

# NFT:

## Not Free of Taxation

An accounting professional's guide to navigating  
the wild world of NFTs and their tax implications  
(2022)

by Gusto and Jason Staats



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# The NFT craze

NFTs have taken the internet by storm. In 2021, trading volume increased to **\$24.9 billion**, up from just \$94.9 million in 2020. There are now **more NFTs on OpenSea** (an NFT marketplace) than there were websites in 2010. And with art giants like **Sotheby's** getting in on the trend and **the NFL** handing out NFTs with each Superbowl ticket this year, they've crossed over from the realm of **crypto bros** to the mainstream.

Beyond the craze, it's a very real thing. NFTs have a lot of promising use cases and hold the potential to help us entirely rethink ownership in the digital age. But not beyond the craze, your clients might have gotten caught up in the hype, and made big purchases or racked up a bewildering number of microtransactions without realizing they're taxable events.

Today, buying an NFT is simpler than ever thanks to wallets like MetaMask and Fantom, and marketplaces like OpenSea—but unlike ecommerce sites, these platforms don't (currently) charge buyers taxes at the time of transaction. Most clients do not know this. Caveat emptor. As a result, many will not be aware of the taxes they owe, causing **panic at tax time**.



**When your client finally shares their transaction history**

[Image via Bill Spacman on Twitter](#)

It doesn't help that government advice on NFT taxes is near-nonexistent (at the time of writing, the IRS hasn't updated its cryptocurrency tax guidance since 2014). Thanks to a dearth of reputable information, clients are turning to armchair experts on TikTok and Twitter who offer well-meaning but not always accurate advice. This is something CPA Jason Staats has run into in his practice: "We see it virtually every day on Twitter, you have prominent people in the NFT space saying, 'Here's how a tax thing works with this or that.' Then the tax professionals are saying, 'Yeah, that's not really how it is.'"

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**—Jason Staats**

As accounting professionals, the challenge is to get ahead of the misinformation and provide our clients with accurate guidance on how their NFTs are taxed. In this ebook, we'll cover what NFTs are, how they work, and the tax implications of purchasing, owning, and selling one, so you can feel confident broaching that conversation with your clients.

Don't worry if the NFT space is totally new to you—we're going to cover everything you need to know in a way that's easy, digestible, and dare we say, even fun. NFTs aren't going away anytime soon, so boot up your Discord and unlock your MetaMask, and let's get into it. (Stay tuned for an explanation of Discord and MetaMask in the next section.)

*Special thanks to Jason Staats for providing the ideas that formed the basis of this ebook. Look out for his quotes throughout!*



Jason Staats, CPA, MBA  
Principal at Brenner, LLP

The information in this ebook is meant for educational and entertainment purposes only and does not constitute tax advice. If you have questions, please speak to a tax advisor.

# The ABCs of NFTs

NFT, as you've probably heard, stands for non-fungible token. But all that tells you, as illustrated so delightfully in this sketch by Julie Nolke, is that they can't be "funged." What does that even mean?

Let's go back to Econ 101: All goods in our economy are "fungible" (replaceable or replicable) or "non-fungible" (one of a kind). For instance, a sack of flour is fungible. You can exchange one sack of flour for any other, and be confident they're worth the same amount. On the other hand, the *Mona Lisa* is non-fungible because it's one of a kind. When it was stolen from the Louvre in 1911, the museum couldn't just go out and replace it with any other painting. (Luckily, it was eventually returned.)



Very simply, you can think of NFTs as contracts or certificates of authenticity stored on an open ledger. The block of code on the blockchain is the NFT, which points to the item owned, often a work of art. *The art itself is not the NFT.* To go back to our *Mona Lisa* example, the NFT would be its provenance—which is art-world speak for a record of ownership, used to verify the authenticity of a piece of art. If you can trace a painting's provenance back to its initial creation or sale, you can be pretty sure it's genuine.

The only difference is, when you purchase an NFT, instead of a financial institution verifying the transaction—i.e. your bank saying you bought something and are the rightful owner—all of the other users on the blockchain do it for you.

The reason why art brokers like Sotheby's and Christie's are interested in the technology is because NFTs establish a clear provenance for digital art. While we have records that can identify physical art as a real Rembrandt or Banksy, the infinitely replicable nature of digital art made it much harder to establish provenance for pieces by creators like Song Ting. And provenance is what gives fine art value. "Once you leave aside the technical details of NFTs, putting artworks on the blockchain is like listing them in an auction catalog," writes Anil Dash, one of the co-inventors of the NFT.

What's most promising about NFTs is the potential to completely rethink ownership in the digital age. Our legal and financial systems are set up around physical property—digital property is the next frontier. To date, digital ownership has always had to happen through a specific platform. NFTs are so exciting because they allow people to own something digitally in a platform-agnostic way.

And it's not just digital property—tangible property like homes, land, cars, and so on could also be supported by non-fungible certificates of ownership (i.e. NFTs) stored on the blockchain. Imagine if, instead of digging through the basement of a courthouse looking for a deed to a house, a clerk could find a secure, immutable record of property ownership on the blockchain. That's just one of the potential use cases that NFTs unlock.

While we can't get into every potential NFT use case in this ebook (we'd run out of time to talk about taxes), there is one more worth noting because it's important for understanding the NFT space. NFTs can also give you access to a certain community, such as the Bored Ape Yacht Club. Referred to as decentralized autonomous organizations or DAOs, these communities function almost as co-ops. Members buy NFTs to invest in the community, to access exclusive member perks, and, if the community does well, to reap a return on their investment.

## A glossary of NFT terms

**Blockchain:** A distributed database shared across a peer-to-peer computer network—like a shared spreadsheet, with entries constantly being verified by all of its users. It can guarantee the security and fidelity of its entries without a third-party source, such as a bank, having to verify them.

**Cryptocurrency:** Digital currency like Bitcoin, Ether, and many others. The “crypto” part of the name comes from the cryptography used to secure transactions. But just because they're called “currencies” doesn't mean they're treated as such—many governments classify cryptocurrencies as securities, commodities, or other asset classes.

**Decentralized autonomous organization (DAO):** Similar to a co-op, a DAO is a community that users have shares in, in the form of NFTs or cryptocurrency. Community members may also have access to special perks as a result of their investment. The more successful the project, the more its community members benefit.

**Discord:** A text, voice, and video communication service, Discord consists of invite-only servers (similar to Slack). Once users join a particular Discord server, they can participate in topic-specific channels, launch voice and video calls, and stream video.

**Ether (ETH):** A cryptocurrency powered by the technology Ethereum used to facilitate the majority of NFT transactions. It has the ability to create smart contracts (essentially custom lines of code in the blockchain), which makes it ideal for facilitating the buying and selling of NFTs.

**Fiat:** Any government-issued, centralized currency not backed by a commodity (like gold). This includes most modern paper currencies, such as the U.S. Dollar, Euro, Japanese Yen, and so on.

**Gas fee:** All cryptocurrency transactions take computational effort to execute. Gas fees refer to the cost associated with performing certain operations on the Ethereum network. Much like real gas, the price of virtual gas is variable, depending on the demand for resources on the network.

**Ledger:** A decentralized log of transactions, stored in the blockchain. (Think of it like entries in a spreadsheet.)

**Marketplace:** An online platform for buying and selling NFTs. OpenSea and Rarible are examples of NFT marketplaces.

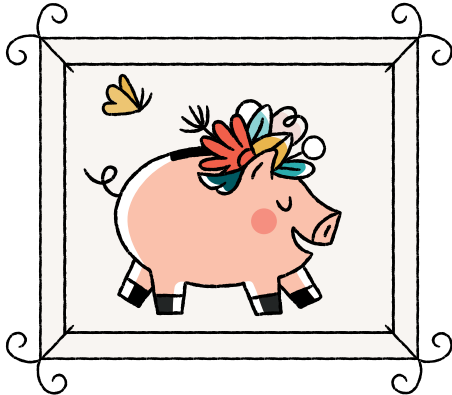
**Minting:** The process of creating an NFT; that is to say, putting an entry on the blockchain which then acts as the certificate of ownership for a digital or physical good.

**NFT:** Non-fungible token. A line of code that acts as a certificate of ownership for a digital or physical good and is stored on an open ledger. It is not the good itself.

**Wallet:** Like a physical wallet, a crypto wallet holds currency—except instead of coins and bills, it stores private keys. Crypto wallets allow users to send, receive, and spend cryptocurrency. MetaMask and Fantom are examples of crypto wallets.

# How do you make an NFT, anyway?

NFTs are shockingly easy to *mint*—that is, create. To illustrate, let's say we wanted to mint an NFT of our mascot, Penny the Pig.



## Step one: Getting the funds

Minting an NFT is essentially the process of creating a smart contract on the blockchain. It costs money to create this smart contract, so we'll need to first acquire some cryptocurrency. To do this, we'll create a crypto wallet, [purchase some cryptocurrency](#), and connect it to a platform like Rarible or OpenSea.

## Step two: Minting our NFT

Using our platform of choice, we can now mint the NFT. This is as simple as making a profile for ourselves, uploading our image file of Penny in an accepted format, and—that's pretty much it. "In OpenSea, the minting process is so easy I kept waiting for a clown to jump out and tell me I'd been tricked," wrote [one poet](#), in a blog post explaining her experiences minting her work.

At this stage, we can also set a percentage of royalties we will earn on future resale of Penny. This feature is incredibly helpful for artists—if their work is ever resold, they can continue to make money from their work.

## Step three: Putting our NFT up for auction

Using the same platform we used to mint our NFT of Penny, we can now put it up for auction. All we have to do is pay the listing fee and then wait patiently—if it sells, we'll collect payment and might need to settle up some final transaction fees, depending on the platform. When someone purchases it, that record of the transaction is logged into the open ledger and the NFT officially belongs to the buyer.

That's it. Easy, right? But wait ... now we might owe some taxes.

# Non-fungible taxes

The tax implications of NFTs are different depending on whether you're a creator or a purchaser. Let's break down both use cases in detail.

## The tax implications of creating NFTs

NFT creators are not currently taxed when they mint an NFT, but are taxed when they sell it. Though, in order to create an NFT, they need to buy crypto to pay the gas fees (the cost of computational effort). As we'll explore in the next section, any time you buy crypto, you trigger a capital gains holding period—in this case, for any change in value from the time you bought the crypto to the time you used it to pay for gas.

Upon selling an NFT, a creator is subject to income and self-employment tax, the same as any other entrepreneur who sells their products. "When a creator sells an NFT on a platform like OpenSea or Rarible, most tax experts agree that the profits should be considered ordinary income and be subject to a rate as high as 37%," writes Allyson Versprille for Bloomberg.

But as Jason Staats notes, that just accounts for the income part of the equation, not self-employment tax, which is an additional 15.3% on top of the individual's income tax rate. "It's a little nuanced because you pay self-employment tax on your net self-employment income, so you could deduct expenses against it," he says. "But if you sold \$100 NFT that you minted yourself, you'll pay ordinary income tax rates plus self-employment tax." (Theoretically, you could claim the gas fees as expenses.)

*"Many new creators might not be aware that they're expected to pay quarterly estimated tax payments"*

Additionally, many new creators might not know they're expected to make quarterly estimated tax payments—especially if they've never been self-employed before. If they don't pay taxes each quarter, and just go ahead and file their annual return like they're used to, they'll likely accrue some unexpected penalties and interest.

Another thing to keep in mind is if they don't immediately convert their NFT proceeds from cryptocurrency into fiat (aka USD or another centralized currency), a new capital gains holding period begins on their crypto. When and if they eventually convert it back, they'll trigger a capital gains/loss taxable event. For folks unused to paying cryptocurrency taxes, this is also something to be aware of.

## The tax implications of buying and selling NFTs

Sticking with us so far? Creating and selling NFTs is taxed in the same way as any other self-employed business endeavor. But what about purchasing NFTs to collect, invest, or any of their other myriad use cases?

The U.S. government still hasn't ruled on whether it plans to treat NFTs as collectibles or securities. Still, most tax experts agree they fall under one of these two treatments. "The tax implications of buying and selling an NFT with crypto are the same in both cases," says Jason Staats. "The only difference is in how the appreciation or depreciation of the asset itself is taxed—as art, or as a security."

With that in mind, there are three key taxable events you and your clients should know about:

## 1. NFT PURCHASE

Buying an NFT (or anything else) with cryptocurrency triggers a capital gain/loss taxable event. This is because the IRS sees crypto as a security, not as a currency. This takes some mental gymnastics: "The U.S. Internal Revenue Service views this transaction as you selling your ETH for fiat and then using the fiat to buy the NFT, thus creating a taxable event for you," writes Jaimin Desai for CoinDesk. (The IRS only views it this way; this isn't what actually happens.) Basically, all you need to keep in mind is this:

**Taxes owed:** The buyer will be taxed on any price appreciation on their cryptocurrency between the time they first bought their crypto and when they used it to buy an NFT.

## 2. NFT APPRECIATION/DEPRECIATION

Selling an NFT for crypto also triggers a capital gain/loss taxable event. Again, since the IRS sees cryptocurrency as a security, not currency, "the IRS views this as you selling your NFT for fiat and then rebuying ETH or another NFT with fiat," writes Jaimin.

**Taxes owed:** Similar to the above, the seller will be taxed on any price appreciation on their cryptocurrency from the time between when they bought the NFT to when they sold it. Depending on how the government rules, this will likely go one of two ways:

### A. NFTs will be taxed as collectables

If the government decides to treat NFTs as collectibles, they'll be subjected to the same taxes as fine art, which means:

- Works of art held for less than a year are subject to personal marginal income tax rates of up to 37%.
- Works of art held for more than a year are taxed at a maximum rate of 28%.

### B. NFTs will be taxed as securities

If the government decides to treat NFTs as securities (a stance CoinDesk and other crypto advocates have argued for), they'll be taxed at the same rate:

- Securities held for less than a year are subject to personal marginal income tax rates of up to 37%.
- Securities held for more than a year are taxed at 0%, 15%, or a maximum of 20%, depending on income.

Since the government hasn't given any clear guidance, how you choose to treat your client's NFTs is a choice. Treating NFTs as fine art is the more conservative stance—your client risks overpaying taxes now, but might get a refund later. Conversely, treating NFTs as securities is the more aggressive stance. While your client may pay less tax now, they could very well be subject to a heftier tax bill later.

### 3. CONVERSION OF NFT PROCEEDS (FROM CRYPTO BACK TO FIAT)

Finally, converting NFT proceeds (which are in crypto) back to fiat triggers a capital gain/loss taxable event, the same as cashing in any other kind of security.

*Taxes owed:* The user will be taxed on any price appreciation from the time when they received their NFT proceeds in crypto, to when they converted it to fiat.

#### Tax Takeaways

Though the guidance is still hazy, we can make some educated guesses on how the government will treat NFTs. That said, it's critical to emphasize to your clients that anything you file now is subject to change later. Until the government rules, there's no wrong answer in terms of choosing to treat an NFT as a collectible or a security—but there are bad decisions, such as not setting aside enough liquidity to account for tax on any large appreciation or capital gains.

#### *Anything you file now is subject to change later*

Make sure your clients are aware that the situation is still evolving and, regardless of how you decide to treat their NFTs, set enough funds to cover any potential additional tax bills down the line.

## How to talk to your client about their Bored Ape NFT

You might be thinking that you can push off the NFT conversation until next tax season—but, as Jason Staats says, don't wait. "The worst thing that can happen is a client comes to you and they're super convinced that their NFT is going to be taxed a certain way, when it's not," he says. "There's a lot more friction in that conversation than if you're proactively sharing the rules as they stand today."

*"The worst thing that can happen is a client comes to you and they're super convinced that their NFT is going to be taxed a certain way, when it's not"*

Tax misinformation around NFTs is rife on TikTok and Twitter. But if you're on top of communicating the guidelines to your clients, you can get ahead of the noise. If you're aware of any current or impending NFT purchases, now's the time to broach the conversation with your clients. The goal is to establish you as their trusted advisor—not the crypto bros on TikTok.



Here's an email template you can share with your client:

Hi \_\_,

As we think about your taxes, it'll be important to track any transactions involving NFTs. Any chance you have minted, purchased, or sold NFTs this calendar year, or plan to? If so, it might be a good idea to schedule some time so we can verify whether those are taxable events, and how we can ensure you don't pay avoidable taxes on those.

Cheers,

Signature

## What clients need to know

The most important thing to emphasize with your clients: Make sure they're keeping a meticulous record of all their trades and transactions. "Try and log your trades and really take this seriously, because if you don't, you're frankly going to get screwed," writes Ben Schiller for CoinDesk. Even as the guidance continues to evolve, this will give them a single source of truth to look back on, so you can help them go through it and figure out what taxes they owe.

Many crypto wallets now let users download a record of all their trades (including any NFT purchases) as a .csv file, which is a feature that NFT aficionados should take full advantage of. There are also tools like Koinly which, for a small fee, use an API to pull a record of transactions from a user's crypto wallets and automatically calculate taxes. We don't recommend relying exclusively on these kinds of tools to calculate NFT taxes because the guidance is still so fuzzy and it's unclear what assumptions the tool might be making about NFTs (e.g. whether it takes a more aggressive or conservative stance); however, it can still be a useful resource for generating a complete picture of a user's NFT transactions across different platforms and wallets.

You can also share that, since NFT tax guidance continues to evolve, there is a certain degree of uncertainty. If you choose to take a more aggressive stance, ensure that your clients have enough liquidity to cover any tax bills down the line, in case the government comes out with a more conservative policy.

## Conclusion: NFTs are here to stay

The NFT craze may have taken the world by storm, but the technology's real use cases mean they're not going away anytime soon. And neither is sketchy tax guidance from well-intentioned, but nonexpert, NFT enthusiasts. That's why it's so critical that we as accounting professionals get up to speed on the trend, so we can be proactive about sharing accurate tax information with our clients. By starting the conversation around NFTs early, we can ensure that clients go to us with their NFT questions—not TikTok



## Non-forgettable takeaways

- An NFT is an agreed-upon mechanism for digital ownership, like a contract or certificate of authenticity.
- There are tons of different ways to use NFTs—not just as a get-rich-quick scheme.
- If you're minting NFTs, it's taxed as ordinary income.
- If you're buying and selling NFTs, it'll either be taxed as a security or a collectible.
- Everything you submit today is subject to change.
- Be proactive about having the conversation with your client so they don't get confused by less reputable sources.
- Ensure your client is keeping track of their trades and transactions.

### Further reading

[Taxation of The Purchase and Sale Of NFTs \(National Law Review\)](#)

[5 Things to Remember When Paying Your NFT Taxes \(CoinDesk\)](#)

[NFT Investors Owe Billions in Taxes and IRS Sets Sights on Evaders \(Bloomberg\)](#)

[Matt Metras on Twitter \(tax professional in the NFT space\)](#)

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