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On behalf of Fidelity Investments

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Hearing on "Making America the Crypto Capital of the World: Ensuring Digital Asset Policy Built for the 21st Century"

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Fidelity Investments - Who We Are

Chairman Schweikert, Ranking Member Sewell, and Members of the Subcommittee, thank you for the opportunity to testify today about the critical topic of digital assets tax policy. We also appreciate Chairman Smith and Ranking Neal's focus on this issue. My name is Sarah Reilly, and I am Senior Tax Counsel at Fidelity Investments based in Boston, Massachusetts. Thank you for the opportunity to appear before you today and to share Fidelity's perspective on digital assets and the importance of implementing a modernized tax framework.

For over 75 years, Fidelity has been "customer obsessed." Where our customers are committed to investing, we build solutions to support them and believe a customer-centric regulatory model is critical. As of the end of Q1 2025, we have nearly $6 trillion in assets under management (AUM) and are one of the country's leading workplace benefits providers and America's largest IRA provider.

Fidelity offers a unique perspective in the digital asset space. As one of the only established, large financial institutions in the digital asset ecosystem, we are a bridge between traditional finance and digital assets.

We began research and development on digital assets in 2014 and have offered custody and trading of Bitcoin since 2018 to support our institutional customers' needs. Three years ago, we launched Fidelity Crypto for retail investors, which provides custody and trading of Bitcoin, Ethereum and Litecoin. In 2024, following SEC approval, we launched two exchange-traded products: the Fidelity Wise Origin Bitcoin Fund (FBTC), now with approximately $21 billion in AUM and the Fidelity Ethereum Fund (FETH), with approximately $1.3 billion in AUM. These products provide greater optionality and ease of access for our customers who wish to have investment account exposure to digital assets.

Our commitment to digital assets is firmwide. We believe blockchain technology and digital assets will play a transformative role in the future of finance. Similar to other pivotal technological advances, such as the internet, this technology is an integral part of the evolution of the financial sector. But for that future to be realized, we need a clear, fit-for-purpose regulatory framework—one that fosters innovation, reflects the unique attributes of digital assets, and, above all, protects investors.

We are encouraged by the recent progress in Congress toward establishing such a framework. While legislation addressing market structure and stablecoins is essential, tax policy must also evolve to avoid becoming a barrier to innovation and adoption.

Why Crypto Tax Legislation is Needed

While digital assets may share characteristics with other types of assets, digital assets are distinguishable in ways that necessitate change to the existing tax framework. Digital assets exist solely digitally and have unique considerations when it comes to activities such as staking or mining. The breadth of use cases for digital assets are more expansive than traditional securities or commodities, with digital assets being used for payments for goods and services, for investments, for governance, and for decentralized finance applications.

The crypto industry urgently needs clear, definitive tax rules. In the absence of comprehensive guidance, taxpayers and institutions are left to rely on general tax principles and

sub-regulatory guidance. This uncertainty has real consequences:

- It undermines taxpayer confidence,
- It results in inconsistent taxpayer outcomes,
- It makes compliance more challenging, and
- It pushes innovation offshore—for example, ambiguity around the sourcing of digital asset staking rewards has already led to a significant shift of staking activity outside the U.S.

A modern regulatory framework is not complete without a modernized tax code. To support the growth of the digital asset ecosystem—including stablecoins and decentralized finance—tax rules must keep pace with technological innovation.

Most tax code provisions were written before the broad adoptions of (and therefore without contemplating) digital assets. The tax code has not been updated to address the tax treatment of digital assets. Tax legislation is needed to both update existing tax code sections that should address digital assets and deal with novel concepts in the digital asset space. In many instances, digital assets face disparate treatment as compared with traditional investment assets (like securities and commodities) despite the growing role of digital assets in our financial system. The inconsistency in tax treatment under various tax rules results in adverse outcomes for taxpayers and the industry overall. Additionally, modernization of the tax code would support increased compliance and reduce abuse. To better support the industry, certain provisions should be updated to specifically address digital assets.

Overview of Digital Asset Taxation Under Current Rules

Under current IRS guidance, digital assets are treated as property for U.S. federal income tax purposes.[1] Generally, this means that any transfer, exchange, or other disposition of digital assets can trigger taxable income. Such treatment as property is consistent with the taxation of securities and commodities but differs from the tax treatment of currency. Under general tax principles, whether income from digital assets is capital gain or ordinary to given taxpayer depends on facts and circumstances – e.g., digital assets held for investment generally generate capital gain upon disposition, while digital assets received for goods and services generally generate ordinary income.

A couple of examples help illustrate[2]:

- Taxpayer A purchases Digital Asset X for $100. Taxpayer A has a tax basis of $100 in the digital asset. After two years, Digital Asset X has risen in value to $200. Taxpayer A then purchases $200 of Digital Asset Y in exchange for their $200 of Digital Asset X. Taxpayer A realizes $100 of taxable long-term capital gain and takes a basis of $200 in Digital Asset Y.
- Taxpayer B has $100 of Digital Asset X with a tax basis of $50. Taxpayer B pays Taxpayer C for services with the $100 of Digital Asset X. Taxpayer B realizes $50 of taxable gain (whether short-term or long-term will depend on their holding period). Taxpayer C realizes $100 of ordinary income and takes a tax basis of $100 in Digital Asset X.

[1] IRS Notice 2014-21.
[2] For simplicity, these examples do not account for transaction fees.

General tax principles are helpful but cannot fully address the full scope of new challenges and complexities introduced by digital assets as compared with other assets taxable as property. For example, rewards from mining[3] and staking[4] differ from other types of income and existing guidance is insufficient for taxpayers.[5] As discussed further below, the tax treatment of these activities and income generated creates novel tax questions, including but not limited to how such rewards are sourced. Other unique issues include, but are not limited to, air drops and forks.[6]

Additionally, the use cases for digital assets are more expansive than other types of property, such as securities and commodities. In addition to being held for investment, digital assets can be used in many other ways, including but not limited to in the ordinary course of business, in personal transactions, in decentralized finance applications, and in other financial transactions. The varied types and uses of digital assets necessitate thoughtful and tailored tax rules that address these unique considerations.[7]

Specific Tax Issues

Staking

Staking is essential to the integrity, security, and success of blockchains utilizing proof-of-stake consensus mechanisms. Despite the importance of staking, the Code has not been updated to address staking and existing sub-regulatory guidance (e.g., Rev. Rul. 2023-14) is insufficient to address all of the important tax issues implicated by staking.

Staking is the method by which transactions are validated on blockchain protocols that use proof-of-stake consensus mechanisms.[8] At a high-level, staking involves a party "locking up" a certain amount of the relevant digital assets (e.g., ETH) in a validator node (i.e., software operating on a computer server). Any digital assets that are staked are unavailable to the taxpayer while staked, and the taxpayer may need to wait in a queue to receive its digital assets upon unstaking. Generally, depending on the blockchain protocol, a validator is chosen at random to validate the

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[3] Rev. Rul. 2014-21 addressed certain tax issues relating to mining.

[4] Rev. Rul. 2023-14 addressed the timing of staking income but not sourcing, character, or other issues.

[5] All digital assets exist on a blockchain protocol, which relies on either a proof-of-work or proof-stake consensus mechanism. Consensus mechanisms are the way in which new transactions are validated and recorded on the blockchain. Proof-of-work consensus mechanisms involve "mining" in which various computers competing to solve a complex cryptographic puzzle in order to be selected as the computer to validate the next batch of transactions – a "block." Proof-of-stake consensus mechanism involve "staking" in which a certain amount of the relevant digital asset being "locked up" via computers (nodes) running software (validators) to validate blocks – how validators are chosen varies by protocol, but it's often random. Both mining and staking are methods of validating transactions on a blockchain protocol which generate rewards for the party validating the transaction.

[6] Rev. Rul. 2019-24 addressed certain tax aspects of hard forks and air drops.

[7] As discussed elsewhere in this statement, certain tax rules could be updated to apply to digital assets with relatively few changes to the general tax rule, but other tax rules may require more thorough consideration to determine if and how such rules should apply to digital assets. For example, to the extent a wash sale rule is considered for digital assets, consideration would need to be given for necessary carveouts (e.g., stablecoins and ordinary course of business transactions) and for necessary tailoring for digital assets (e.g., whether a shorter window is more appropriate given the volatility of digital assets as compared with traditional securities).

[8] Similarly, mining is the method by which transactions are validated on blockchain protocols that use proof-of-work consensus mechanisms (e.g., bitcoin). Unlike staking, mining does not involve the "locking up" of any digital assets, but rather computers compete to solve a complex mathematical puzzle in order to be the next miner to be selected to validate the next "block."

next "block" (i.e., a grouping of transactions) and other validators will cross-check the validity of the block to ensure accuracy. Validators that act maliciously (e.g., validating a fraudulent transaction) may lose part of their staked ETH in a "slashing" event. In exchange for validating the block of transactions, validators receive staking rewards, which include both transaction fees and newly minted digital assets. Depending on the blockchain protocol and staking software utilized, transaction fees include amounts paid by the parties involved in the validated transactions as well as fees resulting from optimization or algorithmic overlays (e.g., maximal extractable value (MEV)).

Sourcing

Sourcing of income from staking activity is not addressed in the Code or any administrative guidance. As a result, taxpayers must attempt to source staking income by analogy to other sourcing rules within the Code, leaving significant uncertainty for taxpayers. Given the lack of clarity, some staking providers structure their operations in a manner that minimizes their connection to the United States (e.g., by locating validator nodes outside the United States in order to minimize the likelihood that staking income of their non-U.S. clients is considered U.S. source income (and therefore subject to U.S. withholding tax). Consistency, clarity, and administrability should be prioritized in determining the appropriate sourcing rule for staking income. In addition, basing the source of staking income based on factors that are easily manipulable would have the effect of creating significantly different tax outcomes based on immaterial differences (e.g., the location of validator nodes). More importantly, consideration should be given to the impact of any sourcing rule on U.S. competitiveness in the digital asset market. Specifically, sourcing staking income to anywhere but the residence of the recipient could adversely impact the competitiveness of U.S. staking providers – foreign investors may opt for non-U.S. staking providers over U.S. staking providers if they wish to avoid a U.S. withholding tax risk. Furthermore, U.S. custodians and U.S. issuers of investment products may be incentivized to engage with non-U.S. staking providers in order to maintain competitiveness among non-U.S. investors.

Trade or business activity

Taxpayers may stake their digital assets in variety of ways, both directly and indirectly.[9] Certain taxpayers stake directly to a self-operated validator node, but many everyday investors opt to stake through a delegated staking arrangement. Rather than operating their own validator node, investors participating in delegated staking will contract with another party (either with a third-party staking provider or through an arrangement with their custodian) to stake their digital assets to a validator node that they do not operate. Taxpayers staking through a delegated staking arrangement do not have direct involvement with the validator node.

Neither the Code nor any administrative guidance expressly addresses whether staking activity (whether direct or indirect) is treated as a trade or business activity versus a passive activity. This analysis is relevant to rules that govern both the taxation of staking income to non-U.S. persons and the treatment of staking income earned by tax-exempt organizations.

Sections 871 and 882 provide that income of a non-U.S. person that is effectively connected with the conduct of a U.S. trade or business is subject to U.S. federal income tax

[9] We note that there are a variety of options for staking that are beyond the scope of what can be covered in this statement, such as liquid staking.

("ECI"). Foreign investors may be deterred from engaging with U.S. staking providers if staking income is treated as income from a trade or business (and therefore potentially ECI), especially if coupled with a sourcing rule other than sourcing to the residence of the recipient (see prior discussion regarding "Sourcing").

Additionally, Sec. 512 provides that income resulting from a business that is unrelated to the tax-exempt purposes of a tax-exempt organization is subject to U.S. federal income tax ("UBTI"), subject to various carveouts for specific types of income (generally passive investment income). Staking is not specifically addressed in the carveouts to UBTI, and thus there is significant uncertainty as to whether staking activity could result in UBTI to tax-exempt investors. This is particularly relevant to tax-exempt accounts, such as individual retirement accounts ("IRAs"), which may hold digital assets that are eligible for staking. Such uncertainty is disadvantageous to taxpayers gaining investment exposure to digital assets through their IRAs – since staking is a significant part of the value proposition of proof-of-stake cryptocurrency (and IRAs would need to incur some amount of tax risk under current law in order to avoid losing out on the value of staking rewards).

Investment structures

Digital asset investment products, such as U.S. digital asset exchange traded products (ETPs), democratize the availability of digital asset investments by making digital assets available in the same way that customers access securities. Existing tax structures (e.g., grantor trusts and partnerships) for ETPs do not contemplate novel concepts such as the staking of digital assets; however, much of the value proposition of investing in proof-of-stake cryptocurrency lies in the ability to stake. Approximately $8B of ETH is held in U.S.-based ETH ETPs, none of which is staked. Once staking by ETPs is approved by the SEC[10], lack of clarity on the tax consequences of staking in by such vehicles could inhibit their ability to benefit fully from staking rewards. As the SEC moves to permit staking in ETPs, legislative clarity on the tax consequences of such activity is critical to support staking in these investment structures.

Most digital asset ETPs are structured as grantor trusts for tax purposes, though some may be structured as partnerships. Generally, ETPs are structured as grantor trusts or partnerships for tax purposes because these structures have only one layer of taxation at the investor level (versus a corporation, which also has a tax at the entity level). Grantor trusts are usually preferred by everyday investors because they issue IRS Forms 1099, which are generally considered to be easier to understand than Schedules K-1 (issued by a partnership) for everyday taxpayers.

Grantor Trusts.[11] Currently, the Code does not expressly address how staking activities should be treated for purposes of the grantor trust rules; as a result, market participants may reasonably take different positions on the issue, resulting in potential inconsistency in tax treatment and the potential for increased risk for everyday investors. Grantor trusts are subject to various rules and limitations, including that the trust cannot (i) be engaged in business activities, and (ii) have the power to vary its investment portfolio. The principle behind these restrictions is to ensure

[10] In a pivot from its policy under the last administration, the SEC has been signaling to the industry that staking will be permissible in ETPs imminently. In its latest move, the SEC released staking guidance on 5/29/25 that is widely considered to be an affirmative step towards such approval.

[11] Note that there are a number of additional details relating to grantor trusts and staking that require further clarity, including liquidity management, and would be ripe for further inquiry and discussion.

that the grantor trust is a passive investment vehicle. Accordingly, activities that produce passive income generally do not run afoul of these limitations. While regulations, guidance, and court cases provide some insight into what is considered a "power to vary" for these purposes, there is no specific guidance on whether staking assets (and staking any resulting staking rewards) constitutes a "power to vary" the assets. Outside of the tax context, the SEC found that staking activities are generally passive in nature, concluding in guidance released on March 29, 2025 that staking for securities law purposes is ministerial or administrative in nature. Similar guidance or legislation has not been issued on the tax side to clarify the treatment of staking activities for purposes of these rules.

Partnerships. For investment products structured as partnerships, clarification is needed on the application of the "qualifying income" exception to the publicly traded partnership (PTP) rules under Sec. 7704 and whether it expressly includes staking income. The PTP rules under Sec. 7704 require certain partnerships to be taxed as corporations if interests in the partnership are, or are effectively equivalent to being, publicly traded. There are exceptions and safe harbors under the PTP rules that allow partnerships that would otherwise be taxable as corporations to continue to be taxed as partnerships. The "qualifying income" exception provides that partnerships with at least 90% qualifying income (generally, passive investment income) will not be taxed as corporations regardless of whether their interests are publicly traded. The definition of "qualifying income" under Sec. 7704(c) does not specifically address staking rewards or other periodic income from digital assets. As noted above, outside of the tax context, the SEC found that staking activities are generally passive in nature, concluding in guidance released on May 29, 2025, that staking for securities law purposes is ministerial or administrative in nature. Similar guidance or legislation has not been issued on the tax side to clarify the treatment of staking activities for purposes of these rules.

Stablecoins

Stablecoins may play an integral role in our financial system, which Congress has acknowledged in its efforts to pass legislation clarifying a legal framework for stablecoins. Clear and administrable tax rules are essential to widespread adoption and success of U.S.-based and U.S. dollar-backed stablecoins.[12] The definition of "digital asset" under Sec. 6045 is broad, and whether stablecoin should be treated differently than digital assets more generally should be considered. For example, as currently drafted, digital asset broker reporting for stablecoin transactions could significantly impede market adoption and proliferation of stablecoins.

Digital Asset Loans

The tax treatment of digital asset loans is a prime example of the disparate treatment of digital assets transactions and their traditional securities counterparts.

Securities lending involves the loan of a security on a short-term basis in exchange for a fee. The lender benefits from the additional income and liquidity, while the borrower benefits from the use of the borrowed securities. Such transactions are an integral part of a healthy financial system and enhance the liquidity of financial markets. In these arrangements, the lender transfers

[12] In addition to the issues here, we note that to the extent a wash sale rule is considered for digital assets, a carveout for stablecoins would be necessary. We note that stablecoins do not raise the policy concerns targeted by the wash sale rules because stablecoin transactions do not generate material losses.

the securities to the borrower and the borrower agrees to return securities identical to those borrowed. Sec. 1058 of the Internal Revenue Code of 1986, as amended (the "Code"), provides that these transfers – both by the lender to the borrower of the borrowed securities and the return of identical securities by the borrower to the lender – are eligible for non-recognition treatment as long as certain statutory and regulatory requirements are met. Such non-recognition treatment was clarified in 1978 with the enactment of Sec. 1058 due to the importance of these lending transactions to financial markets and the adverse effect on markets that would occur if there were a risk of gain recognition upon making a securities loan.

Congress enacted Sec. 1058 in 1978, long before Satoshi Nakamoto released his white paper introducing Bitcoin on October 31, 2008. The statute addresses the lending transactions that were most pertinent in our financial system at the time – the lending of securities, as defined under Sec. 1236(c).[13] Digital assets are not "securities" for this purpose. As a result, digital assets are not expressly addressed by Sec. 1058. Accordingly, it is unclear under common law principles whether digital asset lending transactions result in recognition treatment with respect to the loaned asset each time a loan is initiated.

The lending market has evolved over time and expanded to assets other than solely securities, including digital assets. Sec. 1058, however, has not been amended to keep up with these changes. Without legislative clarity, market participants may take inconsistent approaches to this uncertainty, which creates risk, diminishes liquidity and increases friction in the financial system.

U.S. Trading Safe Harbors

Generally, if non-U.S. persons engage in a trade or business within the U.S., any income from that activity will be treated as income effectively connected to such U.S. trade or business ("ECI") and therefore subject to U.S. tax. Sec. 864 provides a safe harbor for non-U.S. persons trading in securities or commodities through a U.S. broker, custodian or similar agent[14] or for non-U.S. investors trading securities or commodities for their own account[15]. This safe harbor serves to put U.S. brokers, custodians, asset managers, and other agents on a level playing field with their non-U.S. competitors. Without this safe harbor, non-U.S. investors would be deterred from using U.S.-based brokers, asset managers and similar parties in order to avoid any risk of being deemed to be engaged in a U.S. trade or business.

The existing trading safe harbors for securities and commodities do not expressly include digital assets. Although certain digital assets, such as Bitcoin and Ethereum, are generally considered in practice to be commodities for U.S. federal income tax purposes (and therefore likely eligible for the safe harbors), the Code has not been updated to reflect such classification and the treatment for many digital assets remains unsettled. The lack of clarity on whether digital assets are eligible for the securities and commodities trading safe harbor may serve as a deterrent for non-U.S. investors investing in digital assets in U.S. markets and through U.S. managers, which puts U.S. brokers, asset managers and similar parties at a disadvantage as compared with their non-U.S. counterparts. The tax policy reasons for the existing securities and commodities safe harbors

[13] Sec. 1236(c) defines a "security" as any share of stock in any corporation, certificate of stock or interest in any corporation, note, bond, debenture, or evidence of indebtedness, or any evidence of an interest in or right to subscribe to or purchase any of the foregoing.
[14] Sec. 864(b)(2)(A)(i), 864(b)(2)(B)(i).
[15] Sec. 864(b)(2)(A)(ii), 864(b)(2)(B)(ii).

(would presumably apply with equal force to digital assets).

Mark-to-Market

The mark-to-market rules under Sec. 475 specify circumstances under which dealers[16] and traders[17] of securities and commodities are either required to or may elect to deviate from general realization-based tax accounting principles. Dealers in securities generally are required to mark any securities to market at year-end, i.e., the dealer will treat any such securities as though sold at year-end for fair market value and recognizing any resulting gain or loss (which is typically ordinary). Traders in securities may elect into these rules, as may traders and dealers in commodities.

The existing mark-to-market regime does not expressly include digital assets. Although certain digital assets, such as Bitcoin and Ethereum, are generally considered in practice to be commodities for U.S. federal income tax purposes, the Code has not been updated to reflect such classification and the treatment for many digital assets remains unsettled. Accordingly, it is unclear whether dealers and traders in digital assets may elect into the mark-to-market rules under the current statute. Dealers and traders in digital assets may wish to elect into mark-to-market tax accounting for purposes of administrability and in order to provide a more accurate reflection of income, to better align digital assets with other marketable securities, and to avoid creating inconsistencies in tax treatment. Further, this is another example of disparity between the treatment of digital assets and traditional securities and commodities under the Code.

Charitable Contributions of Digital Assets

Subject to various limitations outlined in Sec. 170, taxpayers generally may deduct charitable contributions, including contributions of capital gain property, such as digital assets. If the taxpayer is donating appreciated capital gain property to a tax-exempt organization described in Sec. 170(b)(1)(A) (e.g., churches, schools, public charities), the taxpayer may take a deduction equal to the fair market value of the donated property.[18] If the taxpayer is donating appreciated capital gain property to a tax-exempt organization described in Sec. 170(b)(1)(B) (e.g., private nonoperating foundations), the taxpayer's deduction for the donated property is reduced by any built-in gain, even if it would have been taxable as long-term capital gain. Donations of non-cash property exceeding $5,000 in value generally must be substantiated with a qualified appraisal, resulting in increased costs to the taxpayer.[19]

Readily valued property, such as publicly traded securities, are generally exempted from the limitation on deduction for donations to private nonoperating foundations and the qualified appraisal substantiation requirements. Under Sec. 170(e)(5), taxpayers may deduct the full value

[16] A "dealer in securities" is defined under Sec. 475(c)(1) as a taxpayer who either: (A) regularly purchases securities from or sells securities to customers in the ordinary course of a trade or business; or (B) regularly offers to enter into, assume, offset, assign, or otherwise terminate positions in securities with customers in the ordinary course of a trade or business. The term "dealer in commodities" is not separately defined.

[17] The term "trader" is not defined but is generally considered to a party that buys and sells securities or commodities as part of a trade or business (as compared with an investor buying or selling for their own account). Dealers are differentiated from traders in that their trade or business also involves the sale of securities or commodities to customers. *Arberg v. Commissioner*, T.C. Memo 2007-244.

[18] Any such deduction is reduced to the extent that a portion of the proceeds would not have been long-term capital gain had the taxpayer sold the asset at the time of donation. Sec. 170(e).

[19] Sec. 170(f)(11)(C).

of "qualified appreciated stock" with built-in long-term capital gain donated to private nonoperating foundations; "qualified appreciated stock" means stock of a corporation for which market quotations are readily available on an established securities market. Under Sec. 170(f)(11)(A)(ii)(I), taxpayers are not required to obtain a qualified appraisal for "readily valued property", which includes cash and publicly traded securities.

Despite the ready availability of valuations for actively traded digital assets, the rules requiring qualified appraisals and limiting donations to private nonoperating foundations have not been updated to include actively traded digital assets. The substantiation requirements and limitations on donations to private nonoperating foundations are a deterrent for everyday taxpayers wishing to donate digital assets to tax-exempt organizations of their choice. Further, this is another example of disparity between the treatment of digital assets and marketable securities under the Code.

Conclusion

As digital assets play an increasingly important role in the U.S. financial system, the Code should be modernized to provide taxpayers with clear, consistent, and administrable rules. Tax certainty supports industry growth and encourages business activity to grow domestically rather than offshore. As legislation moves forward to create frameworks for market structure, stablecoins, and other aspects of the digital asset industry, sound tax policy should move in step – without clear tax rules, the industry growth expected from non-tax legislation may be hindered as market participants encounter tax risk and uncertainty.

On behalf of Fidelity and the millions of customers we serve, we appreciate the invitation to share our views and contribute to this important dialogue. We applaud Congressional efforts to identify and address the gaps in the existing tax framework to support U.S. growth in the digital asset industry, and we look forward to continuing to work with the Committee to implement a modernized tax framework for digital assets.