

Tales from the Crypt(o): Estate Planning for Cryptocurrency



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Kelsey is a member of our Wealth Preservation and Estate Planning group. She represents individuals and families in estate planning and the administration of estate and trust matters.

Mainstream interest in cryptocurrency has skyrocketed over the last few years. Despite digital currencies plummeting nearly \$2 trillion in value since peaking in late 2021, the market continues to grow. As of May 2022, one in five Americans invested, traded, or used cryptocurrencies. An estimated 46.5 million more Americans are expected to invest in cryptocurrencies for the first time this year.

For those entering the cryptocurrency market, updating estate planning documents may not be top-of-mind. But incorporating this complex asset class into an estate plan is imperative to protect and eventually gift this unique investment.

Accessibility Issues

In 2021, an estimated 20% of then-existing Bitcoin, worth approximately \$140 billion, was lost or stranded in digital wallets. The same features that make cryptocurrency appealing — security, anonymity, and decentralization — increase the risk these assets will be lost without advance planning.

Cryptocurrency exchange companies do not allow owners to make pay-on-death beneficiary designations. In fact, very few companies have implemented official procedures for the collection and transfer of assets upon death. To prevent digital assets from disappearing at death, crypto investors should take the following initial steps:

- Talk to an estate planning attorney about existing crypto investments and any plans to purchase additional cryptocurrencies.

- Clearly identify the existence of any cryptocurrencies in all planning documents (e.g., wills, trusts, and powers of attorney).
- Grant fiduciaries explicit authority to access and transfer digital assets in all planning documents.
- Provide fiduciaries with detailed instructions about how to access the digital accounts.

Simply put, crypto investors must not only inform family members and fiduciaries that crypto accounts exist, but they must also explain how to access the digital accounts to those who will be handling their affairs.

Fiduciary Considerations

Most states, including Minnesota, have adopted some form of the Uniform Prudent Investor Act, which requires trustees to invest and manage assets in a reasonably prudent manner. Because the value of cryptocurrency is notoriously volatile, investments are risky. As such, it is very challenging for fiduciaries to comply with their duty to act as a prudent investor when an estate or trust contains cryptocurrencies.

The significant risk of liability involved with managing cryptocurrencies makes many fiduciaries reluctant to serve. To reduce risk and alleviate hesitation, estate planning documents should provide fiduciaries with clear authority to retain cryptocurrency and indemnify fiduciaries to the greatest extent possible for doing so.

Tax Implications

The IRS classifies cryptocurrency as *property* for federal tax purposes. Every purchase, sale, or exchange of cryptocurrency creates a potential taxable event that must be reported to the IRS. Such treatment may result in substantial income, gift, and estate tax implications for the inclusion of cryptocurrencies in an estate plan.

Common income and estate tax reduction strategies, including lifetime gifting and charitable giving, become more complicated and potentially less effective with cryptocurrency because its value is difficult to predict at any given time.

To comply with reporting and payment obligations or leverage potential tax benefits of cryptocurrency, investors and their fiduciaries should either obtain an appraisal or track and maintain detailed records of the date, basis, and value of each transaction involving cryptocurrency.

Conclusion

Crypto investors need to take steps to protect and transition their crypto investments as they would any other financial assets. Whether you have an extensive crypto portfolio or are considering investing in the cryptocurrency market for the first time, Moss & Barnett's estate planning attorneys can help you plan for your future by protecting both your traditional and digital assets.