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DIGITAL ASSETS: US AND UK REGULATORY AND TAX TREATMENT

Nick Moore, Christine Lombardo, Sarah Riddell, Steven Lightstone,
Sarah-Jane Morin and Kate Habershon
May 21, 2021

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Topics

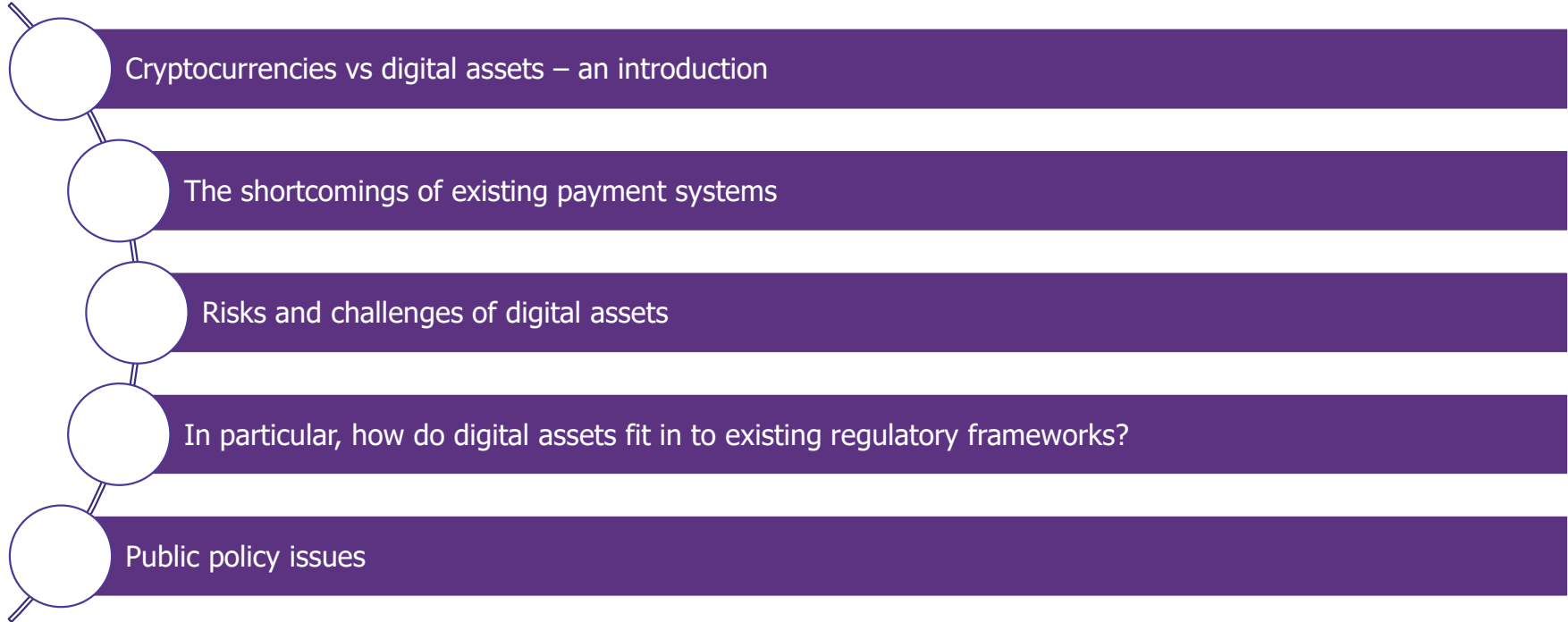
- Nick Moore: Introduction: Digital assets
- Christine Lombardo & Sarah Riddell: US regulatory treatment of digital assets
- Steven Lightstone: UK regulatory treatment of digital assets
- Sarah-Jane Morin: US tax treatment of digital assets
- Kate Habershon: UK tax treatment of digital assets

The background is a dark, almost black, space filled with a dense field of vertical lines of varying heights. Each line is topped with a small, glowing dot in shades of blue, purple, and red. The lines themselves are thin and appear to be composed of small segments, giving them a digital or fiber-optic appearance. The overall effect is a sense of depth and connectivity, reminiscent of a data center or a complex network.

Section 01 Introduction

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Introduction: Digital Assets





Section 02

US & UK Regulatory treatment of digital assets

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US Legislative Efforts

117TH CONGRESS
1ST SESSION

H. R. 1602

IN THE SENATE OF THE UNITED STATES
APRIL 22, 2021

Banking, Housing, and Urban Affairs

AN ACT -

To direct the Commodity Futures Trading Commission and the Securities and Exchange Commission to jointly establish a digital asset working group, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the “Eliminate Barriers to Innovation Act of 2021”.

A BILL

To clarify which Federal agencies regulate digital assets, to require those agencies to notify the public of any Federal licences, certifications, or registrations required to create or trade in such assets, and for other purposes.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*

3 **SECTION 1. SHORT TITLE.**

4 This Act may be cited as the “Crypto-Currency Act
5 of 2020”.

US Regulatory Treatment of Digital Assets

AML

- New FinCEN Proposal
- SEC, CFTC, FinCEN issued a joint statement in 2019 reminding persons engaged in digital asset activities that they are still obligated to comply with AML and countering the financing of terrorism obligations

Money Services Business

- FinCEN
- State considerations

SEC & CFTC Implications

- Regulatory status of XRP in question
- The SEC has continued to issue digital asset guidance
- The CFTC has continued pursuing enforcement actions

Trust Company

- NY Department of Financial Services

State Attorney Generals

- Investigation and enforcement authority

US Regulatory Treatment of Digital Assets



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US Regulatory Treatment of Digital Assets: SEC Developments

- Commissioner Peirce's Token Safe Harbor 2.0 Proposal
 - *Provides a three-year grace period from registration under the federal securities laws.*
- Division of Examinations Risk Alert
 - *Issued to assist firms in their development and enhancement of compliance practices related to digital assets.*
- May 11th Division of Investment Management Staff Statement
- SEC v. Ripple Labs, Inc. Inc., Bradley Garlinghouse, and Christian A. Larsen
 - *The SEC alleges that the defendants engaged in the unlawful offer and sale of securities.*

US Regulatory Treatment of Digital Assets: FinCEN, CFTC, and OCC Developments

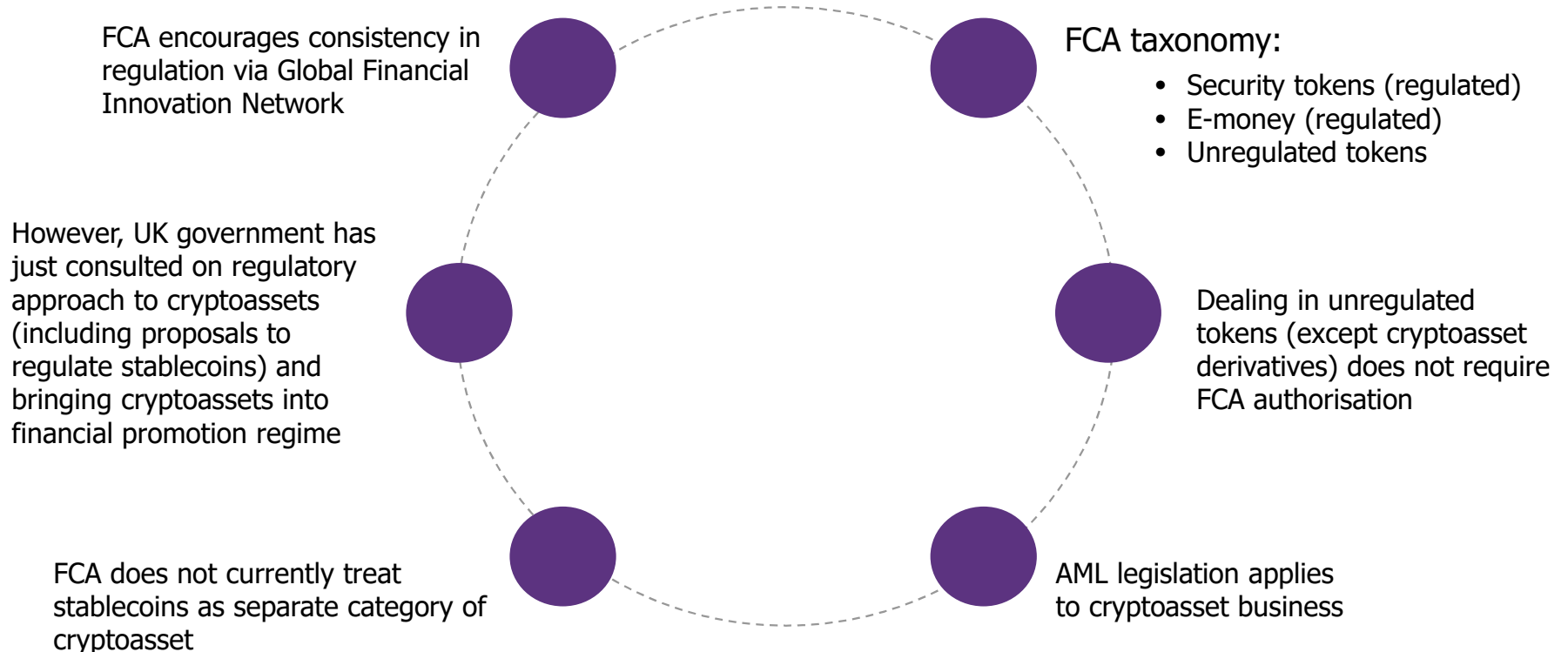
- In December, FinCEN proposed rules that would require banks and FinTechs to submit reports, keep records, and verify the identity of customers in relation to transactions above certain thresholds involving wallets for convertible virtual currency (CVC) or digital assets with legal tender status.
 - CVC: a medium of exchange (such as cryptocurrency) that either has an equivalent value as currency, or acts as a substitute for currency, but lacks legal tender status.
 - Digital assets with legal tender status: any type of digital asset issued by the U.S. or any other country that is designated as legal tender by the issuing country and accepted as a medium of exchange in the country of issuance.

US Regulatory Treatment of Digital Assets: FinCEN, CFTC, and OCC Developments

- In 2021, the CFTC has pursued enforcement actions against Coinbase (\$6.5M civil monetary penalty) and Jaxx (nearly \$400,000 civil monetary penalty and restitution).
- Since January, the OCC has conditionally approved national trust bank charters for Anchorage Trust Company and Paxos National Trust. The OCC has also issued digital asset-related guidance under former Acting Comptroller of the Currency Brian Brooks.
- New Acting Comptroller of the Currency, Michael Hsu, has ordered a review of these recent actions.

"I believe these trends cannot be stopped. They bring great promise, but also risks."

UK Regulatory Treatment of Digital Assets





Section 03
US & UK tax
Treatment of Digital
Assets

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US Tax Treatment of Digital Assets

US Tax Treatment of Digital Assets

IRS Notice 2014-21: convertible virtual currency is treated as property

IRS FAQs on Virtual Currency Transactions

Rev. Rul. 2019-24: Airdrops and forks

CCA 202114020 (March 21)

No specific guidance on stablecoins from the IRS or U.S. Treasury.

Open questions:

Distinguish between stablecoin and other cryptocurrencies?

Gains/losses generated by underlying basket of assets:
Taxable? Reportable? By whom?

UK Tax Treatment of Digital Assets

HM Revenue & Customs has published guidance on the UK tax treatment of cryptocurrencies that has recently been updated to include stablecoin.

Cryptocurrencies are not treated as cash, but rather are treated as assets more akin to securities. Gains will typically be subject to tax, eg as the profits of a trade.

The sterling value of each transaction in cryptocurrencies must be determined to calculate UK tax liabilities.

Stablecoin pegged to sterling may remove some of the issues caused by value fluctuations.

The tax profits of trading in cryptoassets will generally follow the accounting treatment.

The background is a dark blue space filled with a complex network of glowing lines and dots. The lines are thin and radiate from various points, creating a sense of depth and movement. The dots are small and brightly colored, appearing in shades of blue, purple, and red. The overall effect is that of a digital or data landscape, with the lines and dots forming a grid-like structure that recedes into the distance.

Section 04
Presentation
takeaways

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Presentation Takeaways



Overview

The growth of digital assets presents a challenge for global regulators, but also an opportunity to facilitate development of revolutionary access to the modern financial system. A successful way forward will require international collaboration and especially the alignment of the different regulatory spheres into which components of a stablecoin ecosystem will fall.



Global regulation

The cross-border nature of stablecoin gives rise to the need for consistent regulation in relevant jurisdictions. IOSCO's report demonstrates the patchwork of regulation needed to comprehensively regulate stablecoin.



US regulation

The SEC, CFTC, and FinCEN are on the forefront of crypto asset and stablecoin regulatory issues. Based on legislative efforts, we will see FinCEN take the lead on stablecoin issues with the SEC and CFTC responsible for more traditional oversight (such as clearing agency registration).

Presentation Takeaways continued



UK regulation

Digital assets fall within existing regime, but Treasury has consulted on whether further regulation is needed.



US tax

Convertible virtual currency is generally addressed under U.S. tax guidance but digital assets specifically are not.



UK tax

Cryptoassets are for UK tax purposes treated more like assets such as shares rather than cash.

Coronavirus COVID-19 Resources

We have formed a multidisciplinary **Coronavirus/COVID-19 Task Force** to help guide clients through the broad scope of legal issues brought on by this public health challenge.

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To help keep you on top of developments as they unfold, we also have launched a resource page on our website at www.morganlewis.com/topics/coronavirus-covid-19

If you would like to receive a daily digest of all new updates to the page, please visit the resource page to [subscribe](#) using the purple “Stay Up to Date” button.



Biography



Nicholas Moore

London

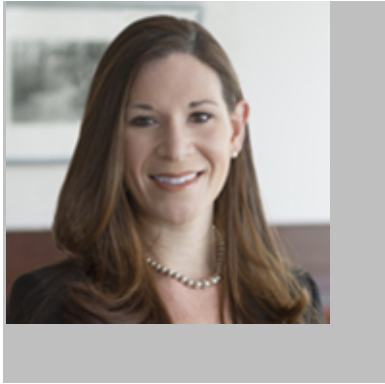
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Nick Moore's practice focuses on complex cross-border M&A, investments, joint ventures, strategic advice and corporate restructurings, with a particular focus on the fintech and TMT sectors.

His clients in the fintech sector include banks, investment banks and insurers, notably advising TSB on its separation from Lloyds, Williams & Glyn on its proposed separation from RBS and some of the largest ever transactions in the UK insurance market including the merger of Allied Zurich and Zurich Allies to create Zurich Financial Services and the acquisition by Swiss Re of GE's UK business.

Biography



Christine M. Lombardo
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Christine Lombardo advises investment managers and broker-dealers on financial regulatory matters.

She concentrates her practice on securities regulation for a broad range of financial firms including retail asset managers, private fund managers, family offices, broker-dealers, other professional traders, and high-net-worth individuals.

Christine also counsels legal, compliance, and business personnel on the structure, operation, and distribution of advisory programs, including digital advisory offerings, and investment products, including hedge funds, private equity funds, venture capital funds, real estate funds, and other alternative investment products.

Biography



Sarah V. Riddell

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Leveraging her experience as a lawyer at the US Commodity Futures Trading Commission (CFTC), Sarah V. Riddell advises domestic and foreign exchanges, derivatives clearing organizations, swap execution facilities, and other financial institutions on a broad range of regulatory matters, including CFTC registration and compliance.

Sarah also assists hedge fund clients with CFTC and National Futures Association (NFA) registration, compliance, and examination questions.

Biography



Steven Lightstone

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Steven Lightstone advises on financial services, securities, and derivatives regulatory issues.

His clients include asset managers across a wide range of asset classes and their funds, fintech firms, banks, broker-dealers, payment institutions, institutional investors, insurers, lenders, and market associations.

Steven is a founding member of the firm's fintech group and regularly contributes to the firm's fintech blog.

Biography



Sarah-Jane Morin

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Sarah-Jane Morin represents public and private companies, private equity funds, venture capital funds, real estate funds, portfolio companies, and alternative investment vehicles in the tax aspects of complex business transactions and fund formations, including domestic and cross-border investment strategies, sponsor investment strategies, limited partner investment strategies, mergers, acquisitions, integrations, buyouts, recapitalizations, debt and equity restructurings, and ongoing operations and tax compliance issues.

She also advises on international tax issues, including the tax aspects of offshore vehicles (CFC/PFIC/GILTI regimes), anti-deferral rules (Subpart F), withholding, cost sharing, and transfer pricing.

Biography



Kate Habershon

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Kate Habershon advises corporations and funds on corporate taxation. Her focuses include tax and structuring issues related to international tax planning, mergers and acquisitions, corporate finance, private equity, executive compensation, internal group restructurings, and financial products. Before joining Morgan Lewis, Kate was tax counsel in the London office of another international law firm, a solicitor on the international and energy tax teams of a Magic Circle firm, and a lawyer in the tax department of the Sydney, Australia, office of another international law firm.

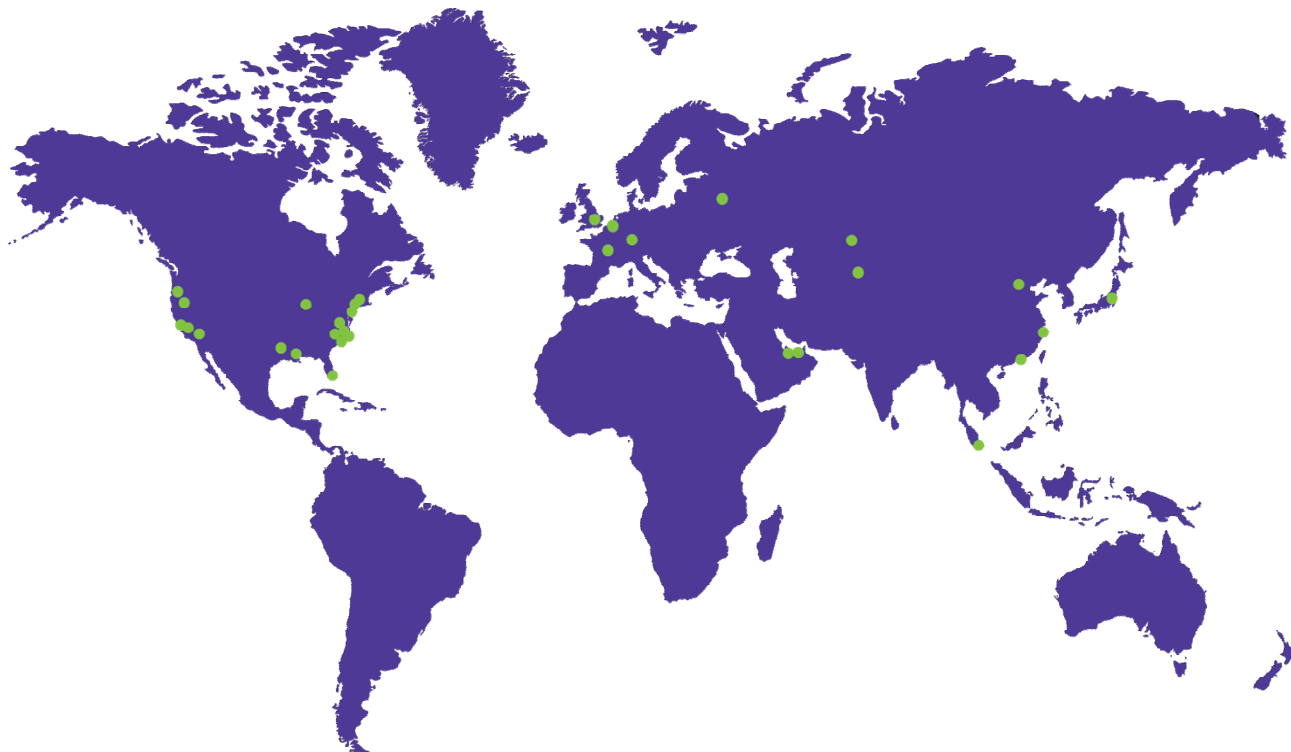
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