

## **THE CRYPTO EXCHANGE s04e8**

### **INSTITUTIONAL ADOPTION, TAX CHALLENGES, AND WHAT'S NEXT FOR CRYPTO IN THE U.S. — INSIGHTS FROM KPMG'S TONY TUTHS**

**Genna Garver:** Welcome to another episode of The Crypto Exchange, a Troutman Pepper Locke Podcast focusing on the world of digital assets. I'm Genna Garver, one of the hosts of The Crypto Exchange and a partner at Troutman Pepper Locke in our investment management and digital assets practice groups.

Before we jump into today's episode, please remember to visit and subscribe to our blogs, [consumerfinancialserviceslawmonitor.com](http://consumerfinancialserviceslawmonitor.com) and [troutmanfinancialservices.com](http://troutmanfinancialservices.com). Don't forget to check out our other podcasts on [troutman.com/podcast](http://troutman.com/podcast).

Today, I am joined by Tony Tuths, the Senior Partner and Leader of the Digital Asset Group at KPMG. We're going to discuss the latest on digital assets. Tony has more than 20 years of experience in tax structuring and advisory services for a broad range of asset management clients. He has worked extensively with the formation and operation of funds, trading a multitude of asset classes and strategies, including digital assets. Tony's group covers everything from development companies and foundations, blockchain infrastructure companies, exchanges, custodians, miners, non-validators, wallet providers, all the way through Fortune 250 companies who are beginning to use digital assets in their own business models.

For anyone looking to enhance their networking skills, Tony is the maestro of the craft. I've never seen anyone so seamlessly work a crowd, and he leaves a lasting impression wherever he goes. He's a great friend of mine. I'm so honored to have him here with us today. Tony, thanks for joining us.

**Tony Tuths:** Thanks for having me, Genna. Happy to be here. Yeah, I'm always happy to recommend my clients to Troutman Pepper as well. I love what you guys do. You give a lot of good guidance in the space, and so happy to be here today. Thank you.

**Genna Garver:** Awesome. We've been talking about crypto and digital assets for at least a decade. I think we're finally starting to get some congressional action with the GENIUS Act signed into law just a few weeks ago, and Congress continuing its work on the CLARITY Act bill. Now, it seems like everyone is focused on institutional adoption and we're seeing new partnerships announced in the press, like Coinbase and JP Morgan. It seems like, these press releases are flowing out of a fire hose. Tony, what are you hearing from your clients since the passage of the GENIUS Act? What are they hoping the pending CLARITY Act will bring? You can't say clarity.

**Tony Tuths:** Yeah, that GENIUS Act is a great first step forward, but it really obviously, just limited to stablecoins. Obviously, very much needed, because one of the things that this act does is it brings a lot of safety and stability to the stablecoin market. Prior to this legislation, at least in the United States, to be honest, anyone could issue a stablecoin. I could issue a stablecoin. One of these things that, it adds a little bit of rigor to the market, so you have to be an authorized issuer, you have to register.

Most importantly, your reserves have to be a specific type of high-quality cash, cash-like items. Those reserves have to be a third-party attested to, and they need an annual audit, third-party audit. Obviously, that puts a lot of stability around that market, it also, obviously, provides clear legislative framework for some of our regulated entities, so banking institutions, to come along and do that. They've been dying to do that. They just didn't have the legislative clarity to do it. I used the word clarity there. I didn't mean to. At least, that allows them to go ahead and do that.

We've already seen announcements by plenty of the large, very large financial institutions in America that are going to do that, as well as some non -bank institutions, which I found very interesting. You'll see that come about. As you were saying, what that's doing, right, spurring these partnerships. If you don't have the expertise, or the infrastructure inside to do it, perhaps you partner with a fintech player that does. I think we're also seeing a lot of M&A activity in the space. Obviously, for people who got caught behind, because this is going to happen very rapidly now following the legislation. And so, some banks have been preparing for this for years. They're ready to go.

Others, not so much. Maybe need to make an acquisition in order to make this happen in a timely manner. Definitely seeing that. That's all around the GENIUS Act. That's great stuff. By the way, the other thing we're seeing related to the GENIUS Act, it's not just stablecoin issuers, but payment routes and payment processors gearing up for the ability to do this in stablecoins. Again, some of them have already been preparing for that for years, so it should roll out fairly quickly, which I think is really interesting.

The other thing that you mentioned is the CLARITY Act, which passed the House, it's sitting in the Senate now. By the way, the Senate already had a framework that had worked up around the market structure for digital assets. Now, what they need to do is take the past GENIUS Act, compare it to their framework and try to integrate the two.

What's really interesting for me, as a wonky tax person operating in the spaces, the way that the CLARITY Act will work is that there's a split of authority between the SEC and the CFTC. Something is a security when it's not sufficiently decentralized, but later if it does become sufficiently decentralized and the issuer goes and makes a statement to the SEC and gets a clearance for that, it all of a sudden becomes a digital commodity and it's looked after by the CFTC, rather than the SEC. I have no idea how they figure out whether it's sufficiently decentralized, but be that as it may, I've been doing this a long time. I don't remember ever in the United States where a security could morph from one thing to another.

**Genna Garver:** I feel like I'm having some dog friend flashbacks with the SEC and the CFTC there. But yeah, I'm like, what's that moment in time? Like, how are you going to know that's happening? Oh, it just happens. Definitely not as clear as I would expect for something called clarity, right? There's so much to impact there. I think one big takeaway is that while, for many people out there, it might seem like nothing's been happening in the past number of years as what we saw the industry really go offshore, but things have been happening in this whole movement on the infrastructure and laying the pipes for when it does happen. I think we're really seeing that now with some of these partnerships and the acquisitions that you mentioned, and there's so much talk about rails.

I mean, it's actually funny. Literally like, oh, we already have the rails for this. It's just going to tack onto our rails. I think we'll see if that ends up being true. Obviously, there are a few existing businesses that would certainly be interested in that, not just your traditional things, but also credit card and other payment institutions that are certainly hoping that might be the case. As you said, we're going to see some non-banking institutions start to get in the game. Perhaps, some big retailers, you can certainly see how they might be looking to offer another payment option that might come with some rewards.

I keep hoping this, maybe this means something great for my personal bottom line and all of my shopping, but now I am also becoming a bit of a conspiracy theorist. I got something in junk mail from my credit card the other day and it was like, "Oh, raising your annual fee, but this is what you're going to get." I'm like, is this because of the GENIUS Act? Or am I just seeing ghosts?

I am messaging John D'Agostino over the weekend. I'm like, "Oh, this, this, that." He's like, "Relax. This is normal course. You probably got the same thing last year." I think we're all just really dying to know how our lives are ultimately going to change, because of all of this innovation and frankly, unleashing of the innovation with the legislation.

Before we move on, I just want to let everyone know, we did a implementation timeline for the GENIUS Act. Considering how much time I spent last week thinking about different shapes and colors, I hope people actually spent time to look at it substantively. It's not necessarily going to happen overnight, but it is happening and that give everyone a sense of the next steps that we need to really get the ball rolling on being able to use stablecoins in a permitted manner here in the US.

I think we're also working on a piece that compares the Senate's work on the crypto framework compared to the CLARITY Act bill. Just stay tuned for some of that were coming out, which will hopefully, give people some tidbits, as opposed to having to try to keep up, read everything, listen to everything. It's a lot going on.

**Tony Tuths:** To your bottom line, Genna, over time, and it will take time as you were just mentioning, but it should be beneficial to your bottom line. I mean, one of the reasons that

you're seeing the large retailers speak about issuing your own stablecoin is because for them, what's important is one, customer interaction and customer stickiness for sure. There's also, when most of their income comes via credit cards. When that happens, yes, the credit card is it charges a small fee, but the bank behind the credit card company charges what's called an interchange fee, and that's the bulk of that 2% to 3% charge that the retailer gets hit with, or has to pass on to their consumers. They want their own stablecoin to bypass that, so they don't have to pay that anymore. Hopefully, that would result in a lower price, to Genna, when she's shopping for Jimmy Choos.

**Genna Garver:** Well, first of all, Tony, everyone knows that my orthotics are not going to fit in Jimmy Choo's. Because I wear orthotics, we also know that I was around at the time when we had landlines, till dump is for that matter. We all thought, "Oh, cellphones. Like, I'm sure this means I won't have to pay for my long-distance calls anymore." Yeah, I guess, I'm just a little bit skeptical when it comes to innovation. I'm not so sure it's people like me who ultimately reap the benefits of that innovation, but –

**Tony Tuths:** That's true.

**Genna Garver:** Hopefully, this time it's true. I mean, I also cut the cord from my cable, and I'm not sure that helped me either. Hopefully, this time it will be different. There is a lot happening. In last week, again, so much more, we had SEC Chair Atkins announce this Project Crypto, which, I guess, is going to enable American financial markets to just move on-chain. That announcement comes on the heels of a report released by the president's working group on digital asset markets. I guess, that report is just really directing financial agencies to build a framework to maintain US dominance in crypto asset markets. I mean, I don't know if it's just maintaining it, or establishing it and now maintaining it. Can you tell us a bit more about that report, and if you think regulators will in fact be able to entice industry participants back on shore?

**Tony Tuths:** Yeah. What ended up happening there, people may not even remember because it happened so fast, but immediately after the election, President Trump signed an executive order telling his Crypto Task Force to please come up with recommendations. This report that

you mentioned that came out last Wednesday is the result of that. It makes a number of recommendations. By the way, they're only recommendations. They don't tell people to do things, but they do make recommendations both to Congress, as well as to some of the regulatory agencies, including SEC, CFTC, and Treasury, to be precise. There's a few others in there for the little detail bits, but those are the main ones.

Immediately after that happened on Wednesday, like you said, on Thursday, the SEC announces its Project Crypto, which is really just telling all of its people, "Hey, this is what we need to do." By the way, it's fascinating to read the prelog to that that, because Chair Atkins, I mean, it's so different than the last SEC. Chair Atkins is saying, "We will be the crypto capital of the world. We're trying to make a pleasant environment for our players in the digital asset space, so it's just amazing to see." Then right after that, on Friday, the CFTC announced what they call their crypto sprint, which just began implementing the crypto-related recommendations in that report.

The report itself calls for several changes. One is for, to create a market structure, and I think we already did show how fast things are moving. That's already happened. That's the CLARITY Act, right? It's already there. It's already in process. There's another section that calls for banking services to the industry and what to do, what not to do, kind of thing. That is really obviously in response to the operation choke point that people claimed was in the market. I mean, maybe it was, maybe it wasn't, but obviously, not today, but it does go into that.

There's another portion, of course, about stablecoins and payments, but again, already done, GENIUS Act. There is another section that I find a little bit troubling, a little bit concerning, which is countering illicit finance, so AML, CFT, sanctions. That section calls for Congress to consider changes to the Bank Secrecy Act, specifically calling out some of the difficulties that we have with DeFi. That's interesting. Every time Congress, or even Treasury has tried to do something with DeFi, amazing amounts of pushback, mostly because the tech culture folks that are out there just can't wrap their heads around the fact that they might create a piece of software that then creates this reporting framework, or causes the government to get involved in what's happening merely because they created software.

I know it sounds silly, but this has to happen, because Treasury in the US, administration finds themselves trapped. They want to create this playground where the blockchain folks can go ahead and build all this fascinating stuff that moves money around the world in a second. For pennies, great. Great innovation. They want to keep that going. At the same time, you can't have a system where somebody within the United States can take a large amount of money and move it in a second to a bad behavior person somewhere in the world, and there's no checks or balances on that. I mean, you just can't have that. How do you balance those two? It's not easy.

By the way, in the report in that section, it doesn't come to any conclusions, as you might imagine. It just says, this is a problem. Someone ought to focus on it. It does call on Treasury and FinCEN and others to work together to solve this issue, but it's just a hard one to crack. It'll be very interesting to see where that calls out.

**Genna Garver:** Yeah. Actually, I think what surprised many of us is the GENIUS Act has quite a runway for AML rules around stablecoin issuers, almost like three years. I mean, that's very interesting to think that all of this could be happening for three years, while we try to figure it out. It's certainly not a new issue. I mean, we are in the private fund space and deal with a number of different AML jurisdictions. As you know, I mean, not just in the US, but certainly, we've seen jurisdictions that decades ago, who, perhaps, had trouble implementing good rules and now are more gold standard in this space, like Cayman. We've certainly seen improved their reputation in this space.

I just think we haven't, for whatever reason, then focused on that. I do hope now we can move forward quickly. I think a lot of our clients, I'm sure you've heard this too, that were trying to engage in digital asset management, had enough obstacles with the SEC and the CFTC, but it definitely felt like there was more pushback coming from somewhere else, which was likely Treasury all of these years. Because just a problem that really does need a solution to continue with markets that have integrity and predictability. I do hope that we can get our act together.

We are going to have our Troutman partners that are focused on AML to podcast with us in the coming weeks. Hopefully, they will have some more insight as to what's to come. I do think that is still probably the biggest issue that's holding back innovation and adoption in particular.

**Tony Tuths:** Yeah. I think you're right. It's amazing to me that the US is willing to not only allow blockchain transfers of wealth internationally, but then to go ahead and make specific legislation to entice that activity, all while they know, we don't have any AML protections built in yet. I guess, part of the reason for that is, well, blockchain already existed, tokens already existed, you can't put the genie back in the bottle, so you might as well do what you can.

By the way, Treasury to its part did try in the last Trump administration, in that tax reform act was a change to section 6045, which is our 1099 reporting piece. What they tried to do, because the problem that AML has is the same problem that tax has, which is for years and years and years, if you wanted to send money to somebody, you went to a bank. The government could always go to the bank and say, "You need to check this, this, and this before you send the money." Now, I don't need a bank so there's no one to do that anymore.

By the way, the other thing that the government would do is they go to the bank and they'd say, "When you go to transfer that money, see if it's subject to US withholding tax. If it is, you have to withhold the tax." They were withholding it again. Well, now I've got peer-to-peer people moving money around, I don't have a withholding agent and I don't have an AML KYC checker. We have the same problem. In that tax act, they changed the rule to require everybody, just not everybody, but most people, that sends money in a commercial manner on blockchain to please collect the forms and do these checks. Please. It's a please.

By the way, that is how it turned out, because in the conclusion, what ended up happening, Treasury wrote final regulations for this and they split them into two pieces; one for custodial brokers and one for DeFi. Problem is now in the second Trump administration, they used the Congressional Review Act to pull the DeFi part. Yes, now all of your custodial brokers will do these checks and they will look for withholding. We can use them in that bottleneck scenario to do this work for us. DeFi still runs wild. You can still do peer-to-peer and there's no answer for that.

**Genna Garver:** Right. It really is running wild. It's pretty much absent from the GENIUS Act. I think there's certainly a lot of work still to do. I mean, we just saw literally, on the heels of the



GENIUS Act, a FinCEN rolled back the investment advisor AML rules that it took at least four attempts over decades, it seems, to even get a final rule. Now, they're at least anticipating that they're going to delay it years and perhaps, narrow the scope. It is hard to get our heads around moving forward here, pulling back here, but that's where we need it. There's just quite a lot to keep up with, and it's going to be interesting to see how this shakes out.

Do you think that we are at this stage yet, where we're finally doing enough to allow institutional players to come in and feel comfortable in this digital asset arena, or is there's just still more for us to do?

**Tony Tuths:** You're already seeing it. Like you said, we already saw a number of large banking institutions make the announcement last week, or the week before that they're going to issue a stablecoin. You're seeing large custody banks executing on their digital asset custody solutions. They've been working on this for years, by the way. They've been dying to do this, so they were just waiting for this. All they really need now is the CLARITY Act to pass. People might not have noticed, because it's a little under the radar, but the Fed, FDIC and the OCC all put out statements over the past several months saying that their regulatory oversight would allow their institutions to deal in digital assets. They have all the clarity they'd need, except for the CLARITY Act. That hopefully will pass in the fall. Yes, you will see every large custody bank in the world will custody digital assets.

By the way, the reason I'm so certain about that is because what you're seeing behind the scenes at the large financial institutions is they've all, for years now, they've been working on it for years, building out their own internal Blockchain capabilities, because every asset in the world will move on blockchain. You mean, I know it. You won't see it. You won't feel it. It's the things that happen in the background, but they're all going to be on blockchain, which means they might not call it tokens, but they are tokens. They need to be able to custody these assets. They're all working on that. They're waiting to do that.

We've also seen recently, some asset management firms announced the intent to allow their customers to trade digital assets in the regular account, the regular security account. Again, what's happening there, you don't see it. It's in the plumbing. But when you look at your account

statement at your asset manager, you'll see your Bitcoin and ETH and Solana right there alongside your stocks and bonds and other things. What you don't know is that, well, some of those assets are being held in DTC regular way, and other what other ones are in a digital wallet, because they're on blockchain. It's on the same state, and so you feel great about it. That looks great.

What I'm waiting for is the day when financial advisors at these large financial institutions actually recommend an allocation of portfolio to digital assets, because that's a big difference, right? It's one thing to say, "Hey, my customers are allowed to treat it that they want to treat it." But for me, to recommend it. Now, we have this other issue, that's you have a fiduciary issue to your customers. It'd be interesting to see if that happens. But to answer your question, yes. I think we are doing all the right things and I think we will be there before the end of the year. We'll be in a position where, yes, large financial institutions can hop into this space.

Part of your last question was some of the participants in this area had moved offshore during our last administration, and do we have what we need to bring them back on shore? I think, yes. Because one of the things we – Troutman was selling them, was sure, you can move offshore, but that doesn't do anything really to help you, because if you still want to sell into the US market, you still have to be compliant. You can't just leave the country and feel like you don't have rules. Obviously, the US market's the largest in the world, so yes, they do want to be involved. Now with regulatory clarity, yeah. I mean, clarity and stability is valuable. Yes, they will come back on shore. We're already seeing that amongst our clients.

**Genna Garver:** Tony, before we wrap up, I just want to go back again to the President's working group report. I believe, there were some tax items in there. You want to tell us about that?

**Tony Tuths:** Yeah, there were absolutely, there were several recommendations for tax changes. Some were recommendations to the IRS and Treasury. Some were recommendations to Congress. But they ran through, basically, litany of holes in the Tax Code with respect to digital assets. A lot of this was taken from, there was a Senate Finance Committee paper that went out to the public asking for comments. Some of these came from that. Some of it also

came from a report that was put out by the JCT in 2023. Same items. There's just these gaping holes, where people don't know how to treat digital assets.

It ran through some of the big ones anyway. One of them was the Corporate Alternative Minimum Tax. Doesn't apply to very many taxpayers, but it does apply to a couple of the large publicly traded digital asset players. The reason there is that corporate alternative minimum tax plays off of gap income. That's how it arrives to the taxable income number. That was fine for a while. Now FASB changed the accounting rule to say, well, digital assets, if they're public, they're traded, they mark to market. You could have a large mark to market game. There's no real income, and all of a sudden, they're subject to tax. They're trying to fix that, and you know who those players are out there that have a ton of Bitcoin on their balance sheet.

Then, also, they asked Treasury to provide guidance for staking inside a grant for trust. The reason that that is so important is because the large ETFs, the Bitcoin and the ETFs that we already have in the US, on the ETTF, they want to stake the assets. The SEC has come out recently and said, "You can do that." Well, that's great. The Treasury has not come out and said, "You can do that," because you're not allowed to do that in a fixed investment trust. That's what that was going to. Hey, someone's got to fix that problem.

Also, really basic question. On-chain, you sometimes take an asset like ETH and you wrap it, so that you can trade it on a different network. I don't know, when I wrap things and unwrap them, is that taxable? I have no idea. It's ask treasury, can you fix that? It also asks for to fill in a lot of nuts-and-bolts gaps, like section A64, which is great for our funds. Our funds when they trade digital assets inside the US and they have offshore investors, and they all do, does that create a US trade or business? Well, there's a protect, there's a safe harbor for that for stocks and commodities, but I don't have one for digital assets. They try to fix that. 475 mark to market, 1058 with your securities lending, 7704, which is our publicly traded partnership rules, wash sale rules, constructive sale rules, all that kind of stuff.

What should be the answer for digital assets in those places? It calls for legislation on that, because that's not a regulatory fix, and I need law for that. Then the other one which I thought was very interesting to call this out, which was for stablecoins, you wouldn't normally care about

stablecoins and tax, right? This is always worth the dollar. Who cares? Well, I'm not going to have gains and losses, at least I shouldn't. But it does call out the fact that if you didn't do anything else you ask the tax lawyer, what is a stablecoin for tax? They would probably have to conclude it's a dead instrument. It doesn't pay any interest. But you gave me a dollar, I owe you a dollar back. It's a dead instrument.

They do point out that that calls into question. We have a rule in the United States against bearer bonds. I mean, that hasn't been an issue for over 100 years, but maybe less actually. So, we don't have bearer bonds anymore. The reason is it's for the prohibiting, but that's really what a stablecoin is, it's a bearer bond. It doesn't pay any interest, so maybe you don't care. But they call that out and they say, there's a bunch of issues to fix around the stablecoins. Which, also, by the way, they don't recognize it explicitly, but it also goes into the reporting, this 1099DA reporting. Why on earth does it apply to stablecoins? We're not going to have gains and losses. If you are, it's going to be de minimis. But yet, they make us do 1099DA reporting, which ridiculous. Hopefully, they'll fix that, too.

The other one which I know is big with all of our customers is mining and staking with the timing of the income. The IRS put out Revenue Ruling 2023-14 saying, they believe you're taxable at the time you receive the staking reward. But the industry does not believe this. Our mining companies definitely don't believe this. It does ask Treasury to review that revenue ruling and think twice about that. Like I said, in this report, they don't tell government agencies what to do, but they definitely did recommend harshly and maybe they want to review that.

Then some other things in there related to reporting of foreign assets and foreign financial accounts, what does FinCEN say about, hey, usually, US people have to identify their foreign accounts and tell the government that they have them. We don't have that here. Obviously, that needs to be fixed in some way, shape, or form. The other thing that's really super interesting if you're a tax wonk is it actually tells Treasury to prepare to adopt CARF, which is the Crypto Asset Reporting Framework that the OECD put out. That's interesting only because in other areas of tax, the US has been pushing back against OECD recommendations, and we're not joining in with the rest of the world on some of these other items. On this one, they seem to say, "Okay, we're going to do it." Very interesting. Lots of tax stuff in here.

I would expect over the next year or so for Treasury to start moving fairly rapidly to try to address some of these, and hopefully, we'll get a legislation, too. There is a bill floating around Congress right now, but it needs a vehicle to attach to in order to get passed, but it contains several of these items.

**Genna Garver:** Okay. Yeah. There is so much. I think it really underscores the need for industry participants to be involved in the legislative process, and providing good feedback to regulators whose primary gig is not necessarily in the space and they would not otherwise be able to flag these concerns and literally fill the holes, without that feedback from the industry. Hopefully, there are enough staff members available, who can dedicate their time and attention to fixing these issues, so you can move forward towards a broader adoption without unknown contingencies hanging out there.

Tony, thank you so much for joining me today. Thanks to our audience for listening to our episode. Please don't forget to visit our blogs and subscribe, so you can get the latest updates. Please, also make sure to subscribe to this podcast via Apple Podcasts, Google Play, Stitcher, and whatever platform you use. We look forward to our next episode.

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