



AMERICAN BAR ASSOCIATION

Tax Section

HYBRID 2022

# MAY TAX MEETING

MARRIOTT MARQUIS • WASHINGTON, DC

## **Cradle to Crypt(o): Tax Exempts and the Life Cycle of a Cryptocurrency Donation**

**Exempt Organizations**

**May 13, 2022**

**taxnotes**<sup>®</sup>  
*Exclusive Diamond Sponsor*

# The Panel

- Eleanor Moran McWaters, Crowell & Moring LLP
- Andrea S. Kramer, McDermott Will & Emery LLP
- Alexander L. Reid, Baker Hostetler
- Duke Kim, The Giving Block

# Objectives

- Learn the fundamental aspects of blockchain and cryptocurrency (what it is, why it has all become so popular, how it works)
- Identify the key tax considerations associated with the donation of crypto to nonprofits
- Explore the tax and legal issues that arise when a nonprofit holds onto and then disposes of crypto

# Agenda

- Cryptocurrency level set
- Donations of crypto generally
- How to accept crypto donations
- How to hold crypto, following donation
- How to report and dispose of crypto, following donation

# Cryptocurrency Generally

- A medium of exchange, a store of value, a utility (prepaid subscription), a security (debt or equity), an asset (commodity) pegged to fiat currency (stable coins), a tokenization of assets (securities or real estate), or combination of the above
- Peer to peer, decentralized, digital asset without legal tender status as fiat currency in any jurisdiction (except for bitcoin in El Salvador)
- Parties transact directly without an intermediary using blockchain technology, a shared distributed ledger that verifies, records, and settles transactions on a secure, encrypted network
- Intangible asset without a physical location

# NFTs Generally

- Each NFT is a unique digitized certificate (referred to as a token) that is a digital unit of data stored on a blockchain
- It can be a representation of something (a work of art, a photograph, a piece of music, a game or a collectible), or it can be an original creation that exists only in digital form
- NFTs are typically purchased and sold using the type of cryptocurrency or digital token used or accepted on that particular blockchain
- Once an NFT is created and stored on a blockchain, all of its subsequent sales are tracked and recorded

# State of Crypto Today

- Sixteen percent of Americans own crypto
- Americans are donating crypto
  - Tax-exempt entities are accepting more and more crypto
  - Approximately \$450MM in crypto given in 2021
  - In 2020, 45 percent of crypto investors donated \$1K+ as compared to 33 percent of the general investor population
  - Select entities are no longer accepting crypto for environmental reasons
- Americans are deducting crypto donations
  - Cryptocurrency is now part of Form 1040
  - Cryptocurrency is generally treated as property
  - Donor may avoid capital gains and receive charitable deduction
  - Donations are more problematic for NFTs

# IRS FAQs

- Q 34: Donation of convertible virtual currency (noncash donation) is not a sale of a capital asset
- Q 35: Calculating the charitable deduction:
  - If held LTCG holding period: deduction is FMV of virtual currency at time of donation
  - If not held for LTCG holding period: deduction is limited to lesser of tax basis or FMV
  - Ordinary asset: deduction limited to FMV of property minus any appreciation (basically tax basis)
  - If loss, deduction is limited to FMV



# Donor Deduction – General Income Tax Treatment

- Most property held for personal or investment purposes is a capital asset. Code § 1221(a).
- The contribution of a capital asset held by a donor for more than 12 months to a public charity is generally deductible at the FMV of the asset up to 30 percent of the donor's adjusted gross income. Code § 170(b)(1)(C).
- When a donor contributes ordinary income property (rather than a capital asset), the deduction is generally limited to the basis in the property, rather than the FMV, but is deductible up to 50 percent of the donor's adjusted gross income. Code §§ 170(b)(1)(A), 170(e)(1)(A).

# Donor Tax Considerations

- Convertible virtual currency is property
- Not foreign currency
- Apply general tax rules that apply to noncash property
- Recordkeeping and documentation gets more detailed as donation increases in value
- Donations of more than \$5,000 require Form 8283, Section B, and Qualified Appraiser (recognized appraiser with at least two years of experience in type of property appraised)
- Must determine FMV for donation
- Identification considerations

# Using NFTs for Charitable Fundraising

- Some organizations can accept NFTs as part of mission (art NFTs donated to an art museum)
- Can face insurmountable hurdles with direct donations
  - How to determine FMV? Qualified appraisal?
  - No IRS guidance for NFTs
- Often NFTs are sold in an NFT marketplace for crypto with proceeds going to organization. If proceeds are in crypto, same issues apply to crypto and NFTs
- How can they be valued given unique nature of NFTs?

# Methods of Making Crypto Donation

- Use of Donor Advised Fund
  - Organization may direct donors to DAFs like Fidelity Charitable or Vanguard Charitable, which accept cryptocurrency
- Use of Processor
  - The Giving Block specializes in enabling nonprofits to accept crypto donations
  - Alternatively, organizations may use a general payment processor, not specializing in non-profit organizations
- Use Embeddable Checkout Experience
  - Crypto exchanges have checkout experiences that offer an automatic conversion to cash
  - This may be embedded into organization's fundraising platform
- Accept Crypto Directly with Crypto Wallet
  - No intermediary
  - Requires technical expertise

# Use of DAF

- Donors can contribute crypto to a DAF and the third-party DAF platform converts the crypto to U.S. dollars or another fiat currency
- The nonprofit does not need to set up a virtual currency wallet and does not assume risks and expenses of converting to fiat currency
- Might allow the nonprofit to insulate itself from undesirable donors that could hurt its mission or pose a reputational risk

# Use of Processor

- Purpose-built platforms such as The Giving Block work with hundreds of nonprofit clients and are well-versed in crypto, operations, and marketing:
  - Abstracts operational friction and enables client to focus on fundraising and impact
  - Exposes nonprofit to new donor community
- Other processors such as Bitpay or Coinbase Commerce are suitable for passive donation receipt but do not actively work with nonprofit clients to maximize campaign outcomes

# DIY Approach

- Accepting
  - Conversion to USD/Fiat
  - Gift Acknowledgment
  - Gift Acceptance Policy
  - Anonymous Donors
  - Form 8283
- Holding and Disposing
  - Holding Crypto Concerns
  - Form 8282
  - Annual Reporting Requirements

# Gift Acceptance Policy

- Necessary for nonprofits accepting crypto directly
- Include policies regarding which crypto to accept, liquidation, valuation, reporting, etc.
- Rules regarding pre-arranged sales
- Determine if anonymous donations will be accepted
- Procedure to protect the nonprofit from security breaches (such as hacks)
- Consider engaging blockchain analytic firm to analyze transactions to determine if money laundering, sanctioned country, terrorist financing, or reputational risk
- Back-up cash donation



# Anonymity and Donations

- Blockchain enables anonymity
  - Blockchain is public and includes the public addresses of each party to a transfer
  - However, blockchain does not contain information about the individual or ultimate donor
- Rise of anonymous giving
  - Generally, using DAFs, using crypto, etc.
  - Concern regarding donors and donee organizations
  - Most gifts are received by “mainstream” organizations
- Nonprofit’s responsibility?
  - Schedule B
  - *Americans for Prosperity Foundation v. Bonta*

# Form 8283, Noncash Charitable Contributions

- Form is required if the donor is claiming a deduction of more than \$500
- Form is the responsibility of the donor
- Nonprofit is to sign for large donations (\$5K+)
  - Additional appraisal requirements apply to large donations
  - There may be an issue of finding a qualified appraiser
  - Signature of the donee does not represent concurrence in the appraised value of the contributed property

# Holding Crypto

- Donors may request the nonprofit holds crypto, in anticipation of price appreciation
- Price volatility / alignment with existing investment policy
- Custody: hot vs cold storage
- Liquidation and withdrawal of USD proceeds

# Form 8282, Donee Information Return

- Nonprofits must file Form 8282 if they sell, exchange or otherwise dispose of charitable deduction property within 3 years of receipt
  - This requirement only applies to *deduction* property (if the donor does not take the deduction, no requirement applies)
  - Form is required for property reported on Form 8283
  - This includes cryptocurrency.
  - See IRS FAQ (“such as the sale of virtual currency for real currency”)
- Nonprofits to provide a copy of Form 8282 to donor
  - Purpose of Form 8282?

# Annual Reporting Requirements

- Form 990
  - Nonprofits report non-cash contributions on Form 990 and its associated Schedule M, if applicable
- Schedule B
  - May raise issue of donor anonymity
  - What duty does the nonprofit have to identify donors?
  - Will too many anonymous donors be a red flag?
  - Could Schedule B be cross-referenced with Form 1040 (which now asks about crypto)? What happens if a donor donates crypto, but does not acknowledge owning crypto?

# Questions?

# Contact Info

- Eleanor McWaters – [emcwaters@crowell.com](mailto:emcwaters@crowell.com)
- Andrea S. Kramer – [akramer@mwe.com](mailto:akramer@mwe.com)
- Alex Reid – [areid@bakerlaw.com](mailto:areid@bakerlaw.com)
- Duke Kim – [duke@thegivingblock.com](mailto:duke@thegivingblock.com)

## For more information

- <https://www.mwe.com/insights/what-you-need-to-know-about-tax-cryptocurrency/>
- <https://www.mwe.com/insights/what-you-need-to-know-about-the-taxation-of-nfts/>
- <https://www.jdsupra.com/legalnews/special-report-a-primer-on-charitable-8477657/?msclkid=1d80ca8dc41511ecab8608071718d8d2>
- <https://www.mwe.com/insights/nfts-and-charitable-fundraising-navigating-tax-hurdles/>