



June 16, 2023

VIA Federal eRulemaking Portal

Internal Revenue Service
Attn: CC:PA:LPD:PR (Notice 2023-27), Room 5203
PO Box 7604
Ben Franklin Station
Washington, DC 20044

Re: Notice 2023-27, Treatment of Certain Nonfungible Tokens as Collectibles

To Whom it May Concern:

Blockchain Association (the “Association”) submits this letter in response to the request for comments of the Treasury Department and the Internal Revenue Service (collectively “IRS”) set forth in Section 3 of Notice 2023-27 (the “Notice”) titled “Treatment of Certain Nonfungible Tokens as Collectibles.”

The Association is the leading nonprofit membership organization dedicated to promoting a pro-innovation policy environment for the digital asset economy. The Association endeavors to achieve regulatory clarity and to educate policymakers, regulators, courts, and the public about how blockchain technology can pave the way for a more secure, competitive, and consumer-friendly digital marketplace. The Association represents over 100 member companies reflecting the wide range of the dynamic blockchain industry, including software developers, infrastructure providers, exchanges, custodians, investors, and others supporting the public blockchain ecosystem.

The Association writes to express its general support of the Notice’s articulation of the concept of a Nonfungible Token (“NFT”), subject to certain qualifications. The Association further writes in support of a look-through analysis for evaluating the extent to which ownership of an NFT may indicate ownership of a collectible for purposes of Section 408(m) of the Internal Revenue Code (“Section 408(m)"). As discussed in detail below, however, the Association believes that the Notice fails to recognize that, as Congress enacted Section 408(m), the term “collectible” includes only *tangible* assets, thereby excluding any digital asset with ownership denoted by an NFT, or an NFT itself, from the definition of collectible.

At the outset, the Association commends the IRS for its issuance of the Notice and for the manner in which the Notice contributes to open communications between the IRS, interested parties, and the general public. In the Notice, the IRS explains its current understanding of the topic and identifies aspects of that topic about which the IRS might harbor uncertainty; states clearly its intent to issue future guidance on that topic; and invites input as to how that future guidance should look. The Association believes the IRS’s initiative to solicit industry and expert perspective prior to proposing guidance in this highly technical and dynamic industry will benefit both the agency and the public. The Association appreciates this process and encourages the

IRS – and indeed all governmental bodies – to approach future regulatory matters in a similar way.

The Association offers the following comments in response to the Notice:

I. While Mostly Appropriate, the Notice’s NFT Definition Provides Inconsistent Signals and has the Potential to Inappropriately Apply to Contexts Outside of Section 408(m).

The Association believes that the definition of “NFT” set forth in the Notice (“a unique digital identifier that is recorded using distributed ledger technology and may be used to certify authenticity and ownership of an associated right or asset”), as a general matter, represents a workable definition for the purpose of considering the possible interaction between NFTs and Section 408(m). The Association further believes that the Notice’s definitions of “distributed ledger technology” (using “independent digital systems to record, share, and synchronize transactions, the details of which are recorded simultaneously on multiple nodes in a network”) and “token” (“an entry of data encoded on a distributed ledger”) also assist in analyzing the potential applicability of Section 408(m) to situations involving NFTs.

The Association, however, wishes to add two points of caution.

First, the Association urges the IRS to recognize that, at the present time, the guidance which the IRS contemplates issuing addresses a relatively narrow slice of the Code. The Association further urges the IRS to recognize that NFTs represent a relatively new technological innovation, which continues to develop and evolve. For these reasons, the IRS should avoid adopting far-reaching definitions (at least without explicitly limiting the reach of those definitions) which the Association believes may then be inappropriately used (based on the fact that such definitions might be the only definitions then in existence) to analyze situations different from the Section 408(m) issue currently under discussion. To the extent that the guidance the IRS issues on this topic includes a definition of NFTs,¹ the guidance should clearly limit the applicability of that definition to that guidance.

Second, the Notice’s inclusion in its definition of NFTs of the phrase “may be used to certify authenticity and ownership of an associated right or asset,” while technically correct, carries with it the potential to create confusion and uncertainty. The confusion stems from the Notice’s discussion, in Section 3, of the “look-through analysis” pursuant to which the IRS intends to look to “the NFT’s associated right or asset” to determine whether Section 408(m) applies to the NFT. The Association reads Section 3 of the Notice as suggesting that the IRS believes that each and every NFT always involves “an associated right or asset.” That suggestion, however, contradicts the Notice’s earlier statement that an NFT “*may* be used to certify authenticity and ownership of an associated right or asset.” This inconsistency can cause uncertainty as to what the IRS believes NFTs to be. Moreover, to the extent that a particular NFT may not involve an associated right or asset, the Notice does not address how the IRS would treat such an NFT for purposes of Section 408(m). Any guidance issued by the IRS should remove the internal inconsistency which characterizes the Notice’s discussion of NFTs.

¹ See discussion in Section IV, in which the Association suggests alternative ways in which the IRS might approach defining NFTs (including not defining NFTs) for purposes of the forthcoming guidance.

The Association suggests that the IRS address this inconsistency by stating clearly that (1) its Section 408(m) guidance applies only to NFTs that certify ownership of an associated asset and (2) such NFTs do not necessarily represent the entire universe of NFTs. Stated differently, before the IRS even gets to the “look-through analysis” discussed in Section 3, it must first determine that the NFT at issue is the type of NFT (i.e., an NFT that certifies ownership of a tangible asset) to which Section 408(m) might apply.

II. NFTs Alone are not Collectibles, Rather it is the Underlying Physical Item that Could Constitute Acquiring a Collectible.

The Association agrees that, for those NFTs which carry with them an associated right or asset, Section 408(m) should apply if “the NFT’s associated right or asset is a section 408(m) collectible.” The Association concurs that Section 408(m) applies where an NFT certifies ownership of a gem and that Section 408(m) does not apply where an NFT provides a right to use or develop a plot of land in a virtual environment.

With reference to the gem example, the Association does *not* agree that the term “collectible” applies to *the NFT* that certifies ownership of the gem. Where the physical item (such as a gem) constitutes a Section 408(m) collectible, the fact that an NFT certifies ownership of that item should not allow the item to escape characterization and treatment as a collectible. But, an NFT is simply a recording of the ownership of the underlying asset. Thus, it is not the NFT that is the collectible and it is not the ownership of the NFT that causes the owner to have acquired a collectible. Rather, it is ownership of the physical item (which the NFT merely certifies) that causes the owner to have acquired a collectible. The guidance should be careful not to conflate the two concepts.

III. The Notice Fails to Recognize that Section 408(m) Applies Only to Tangible Personal Property.

The Association respectfully believes that some of the statements in, and questions raised by, the Notice incorrectly assume that Section 408(m) can characterize an item of intangible personal property as a collectible when, in fact, Section 408(m) in its present form limits the definition of “collectible” to tangible personal property. Section 408(m)(2), in subsections (A) through (E), lists eight (8) specific items that constitute collectibles for purposes of Section 408(m): works of art, rugs or antiques, metals or gems, stamps or coins and alcoholic beverages.² Section 408(m)(2)(F) then adds to the list “any *other* tangible personal property specified by the Secretary for purposes of this subsection.” The use of the word “other” before “tangible personal property” in subsection (F) indicates that the preceding items, listed in subsections (A) through (E), themselves constitute “tangible personal property.” Compare IRC § 48C(c)(1)(A)(ii)(I) through (IV) (listing in (I) through (III) specific types of industrial technology designed to reduce greenhouse gas emissions and concluding with “(IV) any other industrial technology designed to reduce greenhouse gas emissions, as determined by the Secretary”); IRC § 9816(b)(2)(A)(ii)(I) through (V) (in definition of “health care facility” relating to a group health plan or health insurance coverage, listing in (I) through (IV) a hospital, a hospital outpatient

² Section 408(m)(3), however, exempts from the term “collectible” certain coins and bullion.

department, a critical access hospital and an ambulatory surgical center and concluding with “(V) Any other facility, specified by the Secretary, that provides items or services for which coverage is provided under the plan or coverage, respectively”).

a. NFTs Themselves are not Collectibles.

An NFT is intangible.³ An NFT is intangible whether the NFT has value because it certifies authenticity or ownership of an associated right or asset, or the NFT has value due to an embedded feature from which its owner might derive value separate and apart from an underlying right or asset.⁴ Accordingly, an NFT in and of itself can never constitute a collectible under Section 408(m). As stated above, when an NFT certifies ownership of a physical (*i.e.*, tangible) item listed in subsections (A) through (F) of Section 408(m)(2), then a collectible is involved, not because the NFT itself constitutes the collectible but because the tangible item, the ownership of which the NFT certifies, constitutes a collectible. For this reason, the Association respectfully points out that the title of the Notice, “Treatment of Certain Nonfungible Tokens as Collectibles,” is misleading and likely to sow confusion. Any guidance issued by the IRS should avoid terminology that suggests that, under current law, an NFT can constitute a collectible.

b. Digital Files are Intangible and Therefore are not Collectibles.

Recognizing that Section 408(m) confers collectible treatment only on tangible personal property provides answers to some of the questions set forth in the Notice. Specifically, after having stated in Section 2 that “[o]wnership of an NFT may provide the holder a right with respect to a digital file (such as a digital image, digital music, a digital trading card, or a digital sports moment,” the Notice asks in Section 3 (question 3(a)), “What factors might be considered to determine whether a digital file constitutes a ‘work of art’ under section 408(m)(2)(A)?” The Notice also asks in (Section 3, question 3(b)), “What factors might be useful to determine whether an asset is ‘tangible personal property’ under section 408(m)(2)(F), particularly in the context of digital files?”

The Association respectfully suggests that because a digital file is intangible, a digital file, under present law, cannot constitute a work of art under section 408(m)(2)(A), nor can a digital file constitute “any other tangible personal property” under section 408(m)(2)(F).⁵

³ The IRS recognizes that “intangible property includes, but is not limited to, any commercially transferable interest in . . . [c]omputer software. . . [and] [m]ethods, programs, [and] systems.” IRM 4.48.5.1.1(1). The IRM also regards as “intangible property” any other items “similar” to items listed in 4.48.5.1.1(1) and states that “[a]n items is considered similar if it derives its value not from physical attributes, but from its intellectual content or other intangible properties.” *Id.* at 4.48.5.1.1(2). See also *id.* at 4.48.3.1.1(1) (“[t]angible personal property includes items such as vehicles, antiques, silver, artwork, collectibles, furniture, machinery, and equipment. Tangible personal property is anything other than real property or intangible personal property which includes items such as patents, copyrights, stocks, and the goodwill value of a business”).

⁴ For example, an NFT that serves as a ticket to an event may, because of historical or cultural interest in the event, have some value long after the event has ended.

⁵ “At a high level of abstraction, a digital or computer file is a stored segment or block of information that is available to a computer program.” Glossary, Federal Agencies Digital Guidelines Initiative (<https://www.digitizationguidelines.gov/term.php?term=digitalfile#>).

IV. The Association Recommends that the IRS Consider Issuing the Guidance without Establishing a Definition for NFTs or, at a minimum, Clarify that the Definition of NFT has no Applicability in any Context other than Section 408(m).

As mentioned above, the Association believes that the IRS should give serious consideration to issuing guidance as to the intersection between NFTs and Section 408(m) without actually establishing a definition for NFTs. The Association respectfully suggests that using this guidance to articulate such a definition could have unintended and undesired effects on the industry and taxing authorities. Instead, the IRS could promulgate effective guidance by stating the general rule to be something along the lines of the following: in those situations involving ownership of a unique digital identifier consisting of data encoded on independent digital systems to record, share, and synchronize transactions, the details of which are recorded simultaneously on multiple nodes in a network, when the unique digital identifier is used to certify ownership of an associated right or asset, ownership of the identifier will be treated as ownership of a collectible for purposes of Section 408(m) if the associated right or asset falls within the definition of collectible set forth in Section 408(m)(2).

Alternatively, if the IRS feels that it should define NFTs in its forthcoming guidance, then the guidance should clarify that the IRS does not intend the definition to have applicability in any context other than Section 408(m). Stated differently, the guidance should identify the purpose and scope of the guidance as determining that Section 408(m) covers those collectibles (as defined in Section 408(m)(2)(A) through (F)) as to which ownership is certified by an NFT and that Section 408(m) does not apply to assets as to which ownership is certified by an NFT if the assets themselves do not fall within that section's definition of "collectible."

The Association believes that if the IRS adopts the above-stated approach, most of the questions posed in the Notice will resolve themselves. Specifically, with respect to Section 3, question 2(c), if an IRA acquires an NFT which certifies ownership of "more than one associated right or asset," one of which "is a section 408(m) collectible but another one is not," then the IRA has acquired a collectible with respect to the associated right or asset that is a collectible but has not acquired a collectible with respect to the associated right or asset that is not a collectible. With respect to valuation of the collectible portion of the transaction, IRS guidance on this issue should permit the use of any reasonable valuation or allocation method consistently applied. See, e.g., Treas. Reg. § 1.199A-10 (allocating COGS based on any reasonable method); Treas. Reg. § 1.412(c)(1)-2 (valuation of plan assets based on reasonable valuation method).

With respect to Section 3, question 3(c), if an NFT certifies "less than full ownership of an asset" that is a collectible, the IRA acquiring that NFT has acquired a collectible if and only if, and only to the extent that, the "less than full ownership" of the item confers upon the IRA a property right sufficient to allow the conclusion that the IRA has "acquired" the item within the meaning of "acquisition" of section 408(m)(1). The Association believes that, for purposes of Section 408(m), an IRA has not acquired a collectible unless it obtains full ownership of the collectible.

With respect to Section 3, question 2(d), if the IRA acquires an NFT which confers upon the IRA the potential to receive additional rights or assets, the IRA has not acquired a collectible unless one of the "additional rights or assets" is the right to obtain in the future an asset that

qualifies as a collectible under section 408(m)(2) and, even then, not until the IRA actually obtains ownership of the item.

V. Conclusion.

The Association reiterates its appreciation to the IRS for its issuance of Notice 2023-27 and for the opportunity to provide these comments. The Association also reiterates its support for the general principle that the IRS should provide appropriate guidance on the application of the Internal Revenue Code to the digital asset and blockchain technology space. The Association cautions that, when formulating such guidance, the IRS be mindful of the danger of defining terms too broadly or imprecisely and issuing rules or regulations that might cover, or appear to cover, situations beyond those which the IRS intends to cover when it issues the guidance. The Association also respectfully reminds the IRS that the guidance it issues must be consistent with the Code.

Should the IRS wish to discuss any of the issues raised in this letter, or any other issue related to NFTs, digital assets, or the application of tax laws to any use of blockchain technology, the Association remains willing and eager to participate. Thank you for your consideration.

Respectfully submitted,



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