Every Day is Bitcoin Pizza Day: What Clients and Estate Planners Need to Know about Virtual Currency

By Suzanne Brown Walsh | September 8, 2017

The combined value of all of the 867 crypto currencies tracked by CoinMarketCap.com is presently over $161 billion. Only seven years ago, on what is commemorated as "Bitcoin Pizza Day," Bitcoin, then a new crypto currency, was worth barely anything. So, on May 22, 2010, early Bitcoin enthusiast Laszlo Hanyecz exchanged 10,000 bitcoins with another programmer for two Papa John's pizzas (worth about $25), to show that bitcoins could actually be used to buy things. The value of those 10,000 bitcoins today is a stunning $45M, and some businesses, such as Overstock.com, accept bitcoins directly as payment for goods (thus, a bitcoin owner can exchange bitcoins for a product, using it in somewhat the same manner as fiat currency).

Why should estate planners and clients care? We assist our clients in planning for the management and disposition of their property during incapacity and at death. Some of our clients, perhaps unbeknownst to us, have purchased bitcoins, or another virtual (for purposes of this article, I have used the terms crypto and virtual currency interchangeably) currency such as Ethereum or Litecoin. Sound farfetched? It isn't. These days, it seems as if almost everyone is "into" virtual currency. The biggest commercial virtual currency wallet and exchange service, Coinbase, has enabled users without any computer proficiency to easily purchase, hold and sell the three virtual currencies the site currently supports. Fidelity Investments has recognized the popularity of virtual currency, announcing recently that its customers will be able to link and view their Coinbase accounts from its website.

The problem with virtual currency is that it can be held offline, and even anonymously, making it difficult or impossible for fiduciaries to discover. Given the overall growth in value, it is absolutely crucial for owners to address the collection and disposition of their virtual currency, in the event of their death or incapacity.

The Revised Uniform Fiduciary Access to Digital Assets Act, enacted to date in 36 states, provides clear rules that allow fiduciaries to access known virtual currency and to sometimes, but not always, obtain information about online accounts in which it may be held. Coinbase addresses fiduciary access to its accounts, but only in the context of a deceased user. Since Coinbase accounts are linked to bank accounts, typically, the user's email and/or bank records will normally provide a clue that the Coinbase account exists.

It is vital that estate planners ask clients about virtual currency holdings and advise them of the "extra" planning that is required to properly safeguard, manage and distribute it.

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In Revised UFADAA states, at least, fiduciaries who obtain access to email accounts have a reasonable chance of discovering an online virtual currency account, even if the user's bank records do not show any deposits or transfers to the online virtual currency account. Fiduciaries and family members should also look for signs that the user had an online virtual currency wallet by looking on his or her phone, tablet and computer. Since it is also possible (and in some cases, more advisable) to hold virtual currency in "cold" storage, offline, for safety, fiduciaries and family members should be instructed not to throw out flash drives or any devices (or even, paper!) that could be used to store the owner's private keys and backup information necessary to retrieve the coins. None of us wants to represent a fiduciary or family member who mistakenly throws out the private keys to millions of dollars of bitcoin, as has reportedly happened to some early users.

Once the virtual currency is recovered, the fiduciary has to either manage it, or if the owner has died, dispose of it in accordance with the owner's will or revocable trust. Most wills, trusts and powers of attorney do not expressly address the disposition of virtual currency. In 2014, the IRS defined digital currencies as "property" for federal tax purposes, not as currency. See Notice 2014-21 - Internal Revenue Service. For clarity in describing virtual currencies in estate planning documents, planners should avoid generic references to "currency" and should expressly refer to virtual currency that is to be specifically bequeathed, and include it in the definition of the other property included as part of the residuary or trust estate. In addition, it is incumbent on clients who own virtual currency to provide the account and private key information that fiduciaries need to collect these assets, and to educate them on the security precautions that need to be taken to keep the currency safe from loss or hackers.

Most trusts and estates attorneys are familiar with "probate by truck," which occurs when the possession of a recently deceased family member's bonds, paper securities, cash and tangibles by someone with the house keys and a truck is often the equivalent of ownership. Imagine how much worse this problem will be when the property converted is not tangible, but is a virtual currency that is transferred by a family member or other person with full knowledge of the decedent's holdings and keys?

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As to its management, forty-five jurisdictions (43 states, plus Washington, DC and the USVI) have adopted the Uniform Prudent Investor Act, which governs trustees and in some states, other fiduciaries. The UPIA does not expressly address virtual currency or its management, but it applies to trust assets generally. Given the volatility of the virtual currency markets, retaining virtual currency without court or beneficiary approval would be inadvisable. In most cases, then, the fiduciary has to determine how to sell the currency as soon as reasonably feasible. Virtual currency exchanges are sensitive to large sales, just as are traditional securities markets, so some common sense and research is necessary.

As the saying goes, life comes at you fast; as this year's exponential growth in virtual currency valuations has shown.

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