A Comprehensive Guide to Digital Asset Tax Legislation

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On June 9, 2026, the House Ways and Means Committee held a hearing to discuss a number of discussion drafts of legislation and introduced bills that address the taxation of digital assets.[1] While Congress remains at the beginning of a potentially long road to enacting legislation that addresses the many complex questions surrounding digital asset taxation, this public hearing represents a significant step forward. Reflecting months of behind-the-scenes legislative work, the hearing signaled a degree of bipartisan consensus on the fundamental need for comprehensive digital asset tax reform, even as many critical details remain to be finalized.

This public hearing builds upon prior work. On January 23, 2025, the White House released a 166-page report titled "*Strengthening American Leadership in Digital Financial Technology*," which included policy recommendations for the taxation of digital assets (referred to herein as the "White House Report"). This was followed by the introduction on June 30, 2025 by Senator Cynthia Lummis (R-WY) of S. 2207, a comprehensive bill to reform the tax treatment of digital assets (the "Lummis Bill").[2] Most recently, the bipartisan H.R. 8899, the Digital Asset Protection, Accountability, Regulation, Innovation, Taxation, and Yields Act (the "PARITY Act"), was introduced on May 19, 2026 by Representatives Max Miller (R-OH) and Steven Horsford (D-NV). These three initiatives (collectively, the "Prior Proposals") provided important background for the recent Ways and Means hearing.[3]

At a high level, the legislative proposals to date are all directionally aligned: each recognizes that existing federal tax rules were not designed for digital asset markets and that targeted tax rules are needed to reduce compliance friction, eliminate certain tax planning opportunities, and provide administrable rules for market participants. However, there are some significant differences between the proposals, and more work will need to be undertaken before consensus is reached. This article provides a summary of a number of the bills discussed at the committee hearing and the Prior Proposals, so that readers will have an understanding of how various proposals have evolved as well as the differences between them.

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I. H.R. 9178—Less Tax Paperwork for Digital Asset Owners Act

The "Less Tax Paperwork for Digital Asset Owners Act" submitted by Congressman Rudy Yakym (R-IN) seeks to promote administrability by reducing the paperwork burden associated with using digital assets in everyday commerce.

A. Background

Under the present law, the disposition of digital assets in exchange for property or services is treated as a taxable property sale. Thus, taxpayers seeking to use digital assets as a medium of exchange may be required to comply with complex cost basis tracking requirements in order to calculate and report taxable gain or loss (although to some degree these requirements may be reduced through the use of specialized software). Similar issues arise when digital assets are used to pay network transaction fees. These issues are particularly acute in the context of stablecoins, which require the same cost basis and gross proceeds reporting as other digital assets but typically do not have meaningful gain or loss realized upon their dispositions.

B. "Less Tax Paperwork for Digital Asset Owners Act"

1. De Minimis Rule

Under the "Less Tax Paperwork for Digital Asset Owners Act", no gain or loss would be recognized on the disposition of a digital asset to pay a network validation fee, provided the fee amount is no greater than $10. The gain or loss is preserved by reducing the amount of network fees taken into account in determining the amount of gain or loss on the disposition of any asset, in determining the amount of any deduction, or in determining the basis of any asset acquired by the amount of any gain not recognized under the *de minimis* rule.[4]

This *de minimis* transaction fee rule would not apply to any digital asset subject to a mark-to-market method of accounting. In addition, the *de minimis* rule would not apply to the disposition of a digital asset by (i) a trader, broker, or dealer in digital assets; (ii) a person in the trade or business of batching or facilitating the validation of digital asset transactions; (iii) any person in a trade or business which is substantially similar to those described in (i) or (ii), to the extent provided by the Secretary; or (iv) any person that engaged in more than 5,000 digital asset transactions during the preceding taxable year. These exceptions could be relaxed in situations where the taxpayer demonstrates to the Secretary that there will not be a substantial revenue loss from the taxpayer applying the exceptions. The Secretary would be required to issue guidance identifying different types of taxpayers for which the exceptions do not apply and the information required from the taxpayers to demonstrate that there will not be a substantial revenue loss. The evaluation of revenue loss would be required to take into account the method or methods used by the taxpayer for selecting the digital assets used to pay network fees and the average holding period of such digital assets and any revenue loss would be reduced by the amount of administrative costs to the Treasury and the additional compliance costs to the taxpayer that would be imposed if the *de minimis* exception did not apply.

Conforming changes would be made to the broker reporting requirements to exclude from broker reporting transactions subject to the *de minimis* transaction fee rule.

The *de minimis* rule is proposed to apply to the disposition of assets after December 31, 2027.

2. Simplified Accounting for Widely Traded Digital Assets

The "Less Tax Paperwork for Digital Asset Owners Act" would allow taxpayers to elect to mark-to-market widely traded digital assets. The election could be made on a digital asset-by-digital asset basis. For this purpose, digital assets are widely traded if the assets are fungible or are determined under rules provided by the Secretary to have values that are directly linked or highly correlated. Unlike other existing mark-to-market regimes, the mark-to-market gain or loss recognized under this simplified method of accounting would be treated as short-term capital gain or loss in its entirety. This elective treatment may allow taxpayers to reduce their recordkeeping burdens, but it would come at the cost of potentially reducing the amount of gain that could be treated as preferentially taxed long-term capital gain if the digital asset in question were held for more than a year.

In the case of a digital asset loan, the bill treats the loaned digital assets as continuing to be held by the lender. This appears to allow taxpayers to mark-to-market loaned digital assets without taking into account any valuation differences that may result from the contractual lending arrangement (*e.g.*, discounts for credit risk).

Similar to mark-to-market under Code Sec. 475, the bill turns off the wash sale rules of Code Sec. 1091, the constructive sale rules of Code Sec. 1259, and the related party loss disallowance rules of Code Sec. 267 for digital assets subject to this new mark-to-market method of accounting.

The election is effective for the first taxable year beginning after the election is made. This rule prevents the use of any hindsight in making the election.[5] The election procedures do not include rules for first-year taxpayers, but it is possible that rules allowing for a mid-year election during the first year of a taxpayer's existence would be established in regulations. The election cannot be revoked for the first five taxable years to which the election applies. If revoked, the election cannot be made again for the five years following revocation.

Conforming changes would be made to the broker reporting requirements to allow for aggregate reporting of digital assets subject to election, similar to the rules currently in place for Code Sec. 1256 contracts. Customers would be required to notify their broker of their elections.

The simplified method of accounting is proposed to be available for taxable years beginning after December 31, 2027.

3. Special Rules for U.S. Dollar Stablecoin Transactions

The "Less Tax Paperwork for Digital Asset Owners Act" would treat the tax basis of any U.S. dollar stablecoin upon its acquisition, and the amount realized upon its later disposition, as being equal to the redemption value of the stablecoin, if such U.S. dollar stablecoin was acquired and disposed of in a sale or exchange. An exception would be made if it is unreasonable to conclude the value at the time of acquisition or disposition was within 0.5 percent of the redemption value.[6] In the case of transactions between related parties, this exception applies only if it is not unreasonable to assume that the U.S. dollar stablecoin's value is equal to 100 percent of its redemption value at the time of acquisition or disposition. It is not entirely clear how this standard would be required to be met. For example, would changes in liquidity that affect market prices be able to be overcome by looking to the redemption value of the asset and the solvency of the issuer?

This proposal using redemption value would not apply to: (i) taxpayers that have a functional currency other than the U.S. dollar; (ii) a trader, broker, or dealer in digital assets; (iii) any person in a trade or business which is substantially similar to (ii), to the extent provided by the Secretary; or (iv) any person that engaged in more than 5,000 digital asset transactions subject to the U.S. dollar stablecoin exception during the preceding taxable year, determined without regard to trade or business transactions (*e.g.*, accepting U.S. dollar stablecoins as payment for goods or services) and any transaction is a sale (for money) of a qualified U.S. dollar stablecoin at or below redemption value.

Conforming changes would be made to the broker reporting requirements to exclude from broker reporting U.S. dollar stablecoin transactions if the customer's basis at the time of acquisition is at least 99.5 percent of the stablecoin's redemption value. Broker reporting is currently required only for: (i) dispositions of digital assets for cash or stored value cards; (ii) dispositions of digital assets for different digital assets; and (iii) the delivery of a digital asset pursuant to a derivative contract or executory contract. The majority of digital asset broker reporting is for digital asset-for-digital asset exchanges involving U.S. dollar stablecoins. If U.S. dollar stablecoins are not treated as digital assets for this purpose, these transactions would no longer be within the reporting framework. It is unclear if this result was fully intended, as it could result in many digital assets being treated as noncovered securities.

These special rules for U.S. dollar stablecoin transactions are proposed to apply to taxable years beginning after December 31, 2026.

C. Prior Proposals

1. PARITY Act

The PARITY Act would provide that no gain or loss is recognized on the sale or exchange of a regulated payment stablecoin unless the taxpayer's basis in the stablecoin is less than 99 percent of the redemption value of the stablecoin. This exception would not apply to dealers and traders.

The PARITY Act exception differs from the "Less Tax Paperwork for Digital Asset Owners Act" because the exclusion of a stablecoin transaction would require an actual determination of basis. Presumably, the shift from this standard to the "unreasonable to assume" standard used in the "Less Tax Paperwork for Digital Asset Owners Act" is intended to provide greater flexibility and reduce administrative burdens on taxpayers.

The PARITY Act also did not include a provision analogous to the transaction fee exception found in the "Less Tax Paperwork for Digital Asset Owners Act" and would not explicitly address the interaction of the stablecoin exception with the broker reporting rules. However, the PARITY Act would mandate a study on a general *de minimis* exception.

2. Lummis Bill

Section 2 of the Lummis Bill would exclude from gross income "gain or loss from the sale, exchange, or disposition of digital assets to purchase products or services in a personal transaction." This exclusion is intended to operate similar to the current exclusion for personal-use foreign currency transactions under Code Sec. 988(e)(3).

The gross income exclusion has several limitations. For instance, the exclusion would not apply where the sale, exchange, or disposition is for cash or cash equivalents, including payment stablecoins, or in cases in which the property is used in an active trade or business or is held for the production of income. These limitations are intended to distinguish personal-use payment activity from investment, business, or cash-out transactions.

The bill also contains both transactional and annual limitations. First, under a transaction-level limitation, the exclusion would not apply in the case of any sale, exchange, or other disposition for which either:

(i) The total value of the sale, exchange, or other disposition exceeds $300; or
(ii) The total loss which would otherwise be recognized with respect to the sale, exchange, or other disposition exceeds $300.

This limitation is asymmetrical. Gains would be included in gross income in any situation where the *value of the transaction* is greater than $300. If the taxpayer has basis in the digital asset used to effectuate the transaction, the amount of gain that would be captured would be less than $300 (perhaps significantly). Conversely, the second prong of the limitation only ensures that losses are captured to the extent *the loss* exceeds $300. This formulation creates a relatively significant limitation on the benefit of this provision, and does not have an analog in the rules for foreign currency personal use transactions.

To ensure that the transaction level limitation is not circumvented by breaking a transaction into smaller pieces, the Lummis Bill includes an aggregation requirement, in which all sales, exchanges, or dispositions that are part of the same transaction (or a series of related transactions) are treated as a single sale, exchange, or disposition.

The second limitation is applied at the taxpayer level and limits the amount of gain that may be excluded for each taxable year to $5,000.[7]

The third limitation is an anti-abuse provision. It provides that, except as otherwise provided by the Secretary, the gross income exclusion does not apply to a sale, exchange, or disposition of digital assets if the principal purpose of the transaction is to eliminate gains. It would seem unlikely that the Secretary would exercise this authority to allow taxpayers to engage in transactions with the principal purpose of eliminating gains. Therefore, it is unclear why this concept was included in this third limitation.

The various dollar thresholds included in the limitations are subject to inflation adjustments. The provision also provides a broad grant of regulation authority for (i) recordkeeping requirements; (ii) anti-abuse standards; (iii) allocation of basis and characterization of appreciation; and (iv) treatment of mixed transactions (transactions which involve both property eligible for the exclusion and property ineligible for the exclusion).

The provision is intended to create a more administrable framework for personal-use transactions.[8] Notwithstanding that stated goal, the provision imposes significant recordkeeping requirements. Taxpayers must track both basis and transaction values to determine whether a particular transaction is able to be excluded under the transactional-level and taxpayer-level limitations. The provision also explicitly requires taxpayers to maintain books and records or separate wallets or accounts to distinguish between transactions eligible for the exclusion and transactions that are not eligible. It does not allow taxpayers to opt out of the gross income exclusion provision if their current recordkeeping process (which presumably systemically captures all gains and losses) is easier to apply. This lack of an opt-out is also significant because certain taxpayers would experience a gross income *increase* due to the exclusion. The provision would exclude both gains and losses from gross income, excluding net losses in situations in which a taxpayer's losses exceeded gains. The potential for this unfortunate result is increased by the asymmetry of the transaction-level limitation, which results in the more likely capture of losses than gains.

It may be noted that the broad *de minimis* exception of the Lummis bill is not included in PARITY Act and that a number of later proposals provided more targeted administrative relief.

II. H.R. 9175—Tax Clarity for Mining and Staking Act

The "Tax Clarity for Mining and Staking Act" submitted by Congressman Mike Carey (R-IN) is intended to provide clarity for taxpayers engaged in mining and staking and to help maintain America's leadership in the digital asset economy.

A. Background

Blockchains achieve network security using one of two general consensus mechanisms—proof of work ("PoW") and proof of stake ("PoS").

PoW operates using a "peer-to-peer" model that is decentralized in the sense that no single company or person operates the network. Instead, so-called "blockchain" technology, which is sometimes referred to as distributed electronic ledger technology, enables this peer-to-peer model to function. When a given cryptocurrency transaction occurs, it is first broadcast to its network so as to be verified or validated. Validation occurs using cryptography (that is, encryption and decryption). Once confirmed, each transaction is then recorded with other transactions in a "block" of computer code and is then added and linked to previous blocks to form a chain—hence, the term "blockchain." The updated ledger is then distributed across the network, such that all computers on the network are constantly verifying that the blockchain is accurate. In a PoW consensus process, "miners" compete with each other to solve a cryptographic puzzle. The winning miner is given the right to create a new block that is then broadcast to the network and is rewarded with newly minted/created cryptocurrency and, in some cases, also a portion of transaction fees.

Under a PoS consensus process, "validators" lock-up (*i.e.*, "stake") the blockchain's native cryptocurrency and receive rewards (paid in the blockchain's native cryptocurrency) when they create new blocks or validate blocks created by other validators. In most PoS systems, validators are chosen at random to create blocks and are responsible for checking and confirming blocks they don't create. Although validator selection is random, the chances of being selected generally increase with the size of the stake, much like a weighted lottery. If the selected validator successfully verifies a given transaction or creates a new block, then the network updates the blockchain and staking rewards are awarded to the validator. In PoS systems, it may be possible to also earn fees from users.[9]

1. IRS Position: Immediate Income Recognition

In its earliest cryptocurrency guidance (Notice 2014-21), the Internal Revenue Service ("IRS") addressed the timing question related to mining rewards and indicated that such rewards constituted gross income upon receipt.[10] The IRS did not express a position on the tax characterization of blockchain rewards but possibilities that would align with immediate income inclusion include service income, prizes or awards, or some other type of "gross income." Therefore, presumably the result is some kind of ordinary income (as opposed to capital gain). The guidance provided in Notice 2014-21 does not meaningfully address other considerations related to blockchain rewards. For example, the guidance does not consider the source of mining income. It also only tangentially addresses whether mining activities constitute a trade or business by indicating that an individual engaged in mining as a trade or business is subject to self-employment tax.[11] This presupposes the existence of a trade or business (indicating that mining can, at least under certain circumstances, be a trade or business), but the guidance does not elaborate on any criteria that might be considered when determining if a trade or business exists.

The IRS did not directly address the treatment of staking income until much later in Rev. Rul. 2023-14,[12] which considers a situation where a cash-method taxpayer staked a digital asset and received new units of the digital asset as a staking reward. In the facts provided, the taxpayer initially and for a brief period lacked the ability to sell, exchange, or otherwise dispose of any interest in the staking rewards. The IRS again addressed the timing question only and ruled that the fair market value of the staking rewards constituted gross income includable at the time the taxpayer obtained dominion and control over the staking rewards, *i.e.*, the date as of which the taxpayer had the ability to sell, exchange, or otherwise dispose of the cryptocurrency received as a reward. The IRS noted that this result follows even if the staking occurs indirectly through a cryptocurrency exchange (*i.e.*, custodial staking).

As with the prior guidance in Notice 2014-21 addressing mining rewards, the IRS did not provide a detailed rationale or basis for this conclusion, and uncertainty persists about the position of the IRS regarding staking rewards (*e.g.*, as service income, prizes or awards, or "other gross income"). Clarification on this issue could influence other questions associated with staking income, such as sourcing. The facts of the revenue ruling are also limited, as it considers an individual cash-basis taxpayer. Would a similar conclusion be reached for an accrual method taxpayer? Or would staking income be required to be taken into account as it economically accrues? If it should be accrued, how should a taxpayer value the accrual? The IRS ruled that the result was unaffected by whether the taxpayer staked directly or through a custodian. However, the IRS did not weigh in on the other potential consequences of custodial or liquid staking arrangements.[13] Lastly, like Notice 2014-21, the revenue ruling does not provide meaningful guidance on the source of staking income or the situations in which staking activities could rise to the level of a trade or business.

Reinforcing its position as set forth in Rev. Rul. 2023-14, the IRS subsequently released CCA 202444009, which involved the freezing of staking rewards on a cryptocurrency platform with facts that appear to resemble FTX Trading Ltd. The taxpayer was an individual cash method taxpayer who staked cryptocurrency on a platform. The user agreement with the platform provided that staking rewards would be credited to the taxpayer's account (following any applicable lock-up or waiting period), with the taxpayer then able to sell, exchange, or transfer the rewards. Staking rewards were in fact credited to the taxpayer's account. However, later in the year the platform froze all customer accounts, filed a Chapter 11 bankruptcy petition, and the taxpayer was unable to sell, exchange, or transfer the credited awards. Citing Rev. Rul. 2023-14, the IRS again noted that the fair market value of staking rewards constituted gross income at the time the taxpayer gained dominion and control over the rewards. Here, according to the IRS, the taxpayer was in actual receipt of the rewards when they were credited to his or her account and the taxpayer had dominion and control at that time, prior to the account freeze.[14] Accordingly, the taxpayer was required to include the amount of the rewards into gross income for the year, notwithstanding the fact that subsequent events during the year limited access to the rewards.

As a matter of policy, the IRS approach creates a possibility of uneconomic taxable income. Consider the following example:

> Scott receives 100 XTZ as a staking reward on October 3, 2025 when the price of XTZ is $9.14. On February 24, 2026, Scott sells the 100 XTZ received as a staking reward for $265. For purposes of this example, assume that Scott: (i) is subject to a 37 percent marginal ordinary income tax rate, (ii) is subject to a 20 percent capital gains tax rate, (iii) holds XTZ as a capital asset, and (iv) has no other capital gains or capital losses, and would not benefit from capital loss carrybacks or carryovers.
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> Under the IRS position, Scott recognizes $914 of ordinary income in 2025 (100 XTZ × $9.14/XTZ) and pays $338 of tax. In 2026, Scott recognizes a $649 loss for the difference between the amount realized on the sale ($265) and his basis in the XTZ that were sold ($914). If the XTZ is a capital asset in Scott's hands, this loss is capital and generally cannot be used to offset ordinary income. As a result of this staking activity, Scott has a cumulative pre-tax income of $265 ($914 minus $649) and an after-tax loss of $73 ($265 received on sale, minus $338 of taxes paid). Thus, it is possible that the tax consequences of the activity can transform a pre-tax economic income position into an economic loss.[15]

2. Alternative Position: Self-Created Property Theory

There is an alternative to the IRS position. Under a "self-created property" theory, some taxpayers have taken the position that blockchain rewards consisting of newly created cryptocurrency are not taxable upon receipt, because the creation of property is not itself a taxable event.[16] Under the self-created property characterization, income or loss is not recognized until the cryptocurrency received as a blockchain reward is later sold, exchanged or otherwise disposed of in a taxable transaction.

If the recognition of income is tied to a later sale or exchange event, does this mean that the entire amount of economic income or profit from the staking activity could be treated as capital gain? Some commentators have indicated that the answer to this question is "no."[17] Although this conclusion might be intuitive, the character of a gain on a sale or exchange as ordinary or capital depends on the nature of the asset being sold, not whether the receipt of the asset was previously subject to tax.[18] The character of an asset as ordinary or capital is instead determined under the long-standing statutory framework set forth in Code Sec. 1221. In most situations, blockchain rewards are considered capital assets. This is implicit in the IRS frequently asked questions ("FAQs"), which apply only in (the presumably most common) situations where cryptocurrency is held as a capital asset.[19]

As a matter of policy, the self-created property approach would have the benefit of alleviating the issue of character mismatches that might otherwise occur under the IRS approach. Consider the following results (based on the same facts as the previous example):

> Under the self-created property characterization, Scott recognizes no income and pays no tax in 2025. When the XTZ is sold in 2026, Scott recognizes a $265 capital gain and pays $53 of tax. Scott has cumulative pre-tax income of $265 and cumulative after-tax income of $212 ($265 received on sale, minus $53 of taxes paid). This is a markedly different result from the previous example, where economic income was transferred into an overall economic loss as a result of the tax consequences of the staking activity.

The characterization of staking rewards income as capital gain or ordinary income is significant for taxable investors, due to the limitations on the use of capital losses[20] and the preferential rates afforded to capital gains.[21] It is also significant for other investor classes. For foreign investors, the distinction is also relevant as capital gain generally is not considered fixed, determinable, annual, or periodical (FDAP) income subject to U.S. tax.[22] Likewise, the characterization could be important for tax-exempt investors as capital gain (other than dealer property gain described in Code Sec. 512(b)(5)(A) or (B) or gain that is considered debt-financed by reason of Code. Sec. 514) is not subject to tax as unrelated business taxable income ("UBTI").[23]

3. Litigation on the Taxation of Blockchain Rewards

Prior to the release of Rev. Rul. 2023-14, the taxpayers, in *Jarrett*, took the position that staking rewards received on the Tezos blockchain were not required to be included in taxable income until sold and therefore sought a tax refund.[24] The IRS granted the Jarretts a refund, but in doing so did not provide any rationale, analysis, or admission of the Jarretts' technical position. The Jarretts rejected the IRS's refund offer and sought a court ruling that would create precedent and prevent the IRS from challenging their position in the future. The case, however, was dismissed as moot, and it is clear, in light of the subsequent release of Rev. Rul. 2023-14, that the IRS disagrees with the position that staking rewards received were not required to be included in taxable income until sold.[25] In 2024, the Jarretts filed another refund claim for a subsequent year, again asserting the self-created property theory as the basis for the refund.[26] As of the date of publication, this case is still awaiting trial.

The Tax Court recently considered a version of the self-created property argument from *pro se* taxpayers in *Paschall*.[27] Although the self-created property theory was rejected by the court, there are several reasons why that case does not definitively address the validity of the self-created property theory. First, the *Paschall* decision was a memorandum decision and is therefore not a binding precedent. More importantly, the taxpayers in *Paschall* had conducted their staking activities through a custodian, and the court used this fact to refute the self-created property theory. A similar line of analysis would not seem to be applicable outside the custodial staking context. Moreover, the court explicitly disclaimed any reliance on the IRS position as espoused in Rev. Rul. 2023-14, so the case cannot be described as an endorsement of the IRS's broader position.[28] Thus, the final analysis of the self-created property theory will need to wait for the *Jarrett* decision.

4. Other Considerations

Exchange-traded funds ("ETFs") are normally structured as grantor (fixed investment) trusts for tax purposes. One of the requirements of grantor trust classification is that there is not a "power to vary" the investments of the trust.[29] Prior to the publication of Rev. Proc. 2025-31,[30] whether staking the digital assets of the trust would constitute an impermissible power to vary was a significant question. In Rev. Proc. 2025-31,[31] the IRS set forth a safe harbor under which a trust otherwise qualifying as a grantor trust would not lose grantor trust status due to staking activities. However, certain requirements of the Revenue Procedure impose significant restrictions on the manner in which staking activities are conducted.

Also, assuming one adopts the IRS position that staking rewards are ordinary income upon receipt (as opposed to capital gains only when sold), there are also significant questions as to whether staking rewards constitute UBTI and the manner in which staking rewards should be sourced for FDAP withholding purposes. There are also open questions as to whether staking activities could constitute a trade or business, which is relevant to the deductibility of any expenses and to the treatment of foreign investors engaged in delegated staking arrangements with U.S.-based validators who could be subject to tax on effectively connected income ("ECI") if there is a U.S. trade or business ("USTB").

B. "Tax Clarity for Mining and Staking Act"

1. General Rule for Mining and Staking Rewards

The "Tax Clarity for Mining and Staking Act" would generally align with the IRS position on mining and staking rewards, requiring the current inclusion of those rewards as ordinary income. Under this general approach, the costs of acquiring mining and staking rewards would generally be deductible as incurred, but the IRS would have the authority to allow taxpayers to conform the treatment of such costs with their financial accounting treatment.

The "Tax Clarity for Mining and Staking Act" includes language specifying that no inference is intended as to the treatment of newly minted digital assets under prior law. The bill would apply to assets acquired in taxable years beginning after the date of enactment.

2. Deferral Election

The "Tax Clarity for Mining and Staking Act" would also provide an election whereby taxpayers could defer the recognition of income related to newly minted digital assets until those assets are disposed of. If the election is made, acquisition costs would be required to be capitalized. In addition, the gain or loss realized on disposition would be ordinary in character, rather than capital. Thus, the deferral election would align the timing consequences with the self-created property theory, at the cost of any appreciation being subject to tax as ordinary income. In this respect, it has been likened to a reverse Code Sec. 83(b) election.

The deferral election would only apply to "qualified newly minted digital assets." In the case of mining, this definition would require that the taxpayer engage in the validation activities directly and be the first owner of the newly created digital asset. In the case of staking, the definition would similarly require that the taxpayer hold the staked digital assets and be either the first owner of the newly minted digital asset or acquire the newly minted digital asset promptly after it was issued. Controlled foreign corporations ("CFCs") and passive foreign investment companies ("PFICs") would be ineligible for the deferral election.

As the deferral election applies only to newly created assets, it would not apply to any blockchain rewards received as transaction fees. Different blockchains have different reward structures, with some relying more heavily on transaction fees. Thus, the taxation could potentially vary considerably based on the reward structure of a particular blockchain. In addition, separating out transactional fees from newly created assets could be administratively burdensome for some taxpayers, which could reduce the appeal of the election. Another significant scope reduction is the requirement that the taxpayer hold the staked asset. This would not be the case in many custodial staking arrangements, such that taxpayers may need to stake natively on the blockchain to avail themselves of the election, which would require a degree of technical expertise.

As estimated by the Joint Committee on Taxation, the deferral election would result in a significant revenue loss for the government, prompting some commentators to suggest it is overly generous to taxpayers. In particular, there is a possibility that taxpayers staking digital assets might be incentivized to hold them until death in order to avail their heirs of a step up in basis on the assets, thus allowing the value of those digital assets to avoid income taxation. There are also concerns that deferral of otherwise passive income might unfairly advantage digital asset staking *vis-à-vis* other passive forms of yield generation. To address these concerns, Representative Horsford (D-NV) unveiled a discussion draft to amend the "Tax Clarity for Mining and Staking Act" to require taxpayers to recognize any deferred gain after five years.[32]

The "Tax Clarity for Mining and Staking Act" includes branch and partnership rules, treats certain qualified newly minted digital assets as unrealized receivables for partnership purposes, and excludes specified mining and staking income and gain from qualified business income under Code Sec. 199A.

The bill would apply to digital assets acquired in taxable years beginning after the date of enactment.

3. Sourcing

The "Tax Clarity for Mining and Staking Act" would "clarify" that income from the acquisition of a digital asset received in connection with validation activities is sourced to the residence of the taxpayer. This clarification is intended to promote onshore staking activities by ensuring that non-U.S. taxpayers are not treated as receiving U.S.-sourced FDAP income from conducting delegated staking activities with U.S.-based validators. This provision would apply to digital assets acquired in taxable years beginning after the date of enactment.

The "Tax Clarity for Mining and Staking Act" would not address the treatment of staking activities more broadly. For example, the bill does not address whether staking generally constitutes a trade or business activity and does not explicitly exclude staking rewards from the definition of UBTI.

4. Investment Trusts Engaged in Staking

The "Tax Clarity for Mining and Staking Act" provides that an entity or arrangement shall not fail to be treated as a fixed investment (grantor) trust by reasons of the power of the trustee to engage in staking digital assets held by the trust, retain or distribute digital assets received in connection with staking, determine which digital assets to stake, take measures necessary or appropriate to ensure that the trust has sufficient liquidity to make distributions in redemption of interests in the trust, and perform acts related to the exercise of these powers. This would generally align with the IRS guidance provided in Rev. Proc. 2025-31,[33] but would loosen some of the requirements (*e.g.*, the distribution requirement). The proposal would apply to taxable years ending after the date of enactment.

C. Prior Proposals

1. PARITY Act

The PARITY Act is generally structured similarly to the "Tax Clarity for Mining and Staking Act," requiring current inclusion of staking and mining rewards as a general rule, but also offering a deferral election. However, the PARITY Act would include a maximum deferral period of five years.

The PARITY Act provides that passive staking activities do not constitute a trade or business, including for purposes of Code Sec. 512 (UBTI) and Code Sec. 864 (ECI/USTB).[34] Similar provisions were not included in the "Tax Clarity for Mining and Staking Act".

Like the "Tax Clarity for Mining and Staking Act", the PARITY Act would also provide that the ability to stake digital assets is not a power to vary that would cause a trust that would otherwise qualify as a grantor trust to be treated as a partnership entity.

2. Lummis Bill

The Lummis Bill would amend Code Sec. 451 to defer the income recognition of blockchain rewards until the rewards are sold, with the amount being treated as ordinary income. This substantively aligns with the Tax Clarity for Mining and Staking Act. Lummis Bill commentary notes that this "aligns the taxation of mining and staking rewards with the actual realization of economic benefit" and also notes that this new system would prevent cash flow problems.[35]

The Lummis Bill would also amend Code Sec. 863 to provide that for foreign investors any income related to validation of digital asset transactions will be sourced to the residence of the taxpayer.

3. White House Report

The White House Report recommends that Treasury and the IRS review the previously issued guidance related to the timing of income recognition for mining and staking rewards and "consider whether to clarify, modify, or reverse that guidance, taking into account any recent intervening developments since the issuance of such guidance." In the context of legislation, the White House Report indicates that if Congress changes the timing of mining and staking rewards income, Congress should also address second order issues, such as whether the character of income should be ordinary on disposition, what rules should apply to determine the order of dispositions of ordinary versus capital units, and potential differences between the fair market value of rewards at the time of receipt compared with the fair market value of rewards at the time of sale or other disposition.

III. H.R. 9173—Charitable Deductions for Digital Asset Donations Act

The "Charitable Deductions for Digital Asset Donations Act" introduced by Representative Kelly (R-PA) would simplify the process around contributions of digital assets and provide parity between digital assets and other financial instruments.

A. Background

For taxpayers that itemize deductions,[36] a donation of an appreciated long-term capital gain property generally can provide a double benefit: (i) the taxpayer may claim a charitable contribution deduction equal to the property's fair market value on the date of the contribution and (ii) any embedded gain is not required to be recognized by the taxpayer as taxable income.[37] This tax efficiency has made donating appreciated digital assets a common strategy used by individuals to maximize the amount of their charitable giving. However, that strategy is not without traps for the unwary.

To claim a charitable contribution deduction, a taxpayer must satisfy certain substantiation requirements. In general, for contributions of property for which a deduction of more than $5,000 is claimed, the taxpayer must obtain a qualified appraisal of such property for the taxable year in which the contribution is claimed.[38]

To be a "qualified appraisal," an appraisal must be conducted by a "qualified appraiser" in accordance with generally accepted appraisal standards and meet certain other requirements described in the relevant regulations.[39] The term "qualified appraiser" means an individual who (i) has earned an appraisal designation from a recognized professional appraiser organization or has otherwise met minimum education and experience requirements set forth in regulations, (ii) regularly performs appraisals for which the individual receives compensation, and (iii) meets such other requirements described in regulations.[40]

A qualified appraisal is not required for donations of certain readily valued property specifically set forth in the Code and regulations; namely, cash, stock in trade, inventory, property primarily held for sale to customers in the ordinary course of business, publicly traded securities, intellectual property, and certain vehicles.[41] It is possible that some cryptocurrency held for investment would qualify as "publicly traded securities," which term is defined by the applicable regulations by reference to Code Sec. 165(g)(2).[42] Code Sec. 165(g)(2) defines a security as (i) a share of stock in a corporation; (ii) a right to subscribe for, or to receive, a share of stock in a corporation; or (iii) a bond, debenture, note, or certificate, or other evidence of indebtedness, issued by a corporation or a government or political subdivision thereof, with interest coupons or in registered form.

While it is possible that certain digital assets do in fact qualify as securities within the definition of Code Sec. 165(g)(2),[43] most mainstream cryptocurrencies do not fall within the definition. Regardless of the security status of a particular asset, policy would dictate that liquid digital assets certainly should be excluded from the qualified appraisal requirement, given the readily available pricing information. Unfortunately, in CCA 202302012 the IRS concluded that (i) a qualified appraisal is required for cryptocurrency donations if a deduction greater than $5,000 is claimed and (ii) the reasonable cause exception will not excuse noncompliance with the qualified appraisal requirement. In the IRS's view, this result followed given that the cryptocurrency involved was not a "security" as defined in Code Sec. 165(g)(2). Accordingly, the IRS position is that taxpayers making donations of digital assets with a fair market value greater than $5,000 are required to obtain qualified appraisals to claim a tax deduction under current law.[44]

B. "Charitable Deductions for Digital Asset Donations Act"

The "Charitable Deductions for Digital Asset Donations Act" would amend Code Sec. 170 to treat certain widely traded digital assets in the same manner as publicly traded securities for purposes of the qualified appraisal rules. The term "widely traded digital asset" is generally defined to mean a fungible digital asset for which quotations are readily available and for which the market capitalization exceeded $500 million at substantially all times during the calendar year. A digital asset does not, however, meet this definition if it is a tokenized digital asset for which the reference asset is not a traded digital asset. The widely traded digital asset exception also does not apply if the taxpayer and related parties own more than 10 percent of the digital asset.

This provision would address the practical problem identified in CCA 202302012. The policy rationale for the proposal is straightforward. For liquid digital assets traded on exchanges with readily available quotations, the appraisal requirement may impose cost and procedural risk without materially improving valuation accuracy. Removing the appraisal requirement for actively traded digital assets would align the substantiation regime more closely with the treatment of publicly traded securities and reduce the risk that otherwise valid charitable contribution deductions are denied for technical noncompliance.

The bill is consistent with the White House Report's recommendation to remove the qualified appraisal requirement for digital asset donations and with the previous proposals described below. The principal technical issue is line-drawing: the relief is sensible for liquid, actively traded assets with reliable quotations, but more difficult for thinly traded tokens or assets susceptible to valuation manipulation. The proposal's reliance on the "widely traded digital asset" concept is therefore critical to making the provision administrable. Some have raised concerns regarding the ability to manipulate the values of certain digital assets that are not widely traded. To address these concerns, Representative Horsford (D-NV) released a discussion draft of an amendment that would require a written acknowledgment from the donee and limit the amount of deduction to the proceeds of the sale if the donee sold the contributed digital asset.

The "Charitable Deductions for Digital Asset Donations Act" would apply to tax years beginning after December 31, 2026.

C. Prior Proposals

1. PARITY Act

The PARITY Act proposal is similar to the "Charitable Deductions for Digital Asset Donations Act." Under the PARITY Act, a qualified appraisal is not required for the donation of "actively traded digital assets" which are defined as fungible digital assets with a minimum trading volume of $50 million for the two calendar years immediately preceding the transaction, a minimum yearly market capitalization of $10 billion for the three calendar years immediately preceding transaction, and with respect to which the taxpayer and related parties hold no more than five percent of the value or units of the asset.

The PARITY Act also includes special rules for infrequently traded digital assets, which require a written acknowledgment from the donee and limit the amount of deduction to the proceeds of the sale if the donee sold the contributed digital asset.

2. Lummis Bill

The Lummis commentary describes the appraisal requirement as a "bureaucratic barrier" discouraging charitable giving.[45] In line with the White House Report recommendation, the Lummis Bill would amend Code Sec. 170 to treat "actively traded" digital asset contributions in the same manner as a publicly traded security (which is not subject to an appraisal requirement under current law if the security is capital gain property and market quotations are readily available). The Lummis Bill did not precisely define when a digital asset would be considered actively traded.

3. White House Report

The White House Report suggests that legislation remove the requirement of a qualified appraisal for charitable donations of digital assets worth more than $5,000.

IV. H.R. 9176—Providing Analogous Rules for Digital Assets Act

The "Providing Analogous Rules for Digital Assets Act" introduced by Representative Kustoff (R-TN) would allow digital assets to qualify for the same safe harbors as traditional assets and would allow dealers and traders in digital assets to make the same elections as commodities traders and dealers.

A. Digital Asset Loans

1. Background

Securities lending transactions are commonly used to increase the yield on holding a security and are an integral part of the "plumbing" of the capital markets. In the typical securities lending transaction, the securities owner (lender) will lend securities to a counterparty (borrower) under an agreement providing for the return of identical securities upon demand. The securities borrower is also required to pay a "borrow fee" and make "in lieu payments" (*i.e.*, payments equivalent to any dividends, interest, or other payments received on the security being lent). Securities loans are typically collateralized, with the security lender paying a rebate fee on the collateral posted.[46] The securities borrower typically has the right to dispose of the borrowed security and often borrows the security expressly for that purpose (*e.g.*, to enter into a short sale transaction).

Under current law, no gain or loss is recognized if the transfer of a security is pursuant to an agreement that meets certain requirements under Code Sec. 1058.[47] Gain or loss also is not recognized on the return of that security in exchange for rights under the agreement.[48] For this purpose, the term "securities" is defined by reference to Code Sec. 1236(c) and includes corporate stock, notes, bonds, debentures and other evidence of indebtedness, and any evidence of an interest in or right to purchase any of the foregoing.[49]

Proposed Reg. §1.1058-1(b)(3) provides that an agreement is subject to nonrecognition treatment under Code Sec. 1058 only if it provides that the lender may terminate the loan upon notice of not more than five business days. Under this proposed regulation, any securities loan with a fixed duration would be a taxable disposition of the security being loaned.[50] Outside of certain abusive transactions, the policy justification for this result is unclear and purposely "defective" securities loans have been used by taxpayers to trigger gains or losses without divesting of the economics of an underlying position.

The capital markets have changed significantly since Code Sec. 1058 was enacted in 1978 and the proposed regulations were published in 1983. In particular, the variety of assets and the volume of trading in such assets that are not clearly subject to Code Sec. 1058 have both increased greatly. For example, taxpayers seeking to increase yields will frequently lend digital assets in transactions that look similar to customary securities lending transactions. These transactions are not within the scope of Code Sec. 1058 because digital assets are not "securities" as defined by Code Sec. 1236(c).[51] Although it could be argued that Code Sec. 1058 is a safe harbor provision rather than the sole means of achieving nonrecognition,[52] the proposed regulations could be read to suggest otherwise.[53] For a detailed discussion of the arguments for and against recognition in the context of digital asset loans under current law, *see Cryptocurrency Loans—Taxable or Not?*, 17 J. Tax'n Fin. Prods. 1 (2020).[54]

Digital asset taxation is rife with complexity and uncertainty. Although the various proposals discussed in the Ways and Means hearing would fall short of addressing every issue, collectively, they would address many of the most pressing areas of uncertainty and update the tax code in many areas where digital assets slip through the cracks.

Another area of uncertainty with securities lending arrangements is the treatment of "in lieu payments." If a taxpayer holds a bond issued at a discount, the taxpayer is generally required to accrue the discount over the term of the debt using a constant yield to maturity. In *Samueli*,[55] the taxpayer took the position that accrual of discount on a debt instrument was not required when the debt instrument was loaned. If this transaction had worked as intended, the taxpayer would have been able to defer income and convert the income from ordinary interest accruals to capital gain. The taxpayer lost, but the underlying issue of accrual methodology is also relevant to non-abusive transactions and is an area of significant uncertainty. On the other hand, not every payment on a bond or stock is taxable. Should "in lieu payments" in respect of principal payments or non-dividend distributions be taxed when they would not be if the underlying instrument were held directly? The law is not entirely clear.[56]

2. "Providing Analogous Rules for Digital Assets Act"

The "Providing Analogous Rules for Digital Assets Act" would expand the securities loan nonrecognition rules to traded digital assets provided the Code Sec. 1058(b) requirements are met. The bill would require that payments in lieu of any distributions on the loaned digital assets be paid to the lender. The bill would apply to transfers made after the date of enactment.

Although helpful, it may be difficult to structure digital asset loans to meet the "in lieu payment" requirement of this proposal. The barriers to a given individual or entity creating a new digital asset through a hard fork are almost non-existent, but most new digital assets never achieve market acceptance. In recognition of this fact, most digital asset loans provide for in-kind "in lieu payments" of hard fork currencies only in situations where the new digital asset is economically meaningful. It could be argued that these arrangements are within the "spirit" of Code Sec. 1058 and ought to be given nonrecognition treatment. However, the bill does not appear to provide a *de minimis* exception of any kind (although the Secretary could create an exception through regulations). If future regulations do provide a *de minimis* in lieu payment requirement, prevailing market practice might serve as the best guide.

It is also notable that the expanded scope of Code Sec. 1058 in the "Providing Analogous Rules for Digital Assets Act" would be limited to digital assets and would not affect the treatment of other actively traded assets for which the provision could be relevant. For example, many publicly traded partnership interests may be loaned, but there is currently a dearth of guidance as to how those transactions should be treated. The bill would also not address the treatment of fixed-term securities loans or the manner in which income on a loaned asset should be recognized.

3. Prior Proposals

a) PARITY Act. The PARITY Act would expand the securities loan nonrecognition rules in Code Sec. 1058 to "eligible digital assets" in a manner generally similar to the "Providing Analogous Rules for Digital Assets Act." Eligible digital assets would be defined as fungible digital assets: (i) for which a market price is readily ascertainable; (ii) which do not represent or confer any ownership interest, equity interest, debt obligation, or other financial or property right in any entity, asset, commodity, or enterprise; and (iii) which is designed and functions as a medium of exchange, store of value, or unit of account and is recorded and transferred through distributed ledger technology.

The PARITY Act would also provide that the lender is required to include "in income lieu payments" for any staking rewards, transaction fees, protocol distributions, or other amounts that would be payable with respect to a lent digital asset in the same manner as if the lender received the payment directly.

b) Lummis Bill. The Lummis Bill includes a proposal to expand the securities loan nonrecognition rules in Code Sec. 1058 to include loans of actively traded digital assets (referred to as "specified assets"). In addition, and unlike the "Providing Analogous Rules for Digital Assets Act," the Lummis Bill would provide nonrecognition treatment for fixed term loans, except as provided by the Secretary. Additionally, the Lummis Bill proposal would require that income be taken into account by the lender as if the lender had continued to hold the loaned asset. This rule would apply to both timing and character. The bill would provide for appropriate basis adjustments to the loan contract, including when the loaned asset is returned. Lastly, the bill provides regulatory authority to carry out the purposes of the new ruleset for digital asset forks and airdrops, and to fees associated with digital asset lending transactions.

c) White House Report. The White House Report notes the uncertainty with respect to digital asset loans and indicates that legislation should be enacted to amend Code Sec. 1058 to provide that it applies to loans of actively traded fungible digital assets, provided that the loan has terms similar to those currently required for loans of securities. The White House Report also recommends that the Secretary be granted authority to determine when a digital asset is actively traded, and to address differences between the standard terms of securities loans and cryptocurrency loans.

B. Dealers and Traders

1. Background

Code Sec. 475 requires dealers in securities to use the mark-to-market method of accounting for inventory and non-inventory securities held at year end.[57] Gain or loss recognized under this mark-to-market method of accounting is generally characterized as ordinary gain or loss.[58] For purposes of Code Sec. 475, a "security" includes corporate stock, interests in widely held or publicly traded partnerships and trusts, debt instruments, and certain derivative financial instruments.[59] Although the IRS has taken the position that digital assets are property for federal income tax purposes,[60] as of yet, no guidance has been issued on the question of whether any particular digital asset is a "security" for purposes of Code Sec. 475. Nevertheless, many practitioners take the position that digital assets are not securities, as defined by Code Sec. 475(c)(2).[61]

Dealers in commodities and traders in securities or commodities may elect to use the mark-to-market method of accounting.[62] For this purpose, Code Sec. 475(e)(2)(A) defines the term "commodity" to include "any commodity which is actively traded."[63] Thus, there are two requirements—an asset must be (i) a commodity and (ii) actively traded. Under current law, it is not entirely clear whether digital assets meet this definition.[64]

With respect to the first requirement, Code Sec. 475(e)(2)(A) does not attempt to define the term "commodity" in general. In similar self-referential situations where the term being defined is used in the definition, the courts have generally held that an item must fit within the common understanding of the term in order to fall within the definition.[65] In common parlance, the term "commodity" generally connotes fungibility with other assets of a similar class and grade. Many digital assets satisfy this requirement.[66] However, the term commodity might also impart a tangible asset connotation, which arguably would not be satisfied by digital assets.[67]

With respect to the requirement that the commodity must be actively traded, the statute cross-references Code Sec. 1092(d)(1). Futures on Bitcoin ("BTC"), Ethereum ("ETH"), and Solana ("SOL") are traded on the Chicago Mercantile Exchange (a Commodities Futures Trading Commission-regulated commodities exchange), but other digital assets are not similarly traded. Although not entirely clear, most practitioners believe mainstream digital assets are actively traded because the exchange on which they trade operates similar to a traditional commodities exchange.[68]

2. "Providing Analogous Rules for Digital Assets Act"

The "Providing Analogous Rules for Digital Assets Act" would create a new category of assets—"covered digital assets"—that may be marked-to-market at the election of a dealer or trader in those assets. Covered digital assets would include: (i) any widely traded digital asset; (ii) any notional principal contract with respect to any widely traded digital asset; (iii) any evidence of an interest in, or a derivative instrument in, any widely traded digital asset including any option, forward contract, futures contract, short position, and any similar instrument in such widely traded digital asset; and (iv) an instrument that is a hedge of an instrument described in (i)–(iii) and is identified as such before the close of the day on which it is acquired or entered into. Covered digital assets that would also be securities described in Code Sec. 475(c)(2) or commodities described in Code Sec. 475(e)(2) would not be considered securities or commodities for purposes of Code Sec. 475.

The potential availability of a mark-to-market method of accounting for digital assets would be useful for a variety of reasons. Mark-to-market accounting generally provides a clear reflection of income with respect to assets that are traded in established markets. In addition, for financial accounting purposes taxpayers may be required to mark their inventory or trading positions to market. Allowing taxpayers to use their financial accounting valuations for tax purposes may reduce tax compliance costs. The mark-to-market method of accounting would also mitigate the impact of the newly applicable wash sale provisions for electing taxpayers. In addition, it would be helpful for digital asset straddle positions, which are arguably already subject to the loss deferral, capitalization, and special holding period rules under Code Secs. 263(g) and 1092.

The "Providing Analogous Rules for Digital Assets Act" would also provide that a Code Sec. 481(a) adjustment related to adopting the mark-to-market method of accounting (for covered digital assets or otherwise) has the same character as the character of gain or loss which would have resulted from the sale of the property subject to the mark-to-market method of accounting.

The bill would apply to taxable years beginning after the date of enactment.

3. Prior Proposals

a) PARITY Act. The PARITY Act would similarly create an elective mark-to-market regime for dealers and traders in actively traded digital assets. The mark-to-market method of accounting would only apply to digital assets that are considered actively traded (with such term to be defined by the Secretary).

b) Lummis Bill. The Lummis Bill would align with this suggestion by creating a new category of assets—"actively traded" digital assets and derivatives of those digital assets (referred to as "specified assets")—that may be marked-to-market at the election of a dealer or trader in those assets.

c) White House Report. The White House Report suggests that Code Sec. 475 should be amended to apply to actively traded fungible digital assets.

C. Trading Safe Harbor

Code Sec. 864(b)(2) provides generally that non-U.S. traders in stocks, securities, or commodities may trade through an independent U.S. agent, or trade for their own account with U.S.-based personnel, without being treated as engaged in the conduct of a trade or business in the United States. Under current law, it is unclear whether trading in digital assets can qualify under these safe harbors.

1. "Providing Analogous Rules for Digital Assets Act"

The "Providing Analogous Rules for Digital Assets Act" would create a new safe harbor for trading in digital assets. The safe harbor would be structured in the same manner as the existing safe harbors for stocks, securities, and commodities and would apply to taxable years beginning after December 31, 2025.

2. Prior Proposals

a) PARITY Act. The PARITY Act would create a digital asset trading safe harbor substantially similar to the "Providing Analogous Rules for Digital Assets Act."

b) White House Report. The White House Report suggests amending Code Sec. 864(b)(2) to include actively traded fungible digital assets.

V. H.R. 9172—Applying Existing Tax Anti-Abuse Rules to Digital Assets Act

The "Applying Existing Tax Anti-Abuse Rules to Digital Assets Act" introduced by Representative Arrington (R-TX) would expand the scope of the wash sale and constructive sale rules to cover digital asset transactions.

A. Wash Sale Rules

1. Background

Under the wash sale rules of Code Sec. 1091(a), taxpayers who sell stock or securities at a loss are generally prohibited from recognizing the loss if they acquire "substantially identical" stock or securities within a specified "window period" that begins 30 days before the sale and ends 30 days after the sale. If the wash sale rules apply, the disallowed loss is preserved through the application of special basis and holding period rules that tack the basis and holding period of the stock or security that was sold to the replacement stock or security.[69]

The IRS has ruled that commodities[70] and foreign currencies[71] are not securities subject to the wash sale rules. There is also general agreement among commentators that digital assets are not subject to the wash sale rules under current law.[72]

Under current law, the treatment of certain derivative transactions under the wash sale rules is not entirely clear. For example, the tax community is divided on whether certain derivative instruments such as total return swaps should be treated as a contract or option to acquire the underlying stock or security.[73] In addition, it is not clear from the statutory language of the basis tacking rules how basis from the sale of a stock or security tacks to an option contract that triggers a wash sale.[74]

2. "Applying Existing Tax Anti-Abuse Rules to Digital Assets Act"

The "Applying Existing Tax Anti-Abuse Rules to Digital Assets Act" would expand the wash sale rules to cover digital assets other than U.S. dollar stablecoins and contracts or option to acquire or sell a digital asset (other than a U.S. dollar stablecoin). The U.S. dollar stablecoin exception does not apply to taxpayers that have a functional currency other than the U.S. dollar.

The provision would not take into account digital assets acquired in connection with validation activities but does not have broader business use or personal use exceptions. Thus, merchants accepting digital assets in the ordinary course of business and disposing of such digital assets could be required to consider the wash sale rules.

The provision would also clarify the application of the wash sale rules to tokenized assets, treating a tokenized asset as substantially identical to its reference asset if the tokenized asset is economically equivalent to the reference asset. It is unclear how "economically equivalent" should be interpreted, as the tokenization process often creates commercial advantages as compared to direct ownership of the asset (which is, quite obviously, the reason the asset was tokenized in the first place). Presumably, the provision suggests that any advantages conferred solely on account of the token wrapper are not sufficient to render the tokenized asset as non-substantially identical with the reference asset. However, in situations where the tokenization process creates differences in payment terms, credit risk, or other security attributes, it may be possible to conclude that the tokenized asset is not substantially identical to the reference asset.

The "Applying Existing Tax Anti-Abuse Rules to Digital Assets Act" does not adjust the mechanics of the wash sale rules or address existing areas of uncertainty.

The bill would apply to dispositions after the date of the introduction of the Act. There is a transition rule for broker reporting. In the case of any sale or other disposition before January 1, 2028, a customer's adjusted basis in a digital asset may be determined without regard to Code Sec. 1091.

3. Prior Proposals

a) PARITY Act. Similar to the "Applying Existing Tax Anti-Abuse Rules to Digital Assets Act," the PARITY Act would expand the scope of the wash sale rules to cover digital assets. Unlike the "Applying Existing Tax Anti-Abuse Rules to Digital Assets Act," the PARITY Act did not include an exception for U.S. dollar stablecoins or an exception for digital assets acquired through validation activities.

The PARITY Act proposal would also address when two assets are considered "substantially identical." Under the PARITY Act proposal, the substantially identical determination is made based on the economic exposure of the asset and the mere fact that an asset may have different or no voting rights does not prevent the asset from being substantially identical to any other asset. This treatment is not necessarily aligned with current market practice, as many practitioners view voting rights as one of the fundamental rights of stock ownership.[75] The proposal also indicates that the fact that an asset may trade on a different exchange (or no exchange) or a different blockchain (or no blockchain) is not taken into account. Many of these rules would be particularly relevant in the context of tokenized assets, where voting rights are frequently not conferred to the token holder and the token trades on a different platform than the underlying reference asset. However, the PARITY Act proposal stops short of indicating that tokenized assets are in all cases substantially identical to the underlying reference assets, which means that an analysis will still need to be undertaken when there are economic differences (*e.g.*, different payment dates or payment mechanics) that could affect the determination. The proposal also indicates that any asset that would not otherwise be treated as substantially identical to another asset shall not be so treated merely because the asset is based on the same or substantially similar protocol or computer code.

b) Lummis Bill. The Lummis Bill would expand the wash sale rules to cover digital assets, notional principal contracts and derivative instruments with respect to digital assets, and any security (as defined by Code Sec. 475(c)(2)). In this respect, the Lummis Bill proposal is much broader than the "Applying Existing Tax Anti-Abuse Rules to Digital Assets Act" or the PARITY Act proposal. The expanded scope would eliminate uncertainties under current law with respect to certain derivative instruments, widely held trusts, and widely held partnerships. It would also have the effect of bringing within the scope of the wash sale rules instruments that were generally understood to not be subject to the rules under current law, such as foreign currency derivatives. Because the statute would not be amended to apply to physical foreign currency, this would have the somewhat odd effect of subjecting derivatives over currency to the wash sale rules, but not physical foreign currency trades.

The expanded wash sale rules would not apply to transactions entered into by dealers or to stablecoin transactions. The provision does not appear to include exceptions for personal use transactions, *de minimis* transactions, hedging transactions, or other business needs transactions.

The Lummis Bill would also change the basis adjustment provisions of Code Sec. 1091. The Lummis Bill proposal would explicitly provide that basis does in fact tack on to the replacement position, regardless of whether it is a physical security or a derivative instrument. The Lummis Bill proposal would, however, attack a common planning strategy where a taxpayer: (i) sells stock at a loss, (ii) acquires a derivative instrument on the stock (thereby triggering a wash sale), (iii) purchases replacement stock (which is not a wash sale because the derivative already triggered a wash sale), and (iv) terminates the derivative to trigger the loss. The Lummis Bill would provide that in situations where replacement stock is acquired after the derivative instrument is acquired, the basis adjustment is to the replacement stock, not the derivative instrument. The Lummis Bill also provides a broad grant of regulatory authority to address abusive basis adjustment practices.

c) White House Report. The White House Report acknowledges that taxpayers are carrying out wash sale trades in digital assets to capture tax losses and recommends that the wash sale rules be amended to add digital assets to the list of assets subject to the rule. However, the White House Report suggests that stablecoins be excluded from the wash sale provisions.

B. Constructive Sale Rules

1. Background

Code Sec. 1259 provides that if there is a constructive sale of an appreciated financial position, the taxpayer must recognize gain as if such position were sold, assigned, or otherwise terminated at its fair market value on the date of such constructive sale (and the gain must be taken into account in the tax year of the constructive sale).[76] Any gain or loss subsequently realized with respect to such position is adjusted to account for the gain recognized pursuant to the constructive sale, and the holding period of the position is determined as if the position were acquired on the date of the constructive sale.[77]

A constructive sale of an appreciated financial position occurs if the taxpayer (or a related person) enters into certain enumerated transactions that eliminate economic exposure to the appreciated financial position.[78] For this purpose, an "appreciated financial position" is generally defined as any position with respect to any stock, debt instrument, or partnership interest if there would be a gain were such position sold, assigned, or otherwise terminated at its fair market value.[79] Most digital assets do not meet the definition of an appreciated financial position and therefore are not subject to the constructive sale rules.

2. "Applying Existing Tax Anti-Abuse Rules to Digital Assets Act"

The "Applying Existing Tax Anti-Abuse Rules to Digital Assets Act" would expand the scope of the constructive sale rules to cover digital assets other than U.S. dollar stablecoins. The exclusion of U.S. dollar stablecoins is presumably based on the premise that any gain inherent in a U.S. dollar stablecoin would be minimal and not implicate the policy of the constructive sale rules. In keeping with this premise, the U.S. dollar stablecoin exclusion does not apply in situations where the taxpayer uses a functional currency other than the U.S. dollar.

The "Applying Existing Tax Anti-Abuse Rules to Digital Assets Act" also indicates that a tokenized digital asset is treated as substantially identical to any stock, debt instrument, or partnership interest to which the tokenized digital asset is economically equivalent. This is similar to the rules applicable to the proposal on wash sales, described above.

The provision would apply to constructive sales after the date of the introduction of the Act (June 8, 2026).

3. Prior Proposals

Similar to the "Applying Existing Tax Anti-Abuse Rules to Digital Assets Act," the PARITY Act would expand the scope of the constructive sale rules to cover digital assets. The Lummis Bill and White House Report do not address constructive sales.

VI. H.R. 9174—Digital Assets Voluntary Disclosure Program Act

The "Digital Assets Voluntary Disclosure Program Act" introduced by Representative Bean (R-FL) would establish a one-time, voluntary disclosure program to promote tax compliance.

The "Digital Assets Voluntary Disclosure Program Act" would require the Secretary to establish a voluntary disclosure program within 12 months of enactment that allows eligible taxpayers to remedy digital asset violations by fulfilling remedial requirements. The remedial requirements include, in part, a requirement to file amended returns and payment of outstanding tax liabilities and the violations penalty on an installment plan. The violation penalty varies depending on the circumstances of the taxpayer and the amount of the deficiency related to digital assets, but could be as little as zero percent of the deficiency or as much as 40 percent of the deficiency. The benefit of the program would be the waiver of all other penalties and the avoidance of criminal prosecution.

VII. Discussion Draft—End Digital Assets Tax Shelters Act

The discussion draft of the "End Digital Assets Tax Shelters Act" would address residency-based planning employed by certain U.S. citizens in an attempt to avoid taxation on digital asset gains. The proposal notes that this "tax loophole" is based on an improper interpretation of the rules and seeks to establish a bright-line rule that clearly disallows the abuse. In general, the proposal would treat a U.S. citizen or resident alien who was a U.S. resident during any of the prior 10 tax years as a U.S. resident for sourcing gain from the sale of a digital asset.

VIII. Conclusion

Digital asset taxation is rife with complexity and uncertainty. Although the various proposals discussed in the Ways and Means hearing would fall short of addressing every issue, collectively, they would address many of the most pressing areas of uncertainty and update the tax code in many areas where digital assets slip through the cracks. The Ways and Means hearing revealed a promising degree of bipartisan agreement on core principles, yet it also made clear that significant negotiation will be required to successfully bridge areas of disagreement. Whether Congress can navigate these issues to form the consensus necessary to enact legislation addressing these crucial issues remains to be seen.

ENDNOTES

* The information in this article is not intended to be "written advice concerning one or more Federal tax matters" subject to the requirements of section 10.37(a)(2) of Treasury Department Circular 230. The information contained herein is of a general nature and based on authorities that are subject to change. Applicability of the information to specific situations should be determined through consultation with your tax adviser. This article represents the views of the authors only, and does not necessarily represent the views or professional advice of KPMG LLP.

[1] A transcript of the hearing can be found here: *waysandmeans.house.gov/event/full-committee-legislative-hearing-on-digital-asset-taxation/*.

A description and text of the various legislative proposals can be found at: *waysandmeans.house.gov/2026/06/09/new-legislation-modernizes-tax-rules-for-digital-assets-improving-access-to-a-growing-market-and-maintaining-americas-competitive-advantage/*.

[2] Available at: *www.lummis.senate.gov/wp-content/uploads/Lummis-Crypto-Tax-Bill.pdf.*

[3] Available at: *www.whitehouse.gov/wp-content/uploads/2025/07/Digital-Assets-Report-EO14178.pdf.*

[4] This rule operates to ensure that the taxpayer's economic gain or loss will ultimately be taxed. A similar rule does not need to exist for losses to achieve a similar result. For example, assume a taxpayer disposes of a digital asset with a basis of $5 and a fair market value of $9 to pay a network transaction fee in a transaction where a digital asset is acquired for consideration worth $100. The $4 of gain is not recognized and not included in the basis of the asset acquired, such that the acquired digital asset has a $105 basis. If the taxpayer immediately sold the acquired digital asset, the taxpayer would realize a $5 loss, which is equal to the taxpayer's economic loss on the combination of the transactions.

Now assume the same facts as above, except the digital asset used to pay the transaction fee has a $15 adjusted basis. The $6 of loss realized on disposition of the digital asset used to pay the network fee is not recognized and the taxpayer's basis in the asset acquired is $115. Again, if the acquired digital asset were immediately sold, the taxpayer would realize a $15 loss, which is equal to the taxpayer's economic loss on the combination of the transactions.

[5] In this respect, the election is more strict than a Code Sec. 475(f) or Proposed Reg. §1.988-7 election, both of which allow the use of some hindsight in deciding whether to make the election for the first year.

[6] The term "redemption value" is defined to mean the dollar amount for which the issuer is obligated to convert, redeem, or repurchase the stablecoin.

[7] The exact language used is: "If, after applying [the gross income exclusion] to a transaction, the taxpayer's total gain for the taxable year from transactions [subject to the gross income exclusion] exceeds $5,000, no further exclusion shall apply for such year." Although the quoted language simply refers to "gain," it seems relatively clear that the drafters intended the $5,000 limitation to be measured by reference to the net, rather than gross, gain subject to the exclusion.

[8] The commentary included on Senator Lummis' website states: "*This provision recognizes the impracticality of tracking every small digital asset transaction, such as buying coffee with Bitcoin, which creates enormous compliance burdens for ordinary users. The $300 threshold strikes a reasonable balance between tax compliance and practical usability of digital assets as a medium of exchange.*" *See www.lummis.senate.gov/press-releases/lummis-unveils-digital-asset-tax-legislation/.*

[9] For a more detailed description of PoW and PoS systems and the tax considerations associated with each, *see* Ritter and Tompkins, *Proof of Stake—What's Really at Stake on the Tax Front?*, 19 J. Tax'n Fin. Prods. 1 (2022).

[10] Notice 2014-21, IRB 2014-16, 938, Question and Answer #8.

[11] Notice 2014-21, IRB 2014-16, 938, Question and Answer #9.

[12] IRB 2023-33, 484.

[13] For example, the transfer of cryptocurrency to a custodian subject to an agreement, on the part of the custodian, to return identical cryptocurrency could potentially be viewed as a taxable disposition. *See* Tompkins and Raglan, *Cryptocurrency Loans—Taxable or Not?*, 17 J. Tax'n Fin. Prods. 1 (2020), for further discussion of cryptocurrency transfers subject to an agreement to return identical cryptocurrency. Liquid staking arrangements could potentially be characterized as a taxable disposition or, alternatively, as an ongoing interest in the underlying cryptocurrency. Liquid staking arrangements also raise questions as to whether the participants are engaged in a joint venture. For further discussion, *see* Proof of Stake Alliance, U.S. Federal Income Tax Analysis of Liquid Staking (undated), available at *static1.squarespace.com/static/62f147feb8108a08e666aea5/t/63f3fd27f0b0fc45f7d906c2/1676934439845/U.S._Federal_Income_Tax_Analysis_of_Liquid_Staking.pdf.*

[14] Interestingly, the IRS also cited Reg. §§1.451-1(a) and 1.451-2(a) "constructive receipt" principles in its analysis, and noted (in a footnote) that any rewards that accrued but were not credited to the taxpayer's account before it was frozen would not be includible in income, as the taxpayer could not sell, exchange or transfer such rewards prior to the freeze; that is, because they were not actually or constructively received, the taxpayer would not have dominion and control in this scenario.

[15] Because of these potentially negative tax consequences, certain industry participants have advocated for a change in the IRS position. *See* MARA, *Level the Paying Field for Bitcoin Miners* (undated), available at 2025 TNTF 58-37.

[16] *See, e.g.*, Reg. §1.61-4 (farmer recognizes income when crops are sold, not when they are grown); Reg. §1.61-3(a) (miner recognizes income when minerals are sold, not when they are mined). Arguments could also be made that inflationary staking rewards do not represent a true accession to wealth. In addition, proponents of the self-created property approach also frequently point to the economic results that can occur under the IRS position in situations where the cryptocurrency declines in value after receipt. That is, and as noted in our numerical example above, because ordinary income would be recognized for the fair market value of staking rewards when earned, if the staker sells those rewards after a price decline, the staker would generally realize a capital loss at such latter date (*i.e.*, an unfavorable timing and character result).

A detailed discussion of the technical basis for the self-created property characterization can be found in Abraham Sutherland, *Cryptocurrency Economics and the Taxation of Block Rewards*, 165 Tax Notes Fed. 749 (Nov. 4, 2019); Abraham Sutherland, *Cryptocurrency Economics and the Taxation of Block Rewards, Part 2*, 165 Tax Notes Fed. 953 (Nov. 11, 2019). For competing views on the current state of the law and what constitutes sound tax policy, *see* Shakow, *Taxing Bitcoin and Blockchains: What the IRS Told Us (and Didn't)*, Tax Notes Fed. (Jan. 13, 2020); Reuven S. Avi-Yonah & Mohanad Salaimi, *New Framework for Taxing Cryptocurrencies*, 175 Tax Notes Fed. 1391 (May 30, 2022); Omri Marian, *Law, Policy, and the Taxation of Block Rewards*, 175 Tax Notes Fed. 1493 (Jun. 6, 2022); Reuven S. Avi-Yonah, *A Response to Professor Marian on Cryptocurrency Tax Policy*, 175 Tax Notes Fed. 1731 (Jun. 13, 2022); Amanda Parsons, *May I Pay More? Lessons From Jarrett for Blockchain Tax Policy*, 176 Tax Notes Fed. 2063 (Sep. 26, 2022); David Forst & Sean McElroy, *Jarrett Is Based on Law, Not 'Blockchain Interests'*, 177 Tax Notes Fed. 423 (Oct. 17, 2022); Omri Marian, *Taxation of Staking Rewards Is Based in Law, Not Hyperbole*, 177 Tax Notes Fed. 579 (Oct. 24, 2022).

Also, although the self-created property characterization is most commonly discussed in the context of staking rewards, similar arguments could be made in the context of a PoW consensus model, at least to the extent the rewards constitute newly created cryptocurrency (as opposed to transaction fees paid by other blockchain participants).

[17] *See, e.g.*, Unchained Podcast Episode 320, Your 2021 Crypto Taxes: How to Handle NFTs, DAOs, Airdrops and More (Feb. 15, 2022), at 44:00; Omri Marian, *Law, Policy, and the Taxation of Block Rewards*, 175 Tax Notes Fed. 1493 (Jun. 6, 2022); Amanda Parsons, *May I Pay More? Lessons From Jarrett for Blockchain Tax Policy*, 176 Tax Notes Fed. 2063 (Sep. 26, 2022); Omri Marian, *Taxation of Staking Rewards Is Based in Law, Not Hyperbole*, 177 Tax Notes Fed. 579 (Oct. 24, 2022). *But see* David Forst & Sean McElroy, *Jarrett Is Based on Law, Not 'Blockchain Interests'*, 177 Tax Notes Fed. 423 (Oct. 17, 2022).

[18] The enactment of Code Sec. 1221(a)(3) (dealing with certain self-created intangibles) and its repeated expansion demonstrates that, absent inclusion in a category of ordinary assets under Code Sec. 1221, self-created property is a capital asset that gives rise to capital gain when sold. If that were not the case, there would be no reason for Code Sec. 1221(a)(3) to exist. The case law predating Code Sec. 1221(a)(3) is also informative in that it shows that courts and IRS would likely evaluate whether self-created property is an ordinary or capital asset through the statutory framework of Code Sec. 1221 (and in particular Code Sec. 1221(a)(1)). Thus, if a taxpayer adopts the self-created property characterization and is confident that their cryptocurrency rewards are not a category of ordinary property under Code Sec. 1221, the taxpayer should be able to achieve capital gains treatment on the sale of the rewards tokens.

For further discussion, *see* Ritter and Tompkins, *Proof of Stake—What's Really at Stake on the Tax Front?*, 19 J. Tax'n Fin. Prods., No. 1 (2022). *See also* David L. Forst & Sean P. McElroy, *Jarrett Is Based on Law, Not 'Blockchain Interests,* 177 Tax Notes Fed. 423 (Oct. 17, 2022).

[19] IRS, Frequently Asked Questions on Virtual Currency Transactions, Question and Answer #4 and #6 *www.irs.gov/individuals/international-taxpayers/frequently-asked-questions-on-virtual-currency-transactions*. Although the IRS would certainly disagree with the underlying premise of the self-created property theory (and there is certainly a fair degree of doubt as to the viability of that theory), that shouldn't bear on the character of the blockchain rewards as ordinary or capital.

[20] Code Sec. 1211.

[21] Code Sec. 1(h).

[22] Reg. §§1.1441-2(b)(2), (b)(3), and (c). This conclusion assumes that the foreign investor is not engaged in United States trade or business.

[23] Code Sec. 512(b)(5). If the staking rewards are not treated as gain, then it is presently unclear whether such reward constitutes unrelated business taxable income. *See* Ritter and Tompkins, *Proof of Stake—What's Really at Stake on the Tax Front?*, 19 J. Tax'n Fin. Prods. 1 (2022).

[24] No. 3:21-cv-00419 (M.D. Tenn.) (May 26, 2021).

[25] *See* Memorandum Granting Motion to Dismiss, *Jarrett*, No. 3:21-cv-00419 (M.D. Tenn. 2022), *available at www.govinfo.gov/content/pkg/USCOURTS-tnmd-3_21-cv-00419/pdf/USCOURTS-tnmd-3_21-cv-00419-0.pdf*.

[26] *See Jarrett*, M.D. Tenn., No. 3:24-cv-01209 (M.D. Tenn. 2024). The case is currently still pending.

[27] TC Memo. 2026-46.

[28] An IRS ruling is not binding on the courts. *See Halliburton Co.*, 100 TC 216, 232, Dec. 48,914 (1993), *aff'd*, CA-5, 25 F3d 1043 (1994), and *aff'd sub nom. Halliburton*, CA-5, 25 F3d 1043 (1994) ("[A] a ruling or other interpretation by the Commissioner is only as persuasive as her reasoning and the precedents upon which she relies."). Given the limited analysis in the ruling, it is not clear that a judge would find it entirely persuasive.

[29] Reg. §301.7701-4(c)(1).

[30] IRB 2025-48, 743.

[31] IRB 2025-48, 743.

[32] *waysandmeans.house.gov/wp-content/uploads/2026/06/Amendment-to-H.R.-9173-and-H.R.-9175.pdf*.

[33] IRB 2025-48, 743.

[34] With respect to UBTI, it is worth noting that the IRS does not generally consider the existence of a trade or business a requirement for UBTI. A better approach might therefore be to revise the Code Sec. 512(b) exceptions to UBTI treatment to exclude staking income.

[35] *www.lummis.senate.gov/press-releases/lummis-unveils-digital-asset-tax-legislation/*.

[36] A more limited deduction is available for taxpayers choosing the standard deduction.

[37] Code Sec. 170(a). The deduction for property gifted to a private foundation may be limited to the taxpayer's basis in the property. Code Sec. 170(e)(1)(B)(ii).

[38] Code Sec. 170(f)(11)(C).

[39] Code Sec. 170(f)(11)(E)(i). *See also* Reg. §1.170A-17 and Reg. §1.170A-13, as applicable.

[40] Code Sec. 170(f)(11)(E)(ii). *See also* Reg. §1.170A-17(b).

[41] *See* Code Sec. 170(f)(11)(A)(ii)(I); Reg. §1.170A-16(d)(2)(i).

[42] Reg. §1.170A-13(c)(7)(xi).

[43] *See* Tompkins and Dalbey, *Current Events Roundup: Stock Buyback Excise Tax, Corporate AMT, and Digital Asset Guidance*, 19 J. Tax'n Fin. Prods. 4 (2023), for a discussion of the situations where a cryptocurrency might be classified as a Code Sec. 165 security.

[44] CCA 202302012 (Jan. 10, 2023) determined that the reasonable cause standard was not met because the taxpayer did not attempt to obtain a qualified appraisal. The IRS also noted that the appraisal requirement is described on Form 8283, such that a reasonable person reviewing their return should be aware of the requirement. CCA 202302012 (Jan. 10, 2023) then went on to say that "the reasonable cause exception was not intended to provide taxpayers with the choice of whether to obtain a qualified appraisal, but to provide relief where an unsuccessful attempt was made in good faith to comply with the requirements of section 170." Although the cases cited in CCA 202302012 (Jan. 10, 2023) (*H.C. Schweizer*, 124 TCM 232, Dec. 62,113(M), TC Memo. 2022-102; *D. Pankratz*, 121 TCM 1178, Dec. 61,831(M), TC Memo. 2021-26; and *J. Crimi*, 105 TCM 1330, Dec. 59,453(M), TC Memo. 2013-51) certainly support that contention, the properties donated in those cases did not have a readily apparent value (those cases involved the donation of art, oil fields, and undeveloped land). Therefore, taxpayers might possibly attempt to distinguish the donation of digital assets on the grounds that a reasonable person exercising ordinary business care and prudence would not expect that a formal appraisal of actively traded property would be required (because the appraisal would presumably be based on the same trading value the taxpayer used to determine the amount of the donation). Taxpayers might also argue that they reasonably believed cryptocurrencies were securities under the tax law in light of the widely publicized SEC actions treating cryptocurrencies as securities. Nonetheless, obtaining an appraisal is clearly the best course of action.

[45] *www.lummis.senate.gov/press-releases/lummis-unveils-digital-asset-tax-legislation/*.

[46] Frequently the rebate fee will exceed the borrow fee and the two will be netted with only one party making a payment to the counterparty. The tax characterization of rebate fees and borrow fees is not clear, but general market practice is to treat the net payment as interest in the common situation where the rebate fee exceeds the borrow fee. *See* SIFMA, *Re: Guidance on Securities Loan and Repo Payments*, available at: *www.sifma.org/resources/submissions/sifma-submits-comments-to-the-us-department-of-treasury-and-the-irs-requesting-guidance-on-securities-loan-and-repo-payment/*.

[47] Code Sec. 1058(a).

[48] *Id.*

[49] Code Secs. 1058(a) and 1236(c).

[50] *See* Proposed Reg. §1.1058-1(e)(1).

[51] This assumes that the digital asset in question is a security within the meaning of Code Sec. 1236(c). This is not clearly the case in all situations. For example, a DAO token could be characterized as corporate stock for tax purposes (because the DAO is treated as a corporation as a general matter or under Code Sec. 7704). Tokenized securities could also be considered Code Sec. 1236(c) securities, as could stablecoins (which are treated by many market participants as debt instruments for tax purposes).

[52] *See ABA Committee Reports on Securities Lending Transactions*, 91 TNT 107-33 (May 15, 1991) ("In general, *Section 1058(a)* provides that no gain or loss is recognized by the owner of securities when the owner transfers securities for the contractual obligation of the borrower to return identical securities. It constitutes a safe harbor from the recognition of gain or loss where a taxpayer exchanges securities pursuant to an agreement that meets the statutory requirements."); *NYSBA Tax Section Report Addresses Treatment of Securities Loans*, 2011 TNT 112-22 (June 10, 2011) ("There is nothing in the language of [section 1058] itself or the history of the statute to suggest that it was intended to be more than a safe harbor ... In our view, section 1058 should operate as a safe harbor.").

[53] *See* Proposed Reg. §1.1058-1(e)(1) ("If a transfer of securities is intended to comply with section 1058 and fails to do so because the contractual obligation does not meet the requirements of section 1058(b) and §1.1058-1(b), gain or loss is recognized in accordance with section 1001 and §1.1001-1(a) upon the initial transfer of the securities.").

[54] *See also* Shulman, *Loans of Securities, Digital Assets, and Other Fungible Property*, Tax Notes Fed. Volume 173, October 25, 2021; and NYSBA Report No. 1461—Report on Cryptocurrency and Other Fungible Digital Assets, April, 18, 2022.

[55] CA-9, 2011-2 ustc ¶50,697, 661 F3d 399.

[56] Much of the guidance in this area has focused on the tax consequences to the short seller, but arguably there should be parity between the two parties. The general rule is that an in lieu payment is deductible by the short seller and does not result in a basis adjustment. *See e.g.*, Rev. Rul. 60-177 ("[T]he 'short-seller' is required to pay the lender an amount equal to the cash dividend on the stock borrowed to cover the short sale while the stock is on loan. Such an amount, commonly known as a 'short dividend,' is credited to the lender's account by his broker. The 'short-seller' is entitled to a deduction, for Federal income tax purposes, for the amount which he paid to the lender."). However, the IRS's position appears to be that in lieu payments with respect to return of capital

distributions are capital expenditures of the short seller, rather than deductible expenses. *See* Rev. Rul. 72-521 ("The additional shares purchased in the case of a nontaxable stock dividend as well as the compensating payment in the case of a liquidating dividend are each in the nature of a repayment of principal. The amount paid in either case is part of the cost of replacing the borrowed stock and is, hence, a capital expenditure."); GCM 38604 ("Any expenditures incurred by the short seller to obtain securities for delivery in the short sale should be capitalized (added to the cost of the covering transaction) rather than immediately deducted."). In *Main Line Distributors, Inc.*, CA-6, 63-2 USTC ¶9655, 321 F2d 562, the court rejected the IRS's position that a nontaxable distribution was a capital expenditure, stating: "[i]t is our view that the [in lieu] payment is allowed as a deduction, not because it is a repayment of a particular kind of 'dividend' which the lender would have received if the stock had not been borrowed, but because it is a repayment to the lender of what he has lost by lending his stock to the borrower, which the borrower is obligated to repay by reason of his contract with the lender. It is a contractual expense incurred by the taxpayer as a necessary cost of obtaining for a temporary period the use of the stock of another, irrespective of whether it is a taxable or nontaxable dividend to the purchaser." The court went on to deny the taxpayer's deduction on other grounds, but the discussion quoted above does inject a degree of uncertainty as to the proper treatment of an in lieu payment in respect of a nontaxable distribution (such as a return of capital). For further discussion, *see* Jeff Maddrey, *Accounting for Income from Securities Lending Transactions,* 12 J. TAX'N FIN. PRODS. 2 (2014).

57 Code Sec. 475(a).

58 Code Sec. 475(d)(3)(A)(i).

59 Code Sec. 475(c)(2).

60 Notice 2014-21, IRB 2014-16, 938.

61 As a technical matter, this may not necessarily be true in all cases. Included in the definition of a security under Code Sec. 475(c)(2)(C) is any "note, bond, debenture, or other evidence of indebtedness." Some commentators have suggested that "traditional" (non-algorithmic) stablecoin investments could be classified as debt instruments because holders have a legally enforceable claim to demand that the sponsor redeem its stablecoin for U.S. dollars and have a reasonable expectation that the sponsor will have sufficient liquid assets to meet a redemption demand. *See* New York State Bar Association, *Report No. 1461—Report on Cryptocurrency and Other Fungible Digital Assets* (April 18, 2022). However, given the "stable" nature of stablecoins, this point appears to be more academic than practical because there would presumably be only trivial mark to market adjustments for such assets. A more significant question is whether certain DAO tokens could be considered an interest in a widely held partnership (a security under Code Sec. 475(c)(2)(B)) or potentially a corporation (a security under Code Sec. 475(c)(2)(A)) if the DAO is a publicly traded partnership treated as a corporation under Code Sec. 7704.

62 Code Secs. 475(e) and (f), respectively.

63 Also included in the definition of a "commodity" is any notional principal contract with respect to any actively traded commodity, and certain other derivative financial instruments and hedges with respect to such commodities. Code Sec. 475(e)(2)(B)-(D).

64 For a more detailed discussion of the tax implications of this determination, *see* Vadim Novik, *Hot Commodities and Hotshot Market Makers: Why Should I Care Whether Virtual Currencies Are Commodities for Purposes of Section 475?*, TAXATION OF FINANCIAL PRODUCTS & TRANSACTIONS 2022, Chapter 8.

65 *See, e.g., MoneyGram Int'l, Inc.*, CA-5, 2021-1 USTC ¶50,159, 999 F3d 269, 274 (2021).

66 One obvious exception to this general rule would be non-fungible tokens ("NFTs").

67 The question of whether intangible property such as a digital asset can be a "commodity" is reminiscent of the jurisdictional battle in the late 1970s and early 1980s between the SEC and CFTC over the classification of financial instruments such as Treasuries and GNMAs as "commodities" for purposes of regulating futures contracts on those assets, a battle that finally was resolved by a jurisdictional accord reached between the SEC and CFTC in the Futures Trading Act of 1982, P.L. 97-444. *See, e.g., Board of Trade of the City of Chicago v. Securities and Exchange Comm'n*, CA-7, 677 F2d 1137 (1982), *vacated as moot*, SCt, 459 US 1026, 103 SCt 434 (1982).

68 *See* New York State Bar Association, *Report No. 1461—Report on Cryptocurrency and Other Fungible Digital Assets* (April 18, 2022).

69 Code Sec. 1091(d); Reg. §1.1091-2 and Code Sec. 1223(3); Reg. §1.1223-1(d).

70 GCM 34630 (1971); Rev. Rul. 71-568, 1971-2 CB 312. *See also Corn Products Refining Co.*, CA-2, 54-2 USTC ¶66,082, 215 F2d 513; *Sicanoff Vegetable Oil Co.*, 27 TC 1056, Dec. 22,310 (1957), *rev'd on other grounds*, CA-7, 58-1 USTC ¶9233, 251 F2d 764.

71 Rev. Rul. 74-218, 1974-1 CB 202.

72 *See Cryptocurrencies and the Definition of a Security for Code Sec. 1091*, 18 J. TAX'N FIN. PRODS. 2 (2021). There have been prior proposals to revise Code Sec. 1091 to include digital assets. *See* the budget reconciliation legislation known as the "Build Back Better Act" passed by the House of Representatives on November 19, 2021, pursuant to instructions in S. Con. Res. 14, the Concurrent Budget Resolution for FY2022, S.Con.Res.14, 117th Cong. (2021-2022). Substantively identical proposed wash sale rules were introduced in the Senate by Senator Ron Wyden on December 11, 2021. For a discussion of this prior proposal *see* Joshua Tompkins and Liz Dyor, *Related Party Wash Sale Transactions: An Evaluation of the Current State of the Law and Recent Legislative Proposals,* 19 J. TAX'N FIN. PRODS. 2 (2022); NYSBA Report No. 1456—*Comments on Wash Sale Provisions of the House Proposals for the Build Back Better Act*, January 14, 2022. Subsequently, a bill from Sens. Cynthia M. Lummis, R-Wyo., and Kirsten E. Gillibrand, D-N.Y. introduced in July 2023 set forth provisions related to digital assets and wash sales.

73 *See, e.g.,* L. Farr and M.S. Farber, *Dirty Linen: Airing Out the Wash Sale Rules,* 3 J. TAX'N FIN. PRODS. 3 (2002).

74 Code Sec. 1091(d) provides:

> If the [acquired] property consists of stock or securities the acquisition of which (or the … option to acquire which) resulted in the nondeductibility … of loss from the sale … of substantially identical stock or securities, then the basis shall be the basis of the stock or securities so sold … increased or decreased … by the difference, if any, between the price at which the property was acquired and the price at which such substantially identical stock or securities were sold ….

In situations where a taxpayer sells stock and enters into an option to acquire such stock, it is not entirely clear that Code Sec. 1091(d) tacks basis to the option. Instead, the statute could be read to tacks basis only on stock or securities acquired through the exercise of that option. Obviously, this would be a harsh result ungrounded in any policy concern and we are unaware of the IRS taking this position.

75 *See I. Himmel*, CA-2, 64-2 USTC ¶9877, 338 F2d 815 ("Ownership of stock can involve three important rights: (1) to vote, and thereby exercise control, (2) to participate in current earnings and accumulated surplus, and (3) to share in net assets on liquidation."). *See also* Rev Rul. 75-502, 1975-2 CB 111.

76 Code Sec. 1259(a)(1).

77 Code Sec. 1259(a)(2).

78 Code Sec. 1259(c).

79 Code Sec. 1259(b)(1). Code Sec. 1259(b)(2) excludes from the definition of an appreciated financial position certain positions with respect to debt, hedges of such debt positions, and any position that is marked to market.