

## **Cryptocurrency & Estate Planning**

by Monique M. Nevarez, Esq.



Cryptocurrency or virtual currency (used interchangeably) has become quite the coveted asset among investors because of the seemingly lucrative return due to its fast-appreciating nature. Cryptocurrency has also been the subject of growing interest by government regulators, including the Internal Revenue Service (“IRS”).

But what is virtual currency? How is it treated for tax purposes? And how is it transferred at death?

### **What Is It?**

A cryptocurrency is an electronic payment system that is based on cryptographic proof, permitting parties to exchange the cryptocurrency with each other using blockchain technology. A blockchain is a decentralized ledger of all transactions in a network. The blockchain technology permits participants in the network to confirm transactions without the need for a trusted third-party intermediary (such as a bank, for example).

The IRS defined “virtual currency” in FAQs as “a digital representation of value, other than a representation of the U.S. dollar or a foreign currency, that functions as a unit of account, a store of value, and a medium of exchange.” The term “cryptocurrency” is a subcategory of virtual currency in which encryption techniques are used to regulate the various generation of units of currency and verify the transfer of funds.

Regardless of the label applied, if a particular asset has the characteristics of virtual currency, it will be treated as virtual currency for tax purposes.



## Is Cryptocurrency Taxable?

The short answer is, yes.

There has been very limited guidance from the IRS regarding cryptocurrency. However, so far, the IRS released IRS Notice 2014-21, which was released in early 2014, and in 2019 it released further guidance with Revenue Ruling 2019-24. The IRS also published its position on virtual currency via its FAQs on the IRS.gov website. It is important to note, however, that FAQs are treated only as "communication" and are not binding on the IRS or the taxpayer.

Cryptocurrency is treated as property for federal income tax purposes. General tax principals applicable to property transaction apply to transactions using virtual currency. This means that capital gains and losses apply to the virtual currency.

IRS guidance provides that cryptocurrency is not currency because it is not designated as legal tender by any jurisdiction. Virtual currencies which can be exchanged for real currency, are considered "convertible virtual currency", but they are still governed as a property transaction.

Virtual currency received as payment for services constitutes wages for employees and self-employment income for independent contractors and is subject to applicable withholding and information reporting requirements.

A taxpayer who receives currency as payment for goods or services must include in its gross income the fair market value of the virtual currency measured in U.S. dollars, as of the date that virtual currency was received. Furthermore, the basis of virtual currency a taxpayer received as payment for goods or services is the fair market value of the virtual currency in U.S. dollars as of the date of the receipt.

If a taxpayer receives virtual currency as a bona fide gift, the taxpayer will not recognize income until the taxpayer sells, exchanges, or otherwise disposes of that virtual currency.

Taxpayers engaged in any transaction involving virtual currency must file Schedule 1 (Form 1040 or Form 1040-SR). Additionally, depending on the transaction, the taxpayer may need to file supplemental forms.



## Cryptocurrency & Estate Planning

Virtual currency is generally accessed through a private key (like a cryptic password) and stored in a "digital wallet." Because there is generally no document that proves ownership, essentially, whoever has the key, can control the cryptocurrency. This can make the cryptocurrency susceptible to theft or loss. This also makes estate planning with virtual currency tricky.

Take Bitcoin for example; a Bitcoin wallet has a public address and a private key. There is no social security number, deed, or ownership account of any kind tied to the wallet. Whoever has the private key owns the Bitcoin. Because there is no ownership title, it is not something you can transfer into a trust.

The challenge to passing on your cryptocurrency to your heirs is providing enough information and detail to identify the accounts/wallets at your passing, but not so much information so that it remains secure while you are alive and at the transfer at your death.

The solution may be storing the information in a safe-deposit box or providing the successor trustee with instructions. Either way, you want to be sure that it is accounted for in your estate plan and that your heirs know what to do when passed on to them.

At Law & Stein, we have experience working with clients to secure their cryptocurrency accounts with a "tech access plan", to protect and securely access your digital wealth for your future beneficiaries.



## **We look forward to serving you & wish you the best**

We are here to provide you with legal guidance you can trust while placing safety and health as a priority. We are happy to meet in person or to accommodate other needs, including Facetime, SKYPE and ZOOM for virtual, face-to-face connections. Contact us directly to speak with someone who can help answer your questions. T (949) 501-4800 Or send us a private email at the link below and we will respond promptly.

[info@lawandsteinllp.com](mailto:info@lawandsteinllp.com)

Visit our website for more information and to review our partner and attorney bios: [www.LawandSteinllp.com](http://www.LawandSteinllp.com)

The Law & Stein Newsletter is a monthly publication to share useful information with our clients in matters of estate planning, tax planning, inheritance dispute litigation, elder abuse, probate and business litigation, and premises and product liability defense.

LAW & STEIN LLP  
2601 Main Street, Suite 1200  
Irvine, CA 92614  
[info@lawandsteinllp.com](mailto:info@lawandsteinllp.com)

