

Charitable gifts of crypto: Old rules to new assets

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Considerations for both the donor and the charitable organization

What is the type of asset being transferred?

Digital assets are generally deemed by U.S. tax authorities to be “property.”¹ There are many types of digital assets that take different forms of “property” per the tax rules. There are even digital assets which are treated as legal tender in some countries (e.g., El Salvador as of date of this publication). Others, such as non-fungible tokens (NFTs), may be best described as a bundle of property rights. The charity’s planned use of the gifted property can have significant tax consequences to the donor. In general, when a donor gifts to charity property that would have generated longterm capital gains if it had instead been sold, the deduction is based on the property’s fair market value. Similarly, if the property is considered tangible personal property and the donee’s use is *related* to its tax-exempt purpose, the donor’s tax deduction is based on the property’s fair market value.² However, if that property is considered tangible personal property and the donee’s use is *unrelated* to its tax-exempt purpose, the donor’s tax deduction is generally limited to its basis in the property³.

Consider a donor who purchases an NFT: a warehouse receipt for an object of art and holds it as a collection piece. Although an NFT is generally not considered tangible personal property, in this case it could be considered a collection of property rights which allows the holder to go to a physical location and collect a physical piece of art. Assuming the gifted asset is deemed to be tangible personal property, the amount of the tax deduction would differ depending on the use of the property by the donee organization. If the donation were made to a public charity that is a museum, where the primary charitable purpose is the owning, curating, and public display of culturally significant art, the donor would be eligible for a tax deduction of the fair market value of the property because the donee’s use is related to its exempt purpose.

However, if the donor gifted the same asset to a donor advised fund, the asset would not be considered related to the donee’s exempt purpose, and the donor’s deduction would generally be limited to basis in the asset.⁴ As NFTs vary a great deal in their design and legal construct, this determination would likely require a legal review of the NFT and the property rights it represents to determine the amount of the donor’s tax deduction.

The IRS in Notice 2014-21 provided guidance that digital assets are treated as property under the federal tax rules. This likely applies to many NFTs. As such, so long as selling the property would generate longterm capital gains for the donor (capital gain property), the contribution base/AGI limitation for a donation to a public charity should be 30% for an individual donor, and the amount of the deduction would be equal to the fair market value as determined by a qualified appraisal.

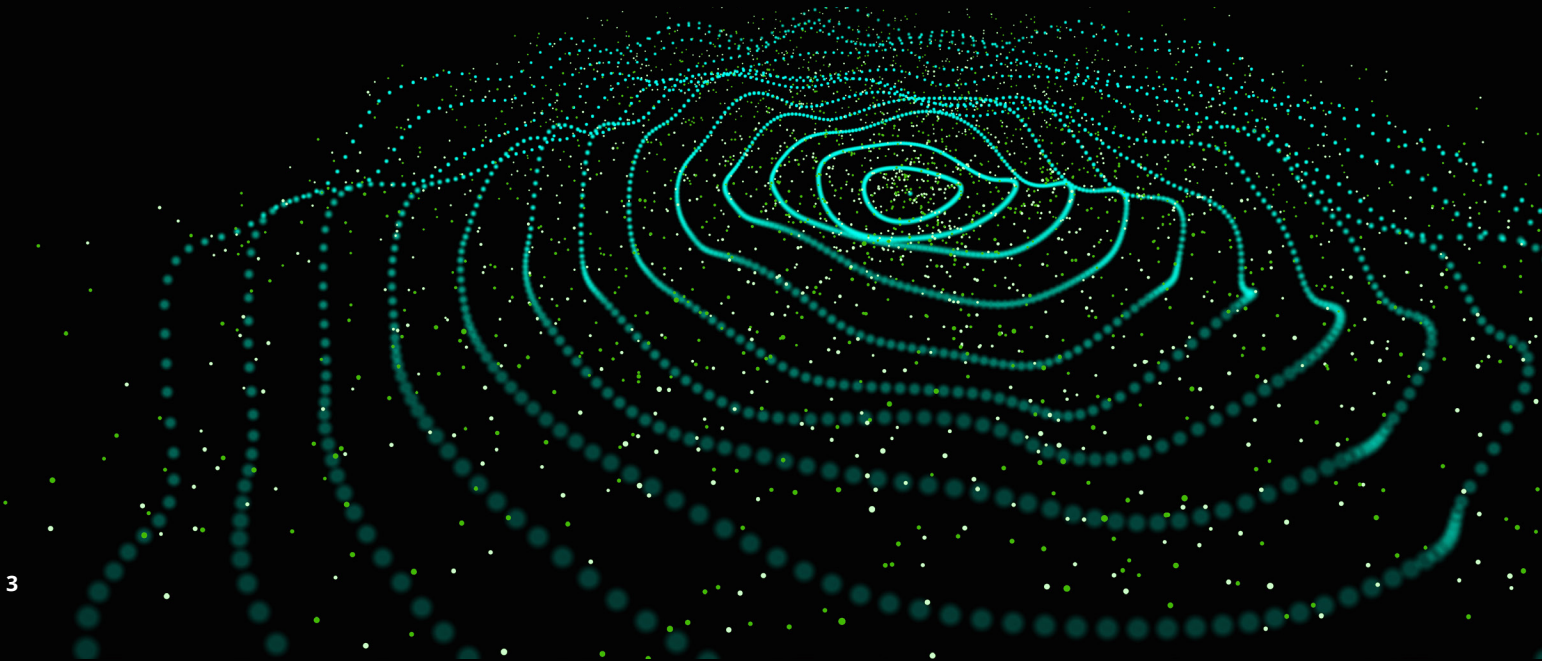
Understanding whether the digital assets donated are “capital gain property” is critical to the donor, as the amount of charitable deduction for donated assets that are not capital gain property is limited to the donor’s basis. For example, an NFT providing art property rights would not be capital gain property to the artist who created the art. The charitable deduction for the donation of that NFT by the artist after creation would be limited to basis.

Is the asset being transferred a donation of a partial interest?

Similar to the first question, it is also important to understand whether the donation represents the donor's entire interest in the property. Subject to some exceptions, the tax rules do not allow charitable deductions for donations of partial interests in property. Accordingly, if a donor contributes the right to use an asset but not the underlying asset, it is a nondeductible contribution of a partial interest. Taxpayers should be aware that certain types of digital assets may provide a donor a retained interest that could be considered a partial interest in property.⁵ This is especially true with self-created digital art, to which the artist may have attached an NFT. The donor artist could reduce this concern by transferring both the digital art and the underlying copyright to a museum. This would be a contribution of the donor's entire interest in the property. Similarly, an NFT which represents the rights to a piece of physical art stored in a warehouse which is contributed to an art museum will likely be a deductible contribution so long as the NFT represents all of the donor's rights in the art.

What is the value of the asset being transferred?

The fair market value is of importance to both donor and donee. The donor is required to obtain a qualified appraisal for any asset with a value in excess of \$5,000.⁶ A gift in excess of this amount also requires the donor to file Form 8283, *Noncash Charitable Contributions*, signed by the recipient organization and the qualified appraiser for assets other than cash and qualified appreciated stock contributions over the \$5,000 threshold. Form 8283 is filed as part of the donor's Form 1040, *U.S. Individual Income Tax Return*. A recipient organization that sells the digital assets within three years of receipt has an obligation to file Form 8282, *Donee Information Return*, upon the disposition of the donated assets. Form 8282 is filed with the IRS with a copy provided to the donor.



Additional considerations for donors

What type of charitable organization is the recipient charity?

The type of charity to which the donor is contributing assets matters. If the charity is a public charity,⁷ whether the tangible asset is used for the public charity's exempt purpose⁸ will be a critical factor in determining the donor's charitable deduction.

Obtain contemporaneous written acknowledgment from the charity for any contribution over \$250

This acknowledgment must be obtained prior to the earlier of (1) the date the return is filed, or (2) the due date (including extensions) for filing such return.

The contemporaneous written acknowledgement of the charitable gift is often thought to be a concern of the charity, but it is, in fact, a concern of the donor. Even though the recipient charity issues the letter, there is no penalty imposed by the IRS on the charity for not providing this letter unless there is a quid pro quo component that is omitted from the letter. Otherwise, the negative consequences of failing to secure a proper letter are all born by the donor in the form of disallowed charitable contribution deductions. A charity may lose out on future charitable contributions from an unhappy donor. However, there are no penalties assessed on the donee by the IRS for failure to provide a complete and accurate contemporaneous written donor acknowledgment letter for contribution of \$250 or more.

The I.R.C. and underlying Treasury regulations⁹ provide a list of what is required in the contemporaneous written acknowledgment letter:

- 1 Name and address of the donee organization;
- 2 Date of the contribution;
- 3 Description of property contributed (no value required for non-cash donations);
- 4 Statement as to whether or not goods or services were provided by the organization in return for the contribution;
- 5 Description and good faith estimate of the value of goods or services (other than intangible religious benefits), that an organization provided in return for the contribution; and
- 6 If the donee organization provided any intangible religious benefits, a statement to that effect.

It isn't necessary to include either the donor's Social Security number or tax identification number on the acknowledgment. Sometimes, even the most sophisticated and well-intended charities can make mistakes in the creation of these letters for their donors.

Additional considerations for the recipient charity

If the organization determines it will accept digital assets, it should consider:

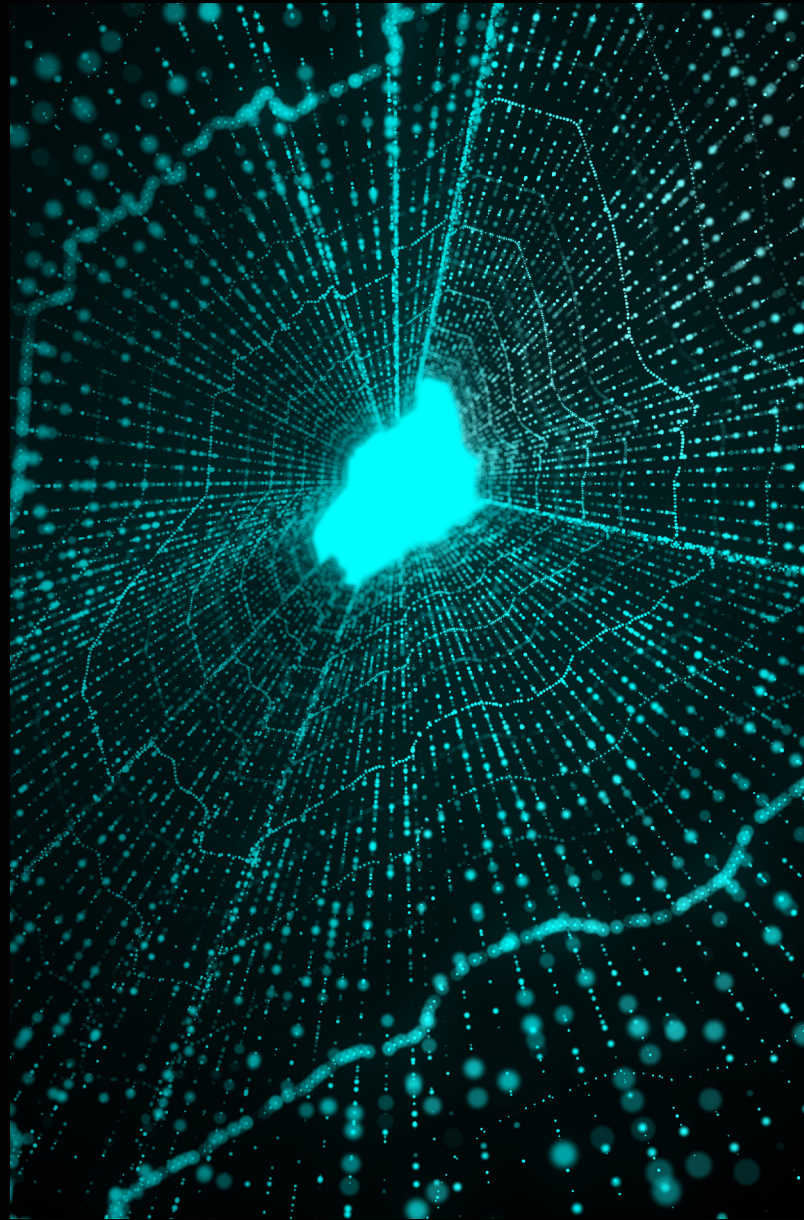
- Whether to set up a wallet to accept digital assets directly or use a digital asset custodian.¹⁰
- Whether it will accept assets anonymously or require disclosure of the donor's identity. If this is not already addressed in the organization's gift acceptance policy, this is something the board may consider exploring with legal counsel.¹¹
- Whether it will immediately convert digital assets to fiat currency (e.g., dollars) or hold them as an asset class in its investment portfolio and the percentage of total assets that represents. If digital assets are added as a category of assets in the organization's investment policy statement, its finance or investment committee may need to update the statement and provide new guidelines to investment management advisors/consultants.
- How best to facilitate the donor's contemporaneous written donor acknowledgment letter in a timely and accurate fashion. Recipient organizations typically send written acknowledgments to donors no later than January 31 of the year following the donation with most issuing them within a day or two of the donation.¹²



Conclusion

Digital assets, and specifically gifts of cryptocurrency, may represent new investment vehicles for both donors and charities. For donors, it may be another opportunity to receive a fair market value deduction for a gift of a highly appreciated asset without recognizing a taxable gain, so long as the asset is considered intangible property or tangible personal property that the charity will use in its tax-exempt purpose. Donors should also consider whether they are retaining any rights in the property, which would make it a donation of a partial interest resulting in a disallowed tax deduction.

For charities and donors, digital assets may represent a new class of asset and diversification. Whatever decisions the parties reach on giving, receiving, and managing the digital asset, they need careful and informed oversight of the process — from idea to execution and beyond.



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Jane Searing has dedicated more than 30 years to serving tax-exempt organizations and their supporters, specializing in private foundations, public charities, and philanthropic tax planning. In collaboration with the Monitor Institute by Deloitte, the Global Center for Excellence in Philanthropy provides a cross-functional focus on philanthropic planning, legacy consulting, and compliance services to individuals, businesses, and tax-exempt organizations.

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Endnotes

¹ See Notice 2014-21.

² Note that the related use rule requires the donee to intend to use the property for three years for the fair market value deduction to be allowed, §170(e)(7). Moreover, the donee organization takes carryover basis from the donor, but records contributions at the fair market value on the date of contribution. All section references are to the Internal Revenue Code (the Code), as amended, or the Treasury regulations promulgated thereunder, unless otherwise indicated.

³ §170(e)(1)(B)(i)(I).

⁴ Donations of property where the fair market value is less than basis will still have a limitation of the deduction equal to fair market value, Reg. §1.170A-1(c).

⁵ Reg. §1.170A-7(b)(1); *Rusoff v. Commissioner*, 65 T.C. 459, *aff'd*, 556 F.2d 559 (2d Cir. 1977).

⁶ Reg. §1.170A-16(d)(1).

⁷ Public charity for this purpose includes donor advised funds, supporting organizations, private operating foundations, and exempt operating foundations.

⁸ §170(b)(1)(B).

⁹ §170(f)(8), §170(f)(17); Reg. §1.170A-13(f)(2), §1.170A-16(a)(1), §1.170A-16(b).

¹⁰ See Peter Smith and Nipun Srivastava, *A Market Overview of Custody of Digital Assets* (2020), available at https://www2.deloitte.com/content/dam/Deloitte/xs/Documents/finance/me_Digital-Custodian-Whitepaper.pdf.

¹¹ For further discussion, see Jane M. Searing and Deby MacLeod, *Cryptocurrency Gift Strategies for Not-for-Profits*, J. of Acc'y (Feb. 1, 2019), available at <https://www.journalofaccountancy.com/issues/2019/feb/cryptocurrency-gift-strategies-for-nfp.html>.

¹² See details in the section "Additional Considerations for Donors," above, for required timing.

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