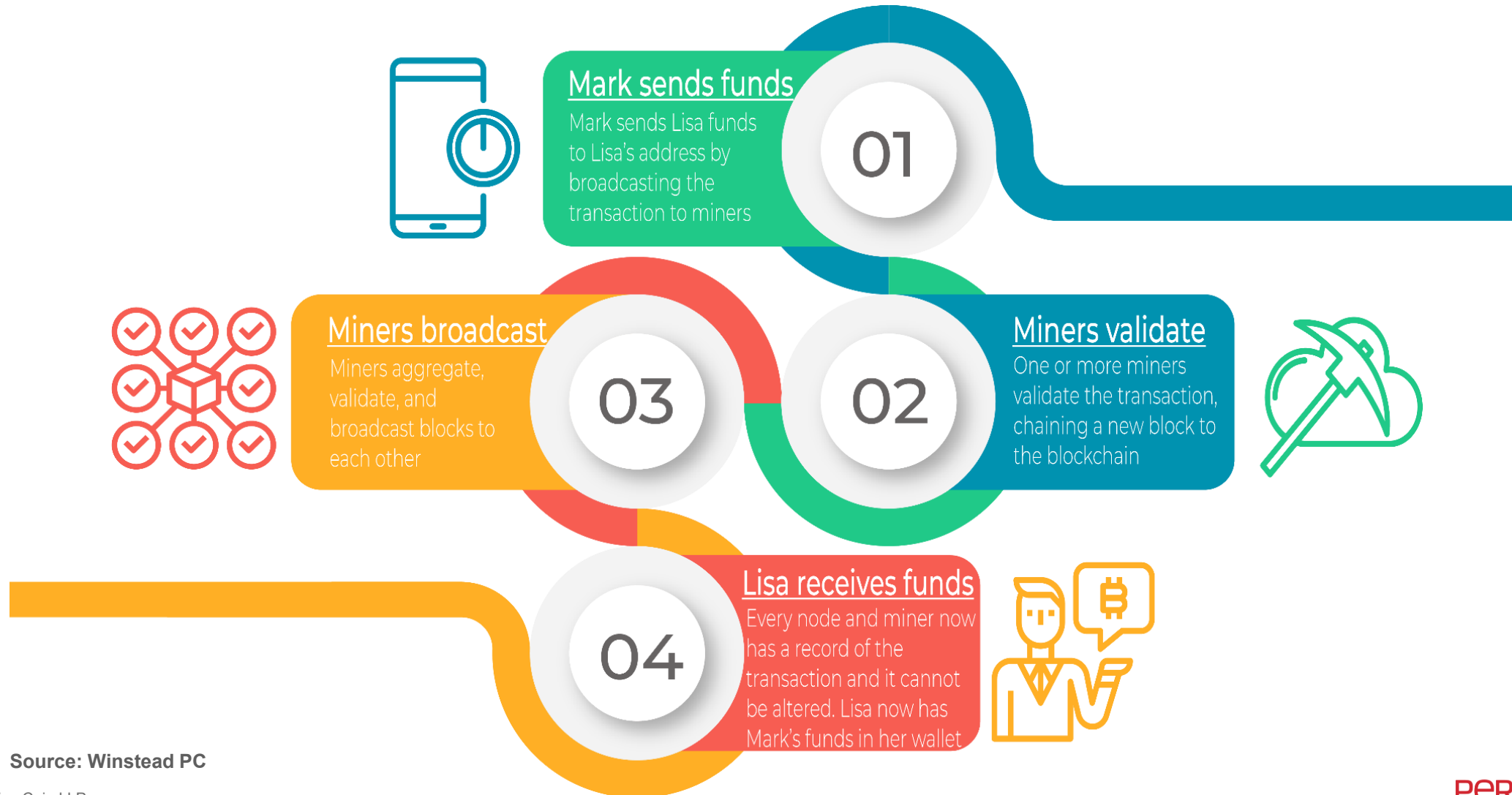
# How Do You Obtain Cryptocurrency?

- Purchase on exchange.
- Accept it for goods or services.
- Mine it.



Source: Abigail Rosen Earthman

# What Does a Transaction on a Blockchain Look Like?



Source: Winstead PC



# What Does a Transaction on a Blockchain Look Like? (continued)

## Sending Funds

- Verify both parties have an eligible cryptocurrency wallet.
- Share address through QR code or barcode.
  - Private and public keys



Source: [https://en.wikipedia.org/wiki/QR\\_code](https://en.wikipedia.org/wiki/QR_code)



### Mark sends funds

Mark sends Lisa funds to Lisa's address by broadcasting the transaction to miners

01



# What Does a Transaction on a Blockchain Look Like? (continued)

## VALIDATING THE TRANSACTION

- Miners validate.
- Miners “hash” the transaction.
- Transactions are grouped together.
- New block is created and added to the Blockchain.



Source: Abigail Rosen Earthman

02

### Miners validate

One or more miners validate the transaction, chaining a new block to the blockchain



# What Does a Transaction on a Blockchain Look Like? (continued)

## BROADCASTING THE TRANSACTION

- Aggregate
- Validate
- Broadcast



### Miners broadcast

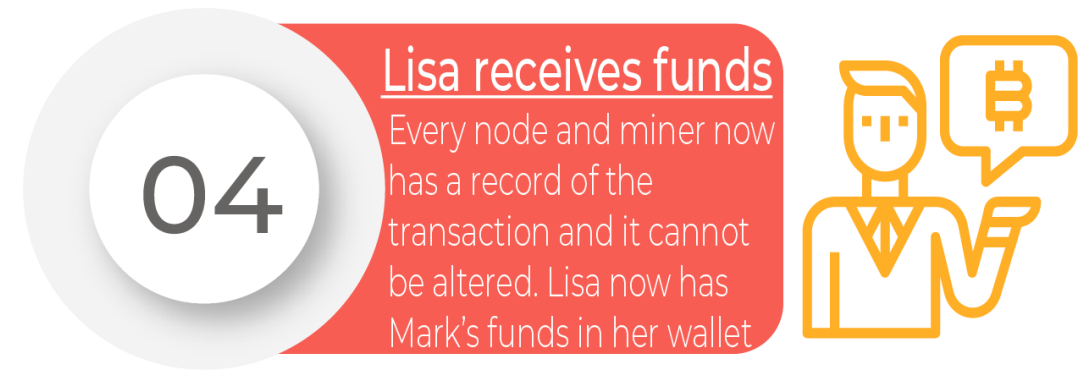
Miners aggregate, validate, and broadcast blocks to each other

03

# What Does a Transaction on a Blockchain Look Like? (continued)

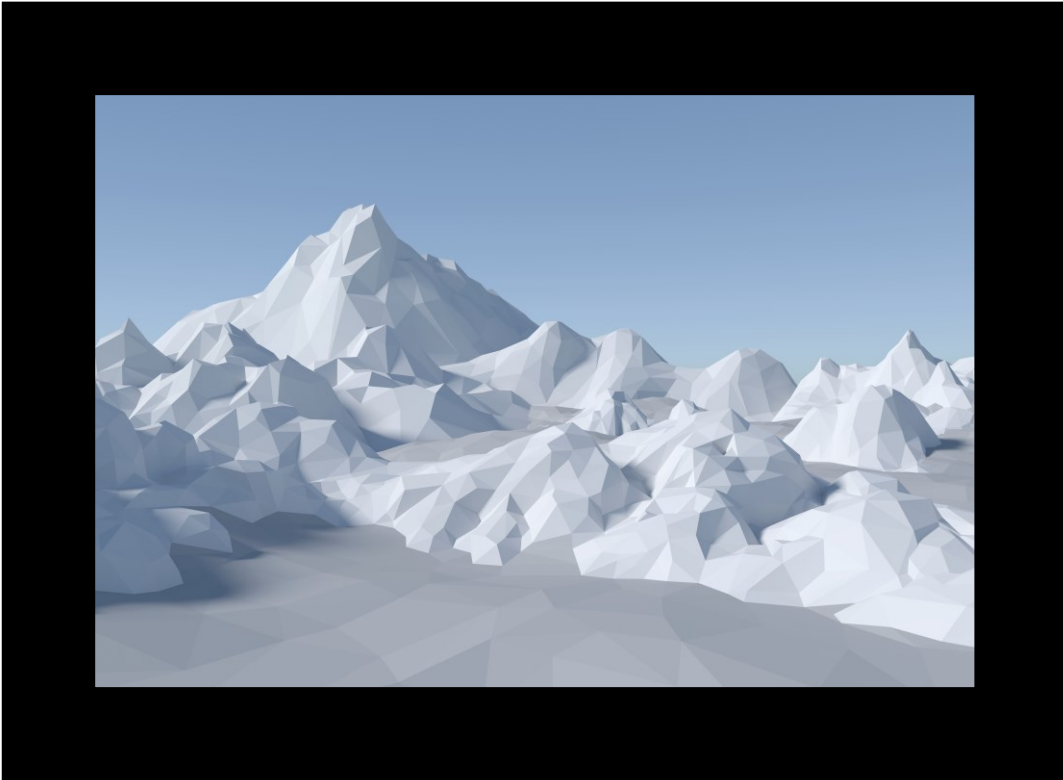
## COMPLETING THE TRANSACTION

- Recorded on distributed ledger
- Cannot be altered or changed
- Transaction becomes public
- Assets are traced, not asset owners



# Storage

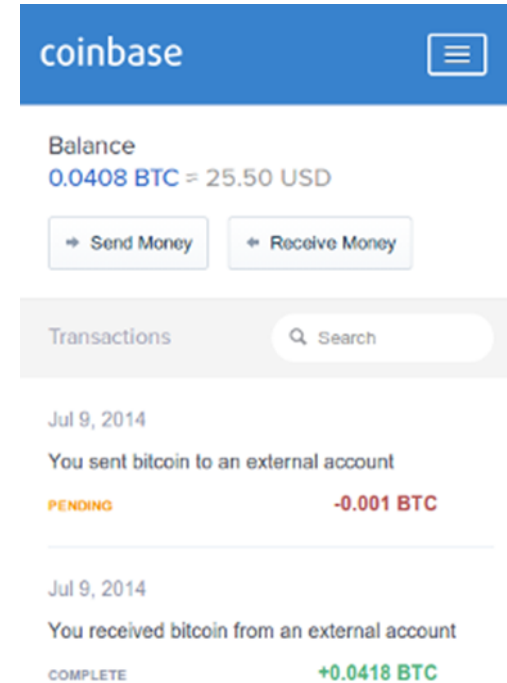
**COLD**



**HOT**



# What is Hot and What is Cold?

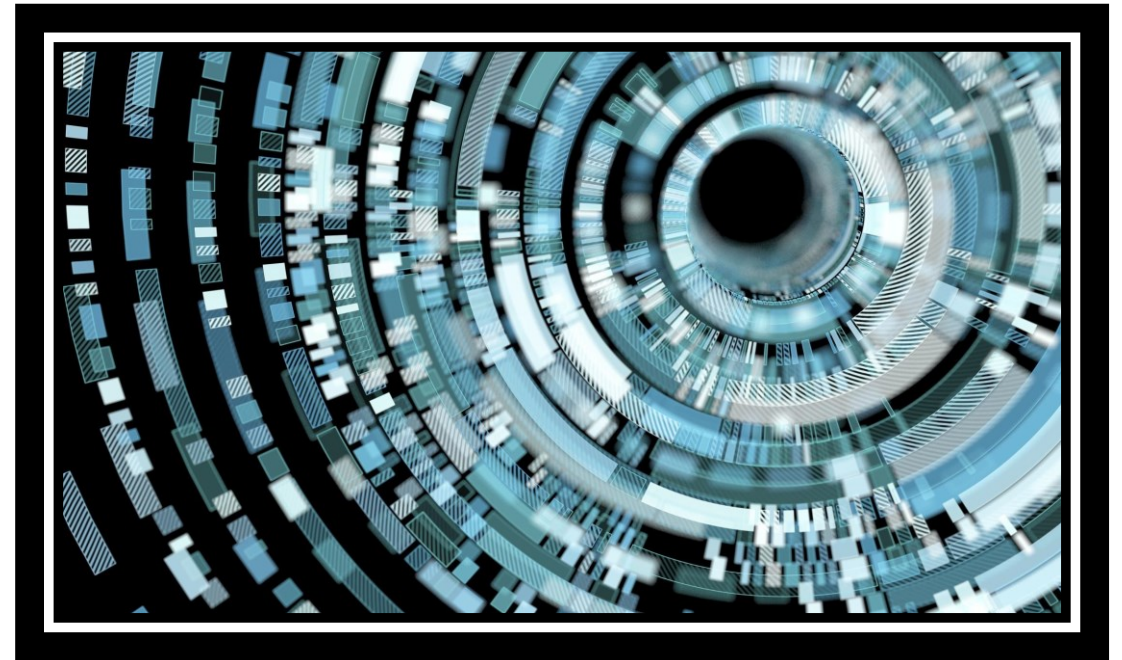


Source: <https://www.amazon.com/Trezor-bitcoin-wallet-white/dp/B00P5HU80A>



# What is an NFT?

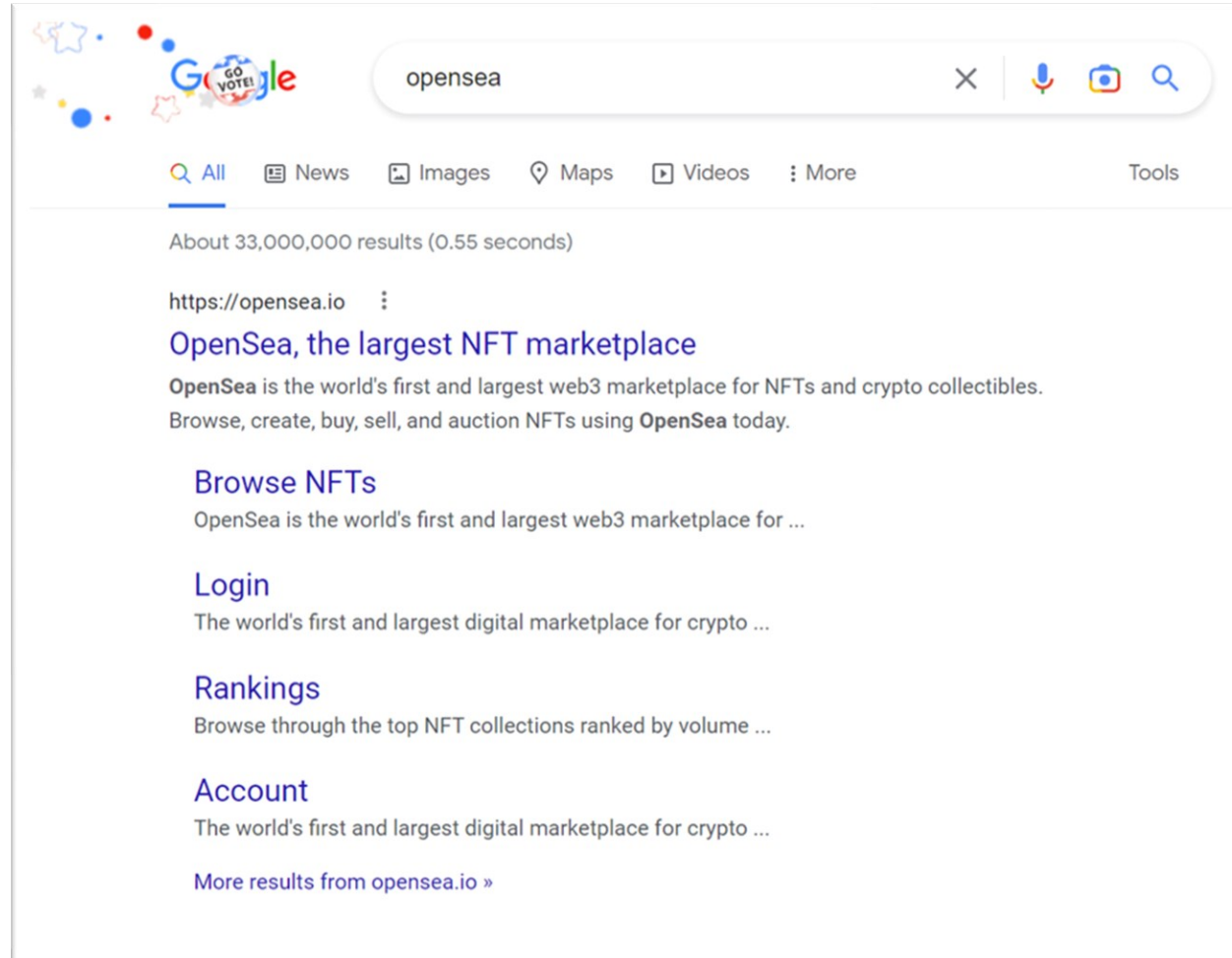
- **Non-Fungible Token**
- **Ownership:** Represents ownership in an underlying physical or digital asset (you can own a fraction of a Van Gogh)
- **Creation:** Anyone with a blockchain wallet and a small amount of Crypto can create and sell an NFT
- **Storage:** Hot, Medium, Cold
- **Protocol:** Derived from the blockchain that the NFT is placed on



# Let's Buy an NFT!

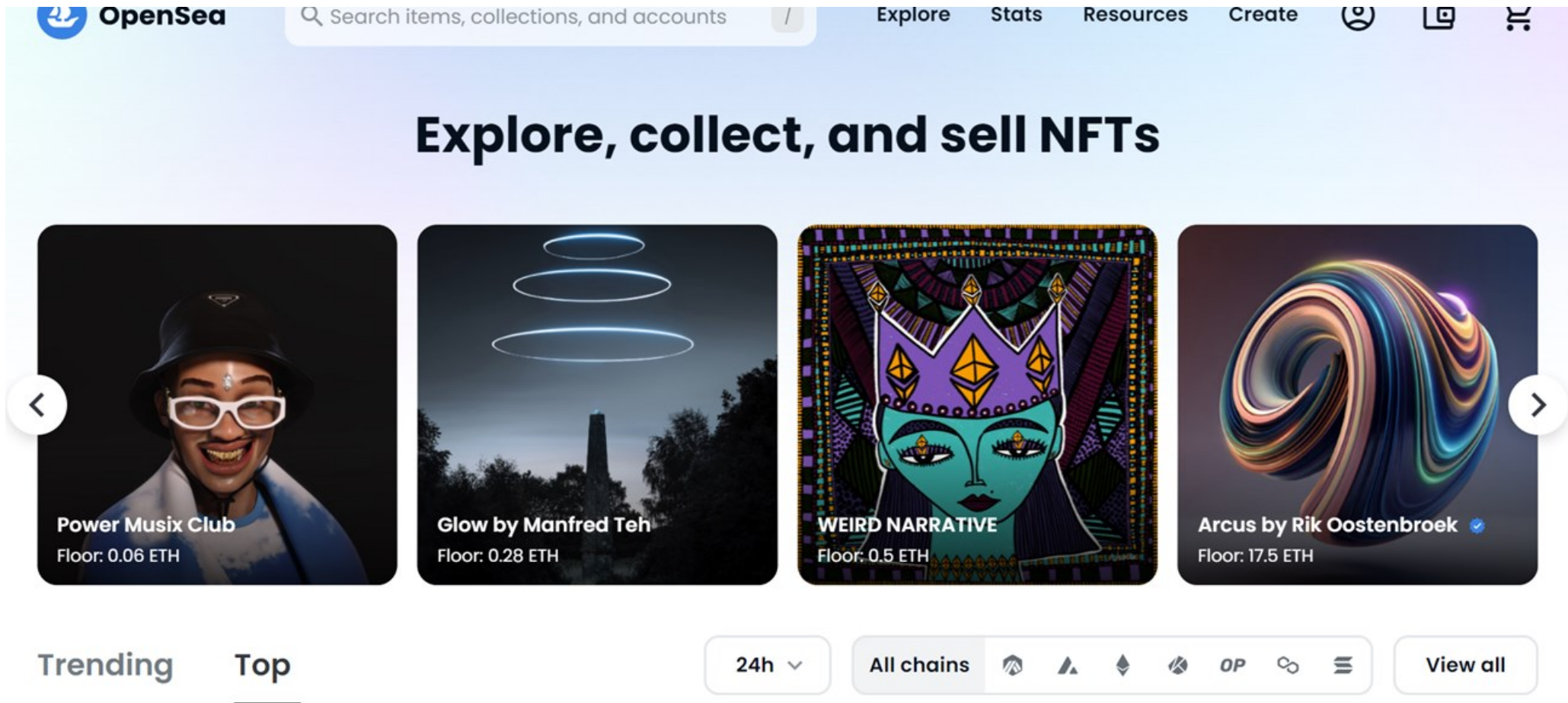


# Find a Platform

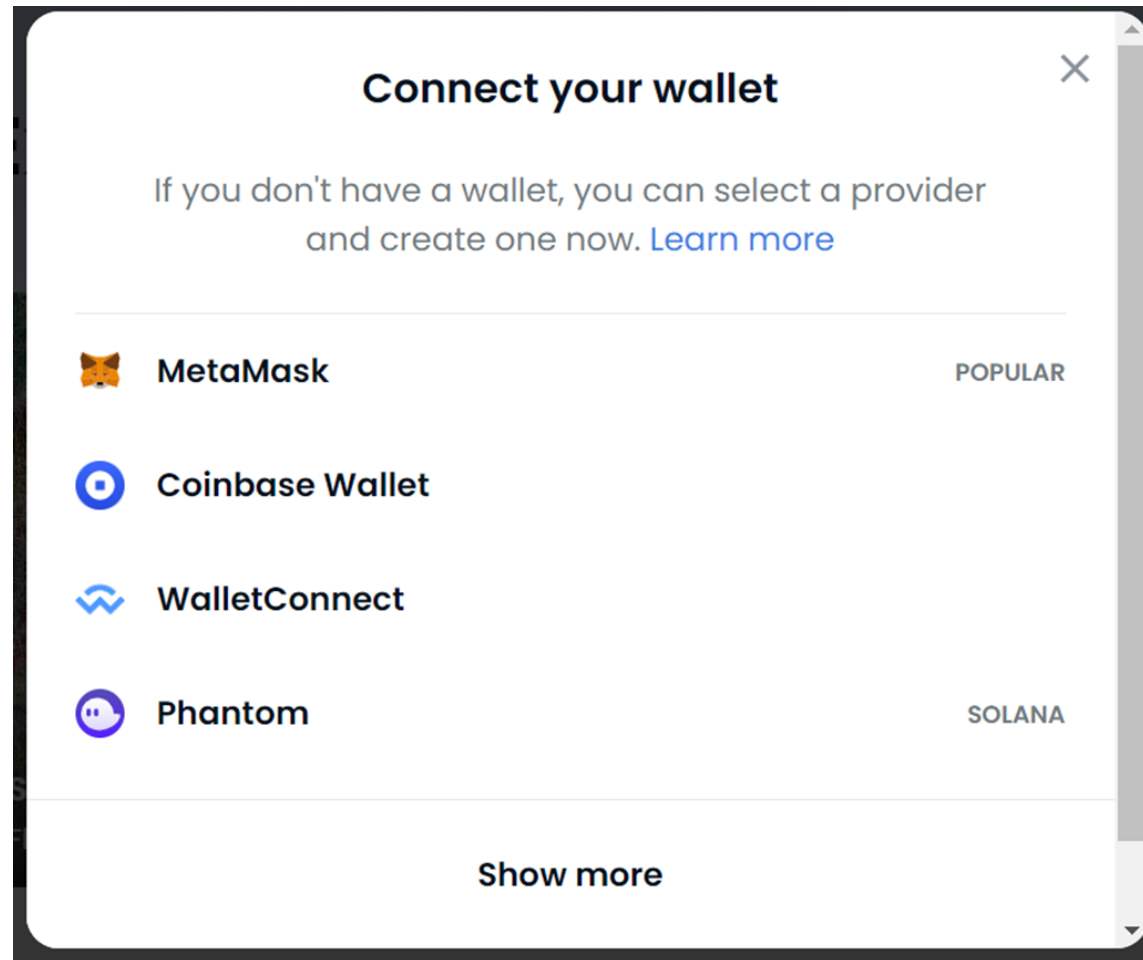




# OpenSea



# Make sure you have an accepted Wallet



# Hot Wallet - AHHHH


Try the Coinbase  
Wallet extension

Install

- Connect to crypto apps with one click
- Your private key is stored securely
- Works with Ethereum, Polygon, and more

Or scan to connect

Open [Coinbase Wallet](#) on your mobile phone and scan



bart0634.cb.id

\$182.50

Buy Swap Bridge Send Receive

Invite your friends

Crypto NFTs DeFi

Ethereum \$182.50 0.135 ETH

# Time to Shop!

The screenshot displays the OpenSea website interface. At the top, the OpenSea logo is on the left, followed by a search bar containing the text "Search items, collections, and accounts". To the right of the search bar are navigation links for "Explore", "Stats", and "Resources". Below the header, there are two featured collection cards: "Gossamer Academy" with a floor price of 0.04 ETH, and "SOL - 365" with a floor price of 1.42 ETH. A dropdown menu is open on the right side of the page, listing various NFT categories: All NFTs, Art, Collectibles, Domain Names, Music, Photography, Sports, Trading Cards, Utility, and Virtual Worlds. Below the featured cards, the "Trending" tab is selected, showing a table of collections. The table has columns for "COLLECTION", "FLOOR PRICE", and "VOLUME". The top entry is "Pirate Nation - Fou..." with a floor price of 0.14 ETH and a volume of 86 ETH. A URL bar at the bottom of the browser window shows "https://opensea.io/explore/collections".

OpenSea

Search items, collections, and accounts

Explore Stats Resources



Gossamer Academy  
Floor: 0.04 ETH

SOL - 365  
Floor: 1.42 ETH

All NFTs  
Art  
Collectibles  
Domain Names  
Music  
Photography  
Sports  
Trading Cards  
Utility  
Virtual Worlds


Trending Top

24h


|   | COLLECTION   |  | FLOOR PRICE | VOLUME |
|---|--|--|-------------|--------|
| 1 |  Pirate Nation - Fou...  |  | 0.14 ETH    | 86 ETH |

https://opensea.io/explore/collections

# Too expensive!



**Fidenza by Tyler Hobbs** 


By **Art\_Blocks** 

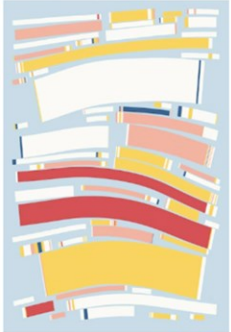
Items **999** · Created **Oct 2021** · Creator fee **7.5%** · Chain **Ethereum**

Art Blocks Collection: Curated ...  
See more ▾


|                                   |                              |                             |                     |                      |                             |
|-----------------------------------|------------------------------|-----------------------------|---------------------|----------------------|-----------------------------|
| <b>53,769 ETH</b><br>total volume | <b>99 ETH</b><br>floor price | <b>69 ETH</b><br>best offer | <b>5%</b><br>listed | <b>457</b><br>owners | <b>46%</b><br>unique owners |
|-----------------------------------|------------------------------|-----------------------------|---------------------|----------------------|-----------------------------|

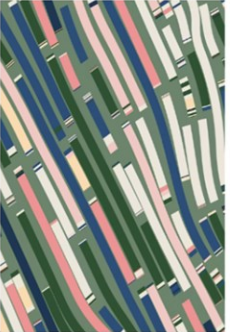
Items Analytics **BETA** Activity

 Updated 1m ago 999 items





**Fidenza #630**  
**99 ETH**






**Fidenza #159**  
**99 ETH**  
Last sale: 1.75 WETH







**Fidenza #970**  
**100 ETH**  
Last sale: 76.69 ETH







# Much Cheaper



## WhoWhos TreeHouse

By A647C9

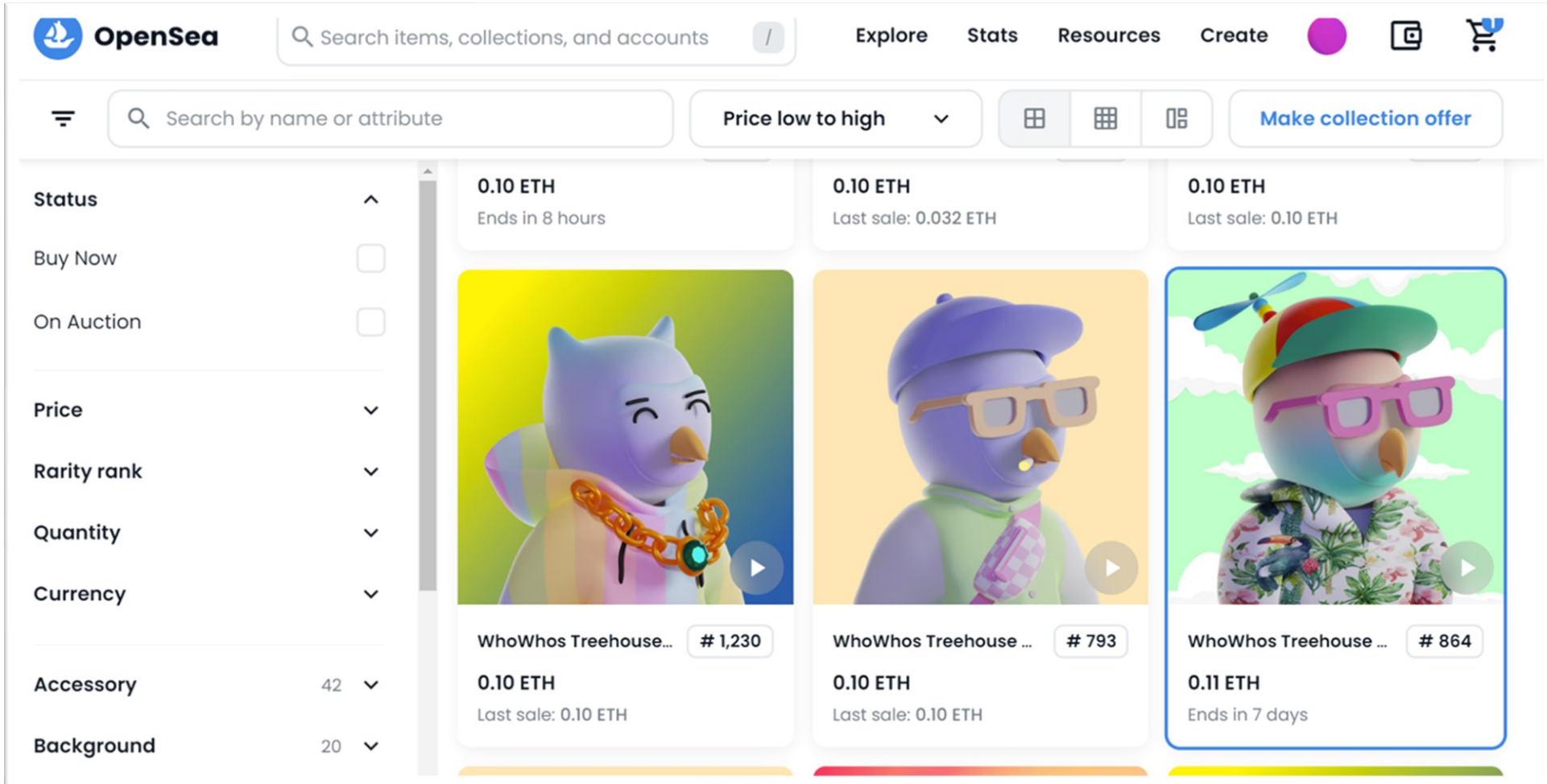
Items 1,722 · Created Apr 2022 · Creator fee 5% · Chain Ethereum

STILL MINTING <https://whowhos.io> WhoWho's TreeHouse is a collection of 7,777 colorful owls that grants holders exclusive access into the musical universe created by Grammy Nominated, Multi-Platinum music producer IllaDaProducer.

[See less ^](#)

|                               |                                 |                                |                     |                      |                             |
|-------------------------------|---------------------------------|--------------------------------|---------------------|----------------------|-----------------------------|
| <b>29 ETH</b><br>total volume | <b>0.059 ETH</b><br>floor price | <b>0.033 ETH</b><br>best offer | <b>2%</b><br>listed | <b>891</b><br>owners | <b>52%</b><br>unique owners |
|-------------------------------|---------------------------------|--------------------------------|---------------------|----------------------|-----------------------------|

# Pick your NFT!




# Checkout!

Your cart ⓘ

×

1 item

Clear all



WhoWhos Treehou...

WhoWhos TreeHou...

Creator fee: 5%

0.110 ETH


Total price


0.11 ETH

\$146.69

Payment method

Crypto

☒  Crypto

☐  Credit or debit card

Send to a different wallet

▼

Complete purchase

+

+

↺

↑

↓

Buy

Swap


Bridge

Send

Receive

Invite your friends

×


 Review

Request from opensea.io ⓘ

Asset changes (estimate) ⓘ

−0.11 ETH

+WhoWhos Tr...



Address

0x0000...e581

↗

Wallet used

0xf632...5E20

↗

Network

Ethereum

Network fee ⓘ

\$46.00 – \$61.62

⚙

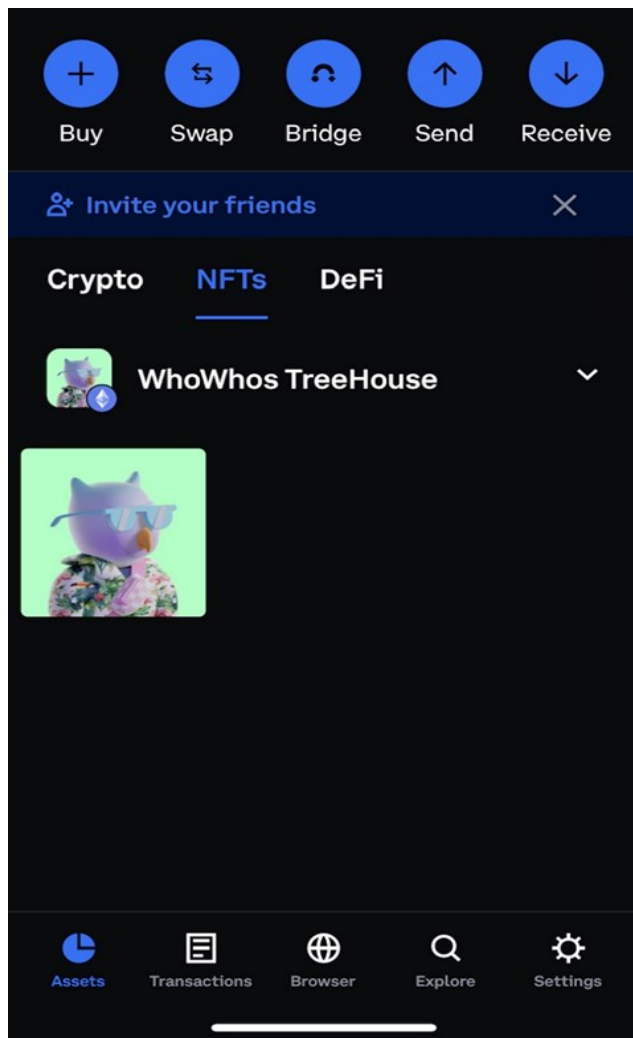
0.0461 ETH (\$61.62) may be required for the transaction. Please deposit more ETH.

Cancel

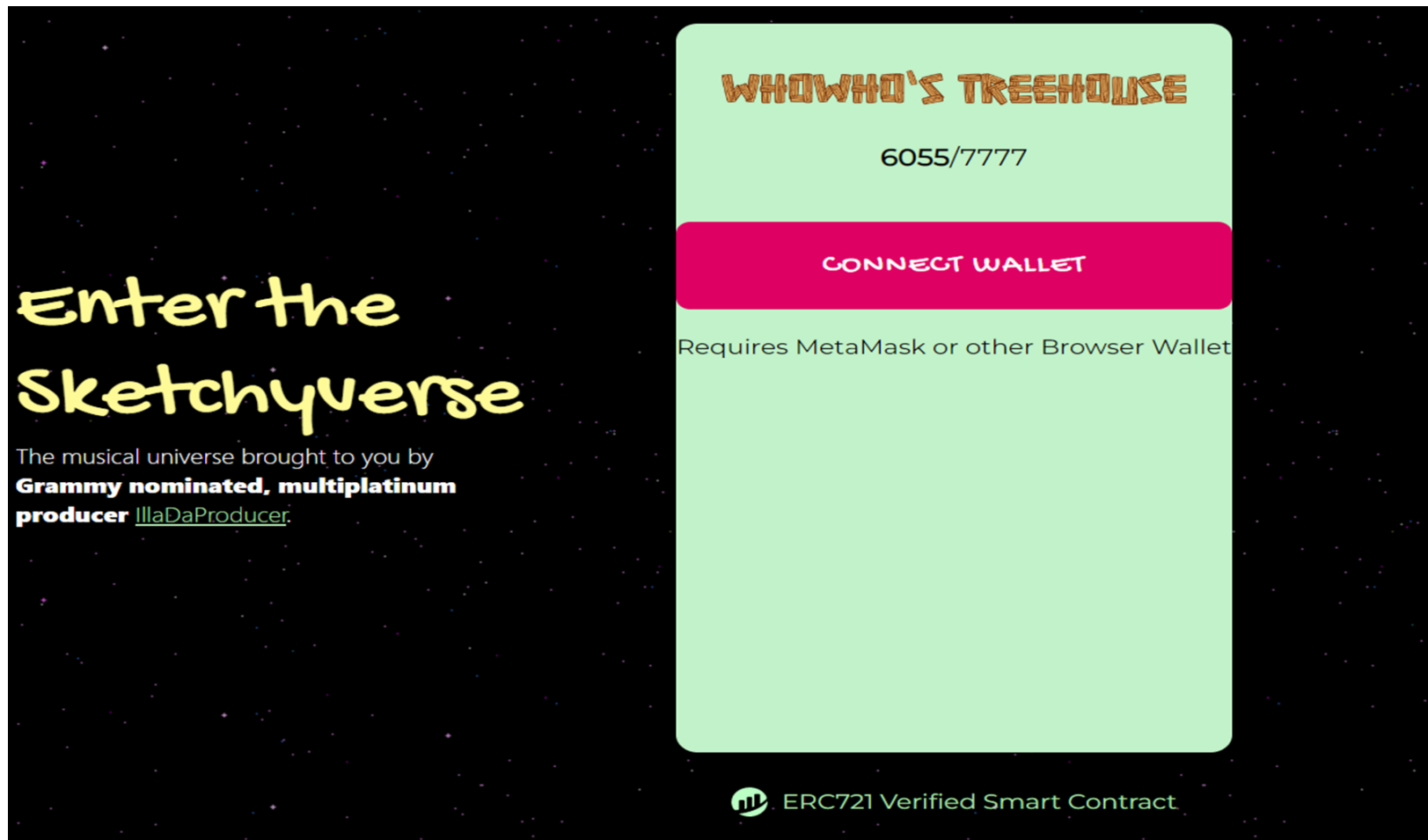
Confirm



# See it in your Wallet



# Bonus Material!



# More Bonus!

## NFT Info

### Benefits to holders

Each NFT has a beat attached to it

In order to win the commercial rights to your beat, you have to write the best song on that beat.

Once you write your song you can submit your track in our discord in the channel named after your beat

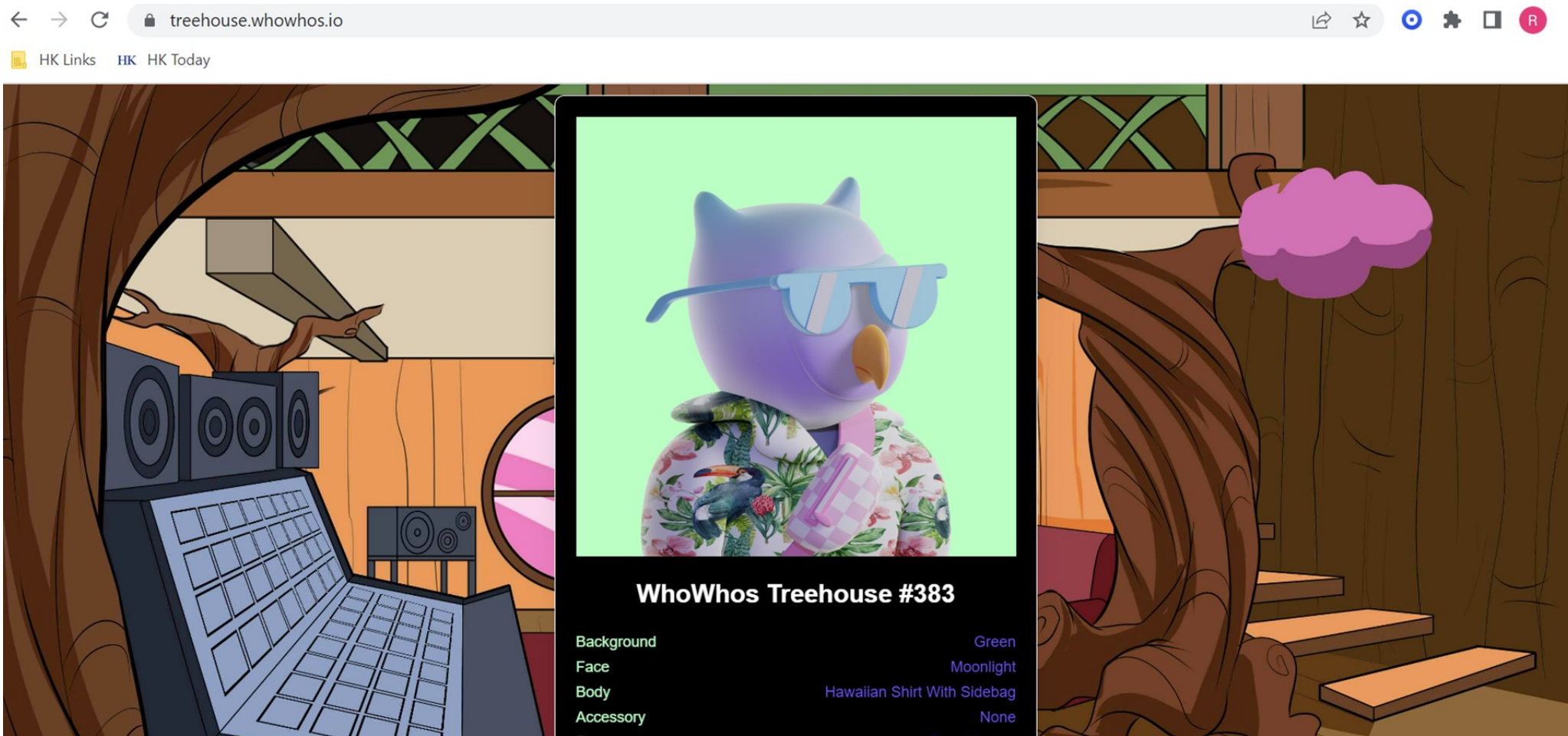
Once you win the track, Illa will submit your song to the biggest labels, A&Rs, publishers and artists in the game if you want your song shopped for you.

If you just want to keep your song then you are free to release your song as an NFT.

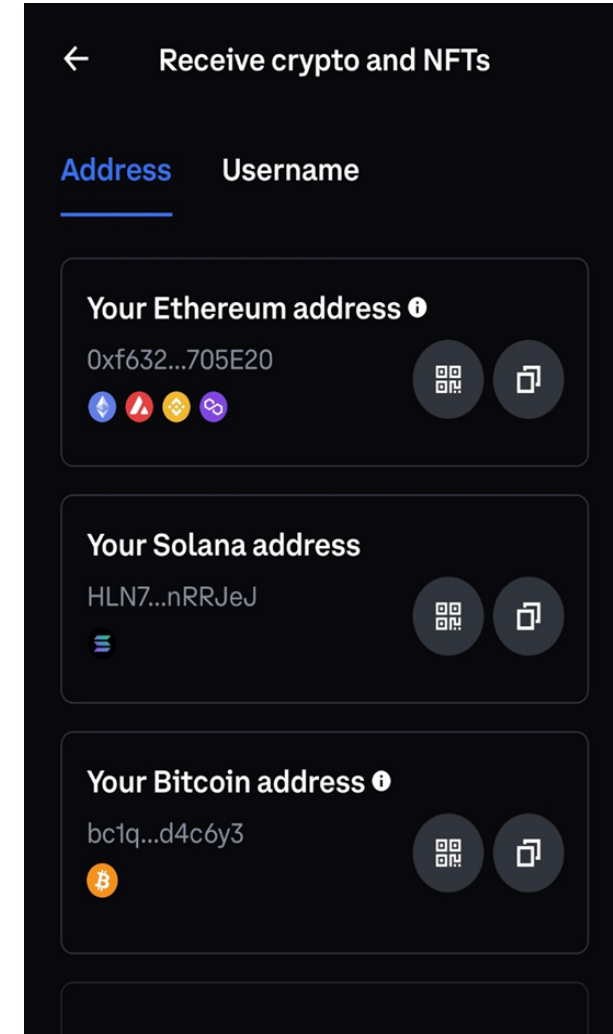
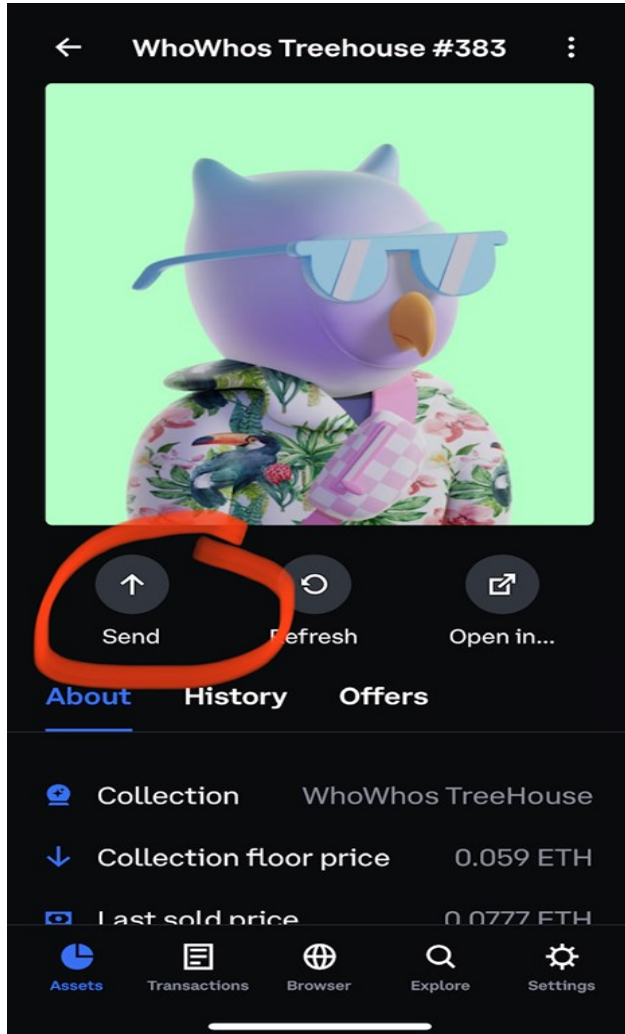
The ownership of the song will be split 50/50 and Illa will help you promote and market your NFT.



# Explore your NFT



# Send or Move your NFT – Hot Storage AHHH





# What is the Metaverse?



## DEFINING FEATURES OF METAVERSE

- **Boundless**
- **Persistent**
- **Immersive**
- **Decentralized**
- **Economic System**
- **Social Experience**

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# Challenges to Fiduciary Access to Digital Assets, In General

## PASSWORDS AND ENCRYPTION

- Federal and state privacy, computer fraud and data protection laws
- Terms of Service Agreements (“TOSA”)/privacy policies governing accounts



Source: <https://www.abposters.com/goldfish-jumping-out-of-the-water-f5767405>



# Computer Fraud and Abuse Acts Prohibit Hacking

- Each state , as well as Congress, has enacted a Computer Fraud and Abuse Act (“CFAA”) that criminalizes (or at least, creates civil liability for) the **unauthorized access** of computer hardware and devices, and the data stored thereon.
- If the cryptocurrency or NFT owner expressly authorized the fiduciary to access her computers, it is unlikely that such computer access violates the CFAA.
- Revised Uniform Fiduciary Access to Digital Assets Act (“UFADAA”) makes that clear.

# What about Password Sharing?

- The easiest way to provide for access to online accounts, and the digital assets held in them, during incapacity or after death is simply to share a password with a trusted friend or family member, which violates most TOSA's.



Source: <https://gizmodo.com/5870226/when-to-give-your-girlfriend-your-password>

# Password Sharing as TOSA and CFAA Violations

- Even if the fiduciary has the user's permission or passwords, the fiduciary may still be breaking the law. Access to a user's online account requires accessing the provider's or another vendor's computer, which requires *the service provider's* further authorization.
- If the provider's TOSA prohibits third parties from accessing the account, as many TOSAs do, when the fiduciary uses a shared password to access the account, he violates the TOSA and thereby exceeds his authorized access *to the service provider's system*. Technically, this violates the CFAA.
- Password sharing among family members and access by individual fiduciaries has not yet been and most likely will not be prosecuted as a CFAA violation.
- However, the CFAA and the cases interpreting it are neither consistent nor clear.
- *A password manager is a good workaround.*

# Revised UFADAA (2015)

- **Facilitates fiduciary access to virtual currency, but cannot guarantee it in all cases.**
  - Takes into account privacy and contractual rights of account holders and compliance with federal and state privacy laws
- Revised UFADAA's limited default authority over electronic communications content will penalize those who fail to plan for third-party access to their online accounts and digital assets. Likewise, advisors who fail to discuss digital assets and access with their clients will be hard-pressed to explain that oversight.
- Sections 15(d) and (e) confirm that a fiduciary is an authorized user of the decedent, protected person, principal or settlor's property under applicable CFAA's and confirms that a fiduciary with authority over devices can access digital assets and files on it and is an authorized user. This clearly authorizes fiduciaries to access private keys stored on electronic devices.

# Cryptocurrency Is a “Digital Asset” under Revised UFADAA

- “Digital assets” are defined as electronic records in which an individual has a right or interest. The term does not include an underlying asset or liability unless the asset or liability is itself an electronic record. Revised UFADAA § 2.
- This is intended to give the fiduciary authority to access cryptocurrency if access is otherwise technologically feasible.

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# Pre- Death Advising Clients & Drafting Considerations

- **Digital Asset Checklist**
  - Consider a “Digital Executor”
- **Social Media Checklist**
- **Client Questionnaire**
  - Include specific reference to digital assets
- **Education of Client and Client’s Family**
- **Drafting Considerations**
  - Directed trusts
  - Authority to retain
  - Access provisions

# Pre- Death- Digital Asset Checklist

## Personal Devices (mobile devices, computer, include both personal and work equipment)

| Device Description | Username | Password |
|--------------------|----------|----------|
|--------------------|----------|----------|

## Password Manager

| Service Provider | Email Address/Username | Password |
|------------------|------------------------|----------|
|------------------|------------------------|----------|

## Email

| Service | Email Address | Password |
|---------|---------------|----------|
|---------|---------------|----------|

## Financials (all financial accounts, banking, investment, credit, budgeting services e.g. mint, tax preparation, life insurance, retirement benefits)

| Service | Email Address | Password |
|---------|---------------|----------|
|---------|---------------|----------|

# Pre- Death- Digital Asset Checklist

| Utilities and Property Services |                |                |          |
|---------------------------------|----------------|----------------|----------|
| Company                         | Account number | Username/Email | Password |

| Cloud based services (iCloud, Google Drive, Dropbox) |                        |          |
|--|------------------------|----------|
| Service Provider                                     | Email Address/Username | Password |

| Online Shopping and Subscription Services (Amazon, Netflix, Blue Apron) |               |          |
|---|---------------|----------|
| Service   | Email Address | Password |

| Security Systems (codes, vacation homes, businesses) |                      |                  |          |
|--|----------------------|------------------|----------|
| Property Address                                     | Property Description | Security Company | Password |

# Pre- Death- Digital Asset Checklist

| Intellectual Property and Specialty Digital Assets (patent, trademarks, videos, photos) |                  |          |             |
|---|------------------|----------|-------------|
| Issue/Creation Date   | Reference Number | Location | Description |

| Websites, blogs, domain names |                        |          |
|-------------------------------|------------------------|----------|
| Registrar/Host                | Email Address/Username | Password |

| Metaverse Accounts and Applications (VR applications, Venmo, Paypal, etc.) |               |          |
|--|---------------|----------|
| Service  | Email Address | Password |

# Pre-Death Advising and Drafting- Intellectual Property

- The most important Estate Planning Technique for IP Assets is to find out that they exist.
  - Don't assume your client will identify or properly identify his or her IP
  - Intangible assets are often harder to identify than tangible assets
- **Question your client about it!**
- Follow two principal strategies:
  - Look for relevant **documentation** and the tangible embodiments of IP (where such exist)
  - Consider **activities**, such as the business, profession, and hobbies of your client (or of the decedent and debtor)
  - Refer to the IP directly in the Will or Trust

# Checklist– Social Media

- Facebook
- Twitter
- Instagram
- Tik-Tok
- Apple ID
- Google/Gmail
- Meta





# Checklist– Facebook

- **Facebook**

- Have you established a legacy contact?

- Twitter
- Instagram
- Tik-Tok
- Apple ID
- Google/Gmail
- Meta

- Can designate legacy contact
- Will create a memorialized page in the event Facebook learns of passing
- Legacy contact can delete account, add friends, pin a tribute post

# Checklist - Twitter

- Facebook
  - **Twitter**
    - Is the person an influencer
  - Instagram
  - Tik-Tok
  - Apple ID
  - Google/Gmail
  - Meta
- Unable to provide account access to anyone regardless of their relationship to the deceased
  - Can request deactivation with proper documents

# Checklist –Tik-Tok

- Facebook
  - Twitter
  - Instagram
  - **Tik-Tok**
    - Likely lost
  - Apple ID
  - Google/Gmail
  - Meta
- Username associated with an inactive account to reset to a randomized numeric username after 180 days.
  - The username may also be reset if the app receives “a valid request, such as a trademark infringement notice.

# Checklist - Apple

- Facebook
- Twitter
- Instagram
- Tik-Tok
- **Apple ID**
  - Legacy Contact
- Google/Gmail
- Meta

- According to Apple's support guidelines, the proper action is to request access to a decedent's Apple ID and the data stored with it or request Apple to delete the account.
- Apple requires and verifies legal documentation before assisting with a deceased person's account.
- Such document generally includes a death certificate "and may also require a court order or other documentation."

# Checklist – Google/Gmail

- Facebook
- Twitter
- Instagram
- Tik-Tok
- Apple ID
- **Google/Gmail**
- Meta

- Google allows a user to “share parts of their account data or notify someone if they've been inactive for a certain period of time.”
- The account holder can specify a “trusted contact” who will receive any data the account holder selected to share after the account becomes "inactive.”
- Google will examine several factors to determine whether an account is "inactive" such as sign-ins, usage of Gmail, and Android check-ins

# Cryptocurrency and NFTs – Checklist

- **Does your client regularly use blockchain technology to store assets?**
- How do you store your wallet – hot, medium, cold?
- If cold, where?
- If cold, diversification?
- How frequently do you want access to asset?
- What is your risk tolerance?
- What is your investment strategy?



# Advising Clients & Drafting Considerations (continued)

- **Drafting Considerations**

- Sample language (provided by Austin Bramwell & Milbank, Tweed, Hadley & McCloy LLP)
  - To make sure that cryptocurrency/blockchain wallets are not included in a bequest of tangible personal property (here, via a revocable trust):
    - All furniture, furnishings, rugs, pictures, books, silver, plate, linen, china, glassware, objects of art, wearing apparel, jewelry, automobiles, boats and their accessories, and all other tangible personal property (excluding cash, bullion, *cryptocurrency wallets of any kind, including any cryptocurrency paper wallets, hardware wallets, desktop wallets, or mobile telephone wallets*, and any tangible personal property used primarily in any trade or business at the Grantor's death) which is held as part of the trust estate (whether directly or indirectly through an entity in which the trust estate has an interest), together with any insurance policies covering the same (the "Grantor's tangible personal property"), shall be transferred, conveyed and paid over to \_\_\_\_\_.

# Advising Clients & Drafting Considerations (continued)

- **Drafting Considerations**

- Sample language (provided by Austin Bramwell & Milbank, Tweed, Hadley & McCloy LLP)

➤ In the powers provisions, add cryptocurrency powers to the digital assets provision:

- In addition to, and not by way of limitation of, the powers conferred by law upon fiduciaries, the Trustee is expressly granted with respect to each of the trust estates herein created, including any accumulated income thereof, the powers hereinafter enumerated, all of such powers so conferred or granted to be exercised by the Trustee as the Trustee may deem advisable in the exercise of sole and absolute discretion . . .
- To access, handle, distribute and dispose of digital assets; to access, use and take control of digital devices, including but not limited to desktops, laptops, tablets, peripherals, storage devices, mobile telephones, smart phones, *cryptocurrency wallets of any kind, including cryptocurrency paper wallets, hardware wallets, desktop wallets, or mobile telephone wallets*, and any similar digital device; to access, modify, delete, control, copy, transfer and otherwise deal with digital assets, including but not limited to e-mails, documents, images, audio, video, software licenses, domain registrations, *cryptocurrency private keys*, and similar digital files, regardless of the ownership of the physical device upon which the digital asset is stored; to access, modify, delete, control, copy, transfer and otherwise deal with digital accounts, including but not limited to e-mail accounts, social network accounts, social media accounts, file sharing accounts, financial management accounts, *cryptocurrency exchange accounts*, domain registration accounts, domain name service accounts, web hosting accounts, tax preparation service accounts, online stores, affiliate programs, and other online accounts.

# Agenda

- I. Introduction**
- II. Types of Digital Assets
- III. Barriers to accessing Digital Assets
- IV. Pre- Death Advising Clients & Drafting Considerations
- V. Post-Death Advising Clients & Drafting Considerations**
- VI. Taxation & Reporting
- VII. Takeaways
- VIII. Q&A

# Post- Death Advising Clients & Drafting Considerations

- **Digital Asset Checklist**
  - Consider a “Digital Executor”
- **Social Media Checklist**
- **Client Questionnaire**
  - Include specific reference to digital assets
- **Education of Client and Client’s Family**
- **Drafting Considerations**
  - Marshalling assets and security

# Risk Assessment – UPIA

- (1) Prudent Investor Rule. A trustee shall invest and manage trust assets as a prudent investor would; that is, by considering the purposes, terms, distribution requirements, and other circumstances of the trust. In satisfying this standard, the trustee shall exercise reasonable care, skill, and caution.
- (2) Management. Under the UPIA, “management” includes the duty to monitor the trust investments.
- (3) Duty to Diversify. “A trustee shall diversify the investments of the trust unless the trustee reasonably determines that, because of special circumstances, the purposes of the trust are better served without diversifying.”

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# Cryptocurrency and Tax

## General Principles

- Cryptocurrency is a novel form of property
- Blockchain technology creates a novel way of transacting
- But that doesn't mean new law is required

## Practitioners Need:

- Familiarity with common issues
- Ability to spot planning opportunities and advise on implementation

## Topic Is as Vast as Tax Law Itself

- Tax consequences to issuers of initial coin offerings
- Outbound anti-deferral rules
- Cryptocurrency traders

# Notices 2014-21 and 2019-24

- **Cryptocurrency Is Property**
  - Not currency
  - No *de minimis* exception
- **Receipt of Cryptocurrency for Goods or Services Is Gross Income**
  - Basis = FMV on date of receipt
  - Cryptocurrency received from mining is gross income on date of receipt
- **Exchange of Cryptocurrency for Cash or Other Property Causes Gain or Loss**
  - Gain or loss may be capital if cryptocurrency was a capital asset
- **Hard Forks and Air Drops**
  - What are they?
  - Is there “an accession to wealth” leading to I.R.C. §61 gross income

# 2019 Letters

- **Letter 6173, Letter 6174, or Letter 6174 -A**
  - Approximately 10,000 total letters sent
  - July 2019 through August 2019
  - “Taxpayers should take these letters very seriously by reviewing their tax filings and when appropriate, amend past returns and pay back taxes, interest and penalties”<sup>1</sup>- Chuck Rettig
- **What is the Taxpayer’s responsibility?**
- **Virtual Currency Compliance Campaign<sup>2</sup>**
  - July 2018 — Announced by IRS Large Business and International division (LB&I)
  - Withholding and International Individual Compliance.

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1. <https://www.irs.gov/newsroom/irs-has-begun-sending-letters-to-virtual-currency-owners-advising-them-to-pay-back-taxes-file-amended-returns-part-of-agencys-larger-efforts> (last visited May 21, 2020).

2. <https://www.irs.gov/businesses/irs-lbi-compliance-campaigns-july-2-2018> (last visited May 21, 2020).

# Valuing Cryptocurrency for Tax Purposes

- **When FMV of Cryptocurrency Needed**

1. Receipt of cryptocurrency in exchange for goods or services
2. Determination of amount realized if cryptocurrency received in a sale or exchange of other property
3. Reportable transfer for gift or estate tax purposes
4. Determination of basis of cryptocurrency acquired from a decedent (and sometimes by gift)
5. Charitable gift of cryptocurrency

- **How to Determine FMV**

1. Notice 2014-21 - FMV is based on exchange rates
2. Conversion into dollars at exchange rates must be made in a “reasonable manner” and “consistently applied”
3. Which exchanges’ prices may be used?
4. May indexes be used?
5. Is average high/low of daily prices “reasonable”?
6. Different methods for different cryptocurrencies?
7. Publicly traded securities exception to requirement of appraisal for charitable deduction substantiation purposes?

- **What Is the Property Acquired from a Decedent at Death?**

# Tracking Basis

- **Challenges in Tracking Basis**

1. The same cryptocurrency may be acquired at different times and at different prices
2. Similar to corporate stock acquired at different times and at different prices
3. Tracking different lots is possible in principle, but difficult in practice

- **Basis Tracking Methods**

1. Treas. Reg. § 1.1012-1(c) provides that first-in-first-out (FIFO) is the default for stock
2. May a taxpayer adopt a similar, consistently applied convention?

# Losses

- **Losses from Sale or Exchange**
  1. Notice 2014-21 confirms that a loss may be realized upon sale or exchange of cryptocurrency
  2. Loss is ordinary or capital depending on whether cryptocurrency was a capital asset
  3. Could loss ever be a non-deductible personal loss?
  4. Wash sale losses Theft Losses
- **Theft Losses**
- **What if Private Key Goes Missing or Becomes Inaccessible?**
  1. Casualty loss deduction?
  2. Non-casualty loss deduction?

# Is Cryptocurrency Tangible?

- **If I Can't Fathom It Conceptually, It's not Tangible (Right?)**
- **Distributed Ledger Is Intangible**
- **What Is It that a Cryptocurrency Investor Owns?**
  1. The FBI "seized" \$18 Million of cryptocurrency possessed by Ross Ulbright
  2. Cryptocurrency owners must be careful not to "lose" their private keys
  3. The safest way to own cryptocurrency is in "cold storage"
- **What Is the Legal Relationship of Coinbase and Its Customers?**
- **Implicit IRS Position on Tangibility**
  1. Notice 2014-21 - Miners' realize gross income as cryptocurrency is received
  2. IRC § 263A - Uniform capitalization rules
- **Does It Matter?**
  1. Situs of cryptocurrency for U.S. gift and estate tax purposes
  2. Charitable gifts of cryptocurrency
  3. Intervening use rule for charitable remainder trusts
  4. Non-depreciable tangible property GRITs
  5. State source income rules
  6. State sales taxes



# Gift Completion Issues

## WAYS TO MAKE A GIFT OF CRYPTOCURRENCY

1. Physical delivery of a wallet
2. Initiation of a transaction on blockchain
3. Transfer to a Coinbase account or other cryptocurrency exchange account

## PHYSICALLY DELIVERING A WALLET: IS THE GIFT COMPLETE?

1. Mere possibility that the donor could retain a copy of the private key
2. What if the donor does retain a copy?
  - Incomplete gift?
  - Transfer with retained interest?
  - Gift subject to a valuation discount?
  - Open transaction?

# Takeaways

- **Communicate**
  - Advisors should ask clients whether they own financial and personal digital assets
  - Clients should notify executor/trustee of the existence of financial and personal digital assets and how to access.
- **Educate**
  - Advisors should educate clients and their officeholders (e.g., executors, trustees) on how to identify/locate digital assets
- **Keep Detailed Records**
  - Date of acquisition
  - Track basis
  - Inventory of all holdings
  - How to access
- **Security & Custody – Cold vs. Hot Storage**