

**LEGAL UPDATES**

Giving Crypto? Substantiation is Key!

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Despite its recent volatility, cryptocurrency remains a hot topic in philanthropy. Donors continue to look for ways to make charitable contributions that give them tax benefits, and charities continue to look for creative ways to broaden support of their missions. With the continued popularity of cryptocurrency with some investors, looking to donations of cryptocurrency is of natural interest to donors and charities alike.

Donors considering making a gift of cryptocurrency to their favorite charity will need to do a little initial research. The donor should ensure the potential recipient is a qualified 501(c)(3) public charity and consult the charity about its ability to accept and process a cryptocurrency gift.^[1] If the charity is not able to accept the gift directly, there may be donor advised funds that are able to accept the gift and then make a further gift to the donor's desired charitable donees. Donors seeking to make a cryptocurrency gift should be aware that there are strict technical requirements set by the IRS in making these types of gifts.

In a recent IRS pronouncement (CCA 20230212^[2]), which follows a long history of pronouncements and cases, the IRS Chief Counsel made clear that the IRS will require substantiation that strictly complies with the letter of the law for income tax charitable deductions even for relatively small gifts of cryptocurrency. The opinion examined a request for non-taxpayer specific advice about the requirements of substantiation for charitable deductions for cryptocurrency gifts. The taxpayer claimed a deduction by valuing the cryptocurrency at the value determined on the applicable cryptocurrency exchange.

In the CCA, the IRS Chief Counsel confirmed that cryptocurrency is "property" (within the meaning of IRS Notice 2014-21) and that tax principles applicable to property transactions apply to cryptocurrency. *See also* Rev. Rul. 2019-24. The IRS Chief Counsel also confirmed that cryptocurrency does not fall within the exclusion from the appraisal requirements that is available for contributions of cash, publicly traded securities or other easily and objectively valued property, even though there are established markets for transferring and trading cryptocurrency.^[3] Thus, the IRS Chief Counsel confirmed that a "qualified appraisal" is required for charitable gifts of cryptocurrency. Further, where the taxpayer argued that her valuation using the value on the applicable

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cryptocurrency exchange should fall within a reasonable cause exception for noncompliance, the IRS Chief Counsel denied that claim. As a result, the charitable deduction was denied.

Thus, to obtain a charitable contribution deduction for a gift of cryptocurrency, donors (and their advisors) need to understand the general rules applicable to property gifts. Code Section 170(a)(1) provides generally that deductions for gifts of property are allowed if verified under regulations prescribed by the Treasury Secretary. Gifts of property for which a deduction greater than \$5,000 is claimed (other than gifts of cash, publicly traded securities or other types of easily and objectively valued assets listed in the Code and the Regulations), must be substantiated by a "qualified appraisal." See I.R.C. § 170(f)(11)(C). The IRS has continuously held fast to its position that strict compliance is required in substantiating charitable gifts for income tax deductions, including the qualified appraisal requirement for certain property.

Code Section 170(f)(11)(E)(i) provides that a "qualified appraisal" is an appraisal that meets the requirements of Treasury Regulations and is conducted by a "qualified appraiser". Those Regulations are very specific, and they are found in Treasury Regulation Section 1.170A-17.^[4] To be a qualified appraisal, the appraisal must comply with generally accepted appraisal standards under the Uniform Standards of Professional Appraisal Practice. Beyond the fair market value of the property on the contribution date, the appraisal must meet the very detailed requirements listed in the Regulation, such as a detailed description of the gifted property or the gifted interest in the property, a description of any restrictions, agreements or information applicable to the property or its use, the methods and specific bases for the valuation, and required statements and undertakings by the appraiser. There are also very detailed requirements in the Treasury Regulation applicable to the timing of the appraisal vis a vis the gift date and the filing date.

A "qualified appraiser" is defined by Treasury Regulation Section 1.170A-17(b) as an individual with verifiable education and experience in valuing the type of property for which the appraisal is performed, as described in paragraphs (b)(2) through (4) of that Section. That Section goes on to specifically define the required education and experience and gives examples. The appraiser's qualifications and lack of a prohibited relationship must be contained in the appraisal. While cryptocurrency exchanges have been around for several years, qualifications of appraisers for that type of property to meet the IRS requirements continues to lag, so donors will need to do some research to locate an appraiser who fits the IRS definition as well as currently possible.

In addition to qualified appraisals, the IRS requires that Form 8283 be completed by the donor and appraiser, and signed by the charity, and that the donor obtain a contemporaneous receipt for the donation from the charity donee. The charity is not required to value the donation in either acknowledgement but simply acknowledges that the property was given to the charity. In the receipt, the charity must identify any goods or services provided by the charity in exchange for the donation, and any such consideration will reduce the deductible amount.

Donors and their tax advisors should consult the substantiation requirements whenever a gift of property other than cash or publicly traded stock is contemplated during the donor's lifetime, and this includes cryptocurrency. Proper planning will require that a qualified appraiser be retained to prepare a qualified appraisal within the preparation and delivery timeframes, and that the appraisal should be reviewed by the donor's tax advisor to ensure that the requirements of the Treasury Regulations are strictly observed. The Form 8283 and receipt requirements will also need to be satisfied. Failure to comply with the IRS's strict and detailed requirements will place the donor's income tax charitable deduction squarely in the IRS's sights for risk of denial.

Many thanks to my colleague, Wade Hauser, for editing this alert.

^[1] While a donor could give appreciated cryptocurrency to a private foundation, the deduction would be limited to the donor's basis in the property (i.e., what the donor paid for it) versus the property's fair market value.

^[2] <https://www.irs.gov/pub/irs-wd/202302012.pdf>. CCAs cannot be cited as precedent.

^[3] See I.R.C. § 170(f)(11)(A)(ii)(I); Treas. Reg. § 1.170A-16(d)(2)(i).

^[4] <https://www.govinfo.gov/app/details/CFR-2022-title26-vol4/CFR-2022-title26-vol4-sec1-170A-17>