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# A Bit-ter Divorce: Using Bitcoin to Hide Marital Assets

Caline Hou

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**A BIT-TER DIVORCE:  
USING BITCOIN TO HIDE MARITAL ASSETS**

*Caline Hou* \*

*Equitable distribution is the process of dividing marital property fairly upon divorce. The confusion surrounding the categorization of Bitcoin, a type of virtual currency that can be obtained and transferred anonymously, frustrates courts' ability to properly value divorcing parties' assets and determine a fair distribution of marital property. This Recent Development argues that North Carolina should clearly define Bitcoin as a security. First, a clear categorization of Bitcoin will notify parties that Bitcoin is a reportable asset for equitable distribution proceedings. Second, recognizing Bitcoin as a security may subject Bitcoin to increased securities regulations. Increased regulation allows for better reporting of Bitcoin transactions, which will help courts and divorcing parties discover and value bitcoins. Courts that correctly understand the value of each party's assets will be better able to determine a truly equitable distribution of property.*

**I. INTRODUCTION**

Nearly one-third of individuals who combine their finances with their significant others have deceived their partner about money.<sup>1</sup> Over half of these individuals hid cash from their

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\* J.D. Candidate, University of North Carolina School of Law, 2016. The author would like to thank her father for introducing her to Bitcoin. The author would also like to thank the staff and editors of the North Carolina Journal of Law and Technology for their invaluable assistance and feedback—especially Britton Lewis, Kyle Evans, Kelly Morris, Nicholas Turza, and Tony Lucas.

<sup>1</sup> Paul Golden, *Three in 10 Americans Admit to Financial Deception with Partners*, NAT'L ENDOWMENT FOR FIN. EDUC. (Jan. 14, 2011), <http://www.nefe.org/press-room/news/admitting-to-financial-deceptions.aspx> (“The National Endowment for Financial Education (NEFE), in cooperation with Forbes.com, commissioned an online poll conducted by Harris Interactive in December 2010, finding that 31 percent of people who combined finances with their significant other have been deceptive with their spouse or partner about money.”).

partners,<sup>2</sup> and over a third lied about finances, debt, or income.<sup>3</sup> As digital technology advances, hiding assets from a spouse may become even easier. Bank statements no longer come in the mail; instead, only individuals with an account holder's username and password can view e-statements online. Rather than stand in line at a bank in public, mobile phone users can transfer cash from one account to another using a mobile application. Bitcoin, a form of digital currency, is the latest technology that many family lawyers are concerned will help spouses hide money from their significant others.<sup>4</sup> Bitcoin's anonymity, combined with its capability for quick bitcoin transfers between wallets, makes hiding marital

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<sup>2</sup> *Id.* (finding that of the individuals who deceived their partners about money, “[n]early three in five of these adults (58 percent) say they hid cash from their partner or spouse”).

<sup>3</sup> *Id.* (finding that of the individuals who deceived their partners about money, “[t]hirty four percent of these adults say they lied about finances, debt, [and] money earned”).

<sup>4</sup> See, e.g., Amanda Williams, *Divorce's New Weapon: Separating Spouses Using Bitcoin to Hide Wealth From Estranged Partners During Court Battles*, MAILONLINE (June 3, 2014), <http://www.dailymail.co.uk/news/article-2646995/Divorcing-spouses-use-Bitcoin-hide-wealth-estranged-partners-court-battles.html> (“Digital currencies like Bitcoin are fast becoming the weapon of choice for divorcing spouses trying to hide wealth from partners during court battles.”); see also Jane Croft, *Bitcoin Could Be Used To Hide Assets In Divorces, Warn Lawyers*, FINANCIAL TIMES (June 2, 2014, 2:15 PM), <http://www.ft.com/cms/s/0/d1131630-9005-11e3-8029-00144feab7de.html#axzz3DLtLpL6I> (“Bitcoin, the electronic currency, could be used by divorcing spouses to hide assets from estranged partners.”); Valerie Surgenor & Jacqueline Stroud, *UK: What's Mine Is Mine and I Shall Hide It! Bitcoin And Divorce*, MONDAQ (June 24, 2014), <http://www.mondaq.com/x/322736/divorce/Whats+Mine+Is+Mine+And+I+Shall+Hide+It+Bitcoin+And+Divorce> (“It is inevitable that divorce proceedings which include debates about Bitcoin are on the horizon and virtual currencies and cryptocurrencies should be borne in mind by all parties involved in divorce proceedings.”); *Watching For Deception: Bitcoin May Be Used to Conceal Assets in Divorce*, MCDEVITT LAW FIRM (July 12, 2014), <http://www.mcdevittlaw.net/2014/07/watching-for-deception-bitcoin-may-be-used-to-conceal-assets-in-divorce/> (“Individuals who wish to cheat their spouses out of their due compensation have been around for as long as the divorce process. Bitcoin is perhaps the latest, but certainly not the last, new method for doing so. Divorce parties, attorneys and judges need to be aware of all asset concealment methods, old and new.”).

assets easier for spouses and thus helps to shield certain assets from being equitably distributed upon divorce.<sup>5</sup>

Equitable distribution is the process of dividing marital property equitably, or fairly, when spouses divorce.<sup>6</sup> If spouses successfully hide assets, courts cannot consider these assets when determining a fair distribution of marital property. Thus, one spouse may obtain much less or much more property than is equitable.

This Recent Development explores how divorcing spouses can abuse Bitcoin to undermine North Carolina's statute governing equitable distribution,<sup>7</sup> and proposes that the best solution to avoid this abuse is to categorize Bitcoin as a security. Part II discusses the history and purpose behind equitable distribution statutes and the process of equitable distribution proceedings. Part III introduces Bitcoin and Bitcoin transactions. Part IV examines the varying approaches that the law has taken regarding whether to label Bitcoin as a currency, security, or other form of asset. Part V argues that labeling Bitcoin as a security will be more conducive to effectuating the purpose of equitable distribution statutes. By labeling Bitcoin as a security, the government can place more regulations on Bitcoin, allowing transactions to be discovered more easily and allowing courts to evaluate marital assets more accurately.

## II. EQUITABLE DISTRIBUTION: HISTORY, PURPOSE, AND PROCEEDINGS

Upon divorce, spouses must determine how to divide property. For spouses who acquired little or no property during their

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<sup>5</sup> See, e.g., Croft, *supra* note 4 (discussing how Bitcoin's anonymity and easy transfer procedures could help spouses hide assets in divorce).

<sup>6</sup> Marital property is "all real and personal property acquired by either spouse or both spouses during the course of marriage and before the date of separation of the parties, and presently owned . . ." N.C. GEN. STAT. § 50-20 (2013).

<sup>7</sup> North Carolina General Statutes Section 50-20(c) provides for "an equal division by using net value of marital property and net value of divisible property unless the court determines that an equal division is not equitable. If the court determines that an equal division is not equitable, the court shall divide the marital property and divisible property equitably." *Id.*

marriage, division of property is not an issue. For couples who have been married for years, or even decades, and have accumulated a great deal of property during their marriage, determining how to divide property can be difficult. Each state has its own statutes governing the division of property upon divorce.<sup>8</sup> While some states continue to divide property equally between divorcing spouses, North Carolina and forty-six other states have adopted a statutory scheme for equitable distribution of marital property.<sup>9</sup> Equitable distribution calls for a *fair* distribution of property, rather than an equal division.<sup>10</sup>

#### A. *History of Marital Property Ownership*

State statutes determine ownership of marital property.<sup>11</sup> Most states, including North Carolina, have the title theory of marital property, while some still use the community property theory of marital property.<sup>12</sup> Under the title theory of property—also called the separate property theory—the spouse who holds the title to a piece of property retains ownership of it.<sup>13</sup> Upon divorce, each spouse leaves the marriage with the property to which he or she holds title.<sup>14</sup> In contrast to the title theory of marital property, some

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<sup>8</sup> See, e.g., *id.*; 23 PA. CONS. STAT. § 3502(a) (2014) (“Upon the request of either party in an action for divorce or annulment, the court shall equitably divide, distribute or assign, in kind or otherwise, the marital property between the parties without regard to marital misconduct in such percentages and in such manner as the court deems just after considering all relevant factors.”); VA. CODE ANN. § 20-107.3 (2014) (“The amount of any division or transfer of jointly owned marital property, and the amount of any monetary award, the apportionment of marital debts, and the method of payment shall be determined by the court after consideration of the following factors . . . (11) Such other factors as the court deems necessary or appropriate to consider in order to arrive at a fair and equitable monetary award.”).

<sup>9</sup> DOUGLAS E. ABRAMS ET AL., CONTEMPORARY FAMILY LAW 473 (3d ed. 2012).

<sup>10</sup> See *infra* notes 17–22 and accompanying text.

<sup>11</sup> ABRAMS ET AL., *supra* note 9, at 471.

<sup>12</sup> *Id.* at 471–73.

<sup>13</sup> *Id.* at 471–72.

<sup>14</sup> *Id.* at 472. Historically, under the title theory of property, many women would leave their divorces with little or no property because men traditionally owned all of the property acquired during marriage. *Id.*

states have adopted the community property theory, stressing that each spouse in a marriage shares equal ownership of most property acquired during marriage.<sup>15</sup> In these states, absent statutory provisions for equitable distribution, parties to a divorce would be entitled to an equal split of marital property, regardless of who holds title to the property.<sup>16</sup>

#### B. *Purpose of Enacting Equitable Distribution*

Because both title theory and community property theory sometimes led to unfair distribution of property upon divorce, many states enacted a statutory scheme for equitable distribution.<sup>17</sup> North Carolina is among the states that adopted an equitable distribution policy for marital property division.<sup>18</sup>

The purpose of equitable distribution is (1) to recognize marriage as a partnership to which both parties contribute either directly or indirectly and (2) to affect a return to each party for the contributions that he or she made.<sup>19</sup> Equitable distribution is a way for states to ensure that both parties are repaid for their contributions to the marriage, even if those contributions did not result in a spouse individually taking title to property.<sup>20</sup> An equitable distribution is not necessarily an equal division.<sup>21</sup> North

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<sup>15</sup> *Id.* at 473.

<sup>16</sup> *Id.*

<sup>17</sup> With the exception of three states, all states have adopted equitable distribution statutes. *Id.* California, Louisiana, and New Mexico remain community property states with equal division of marital property upon divorce. *Id.*

<sup>18</sup> N.C. GEN. STAT. § 50-20(c) (2013) (providing for equitable division of marital and divisible property upon divorce if equal division would not be fair).

<sup>19</sup> *Hinton v. Hinton*, 70 N.C. App. 665, 668–69 (1984).

<sup>20</sup> *Id.* at 669; *Chalmers v. Chalmers*, 320 A.2d 478, 483 (N.J. 1974) (“[T]he statutory provision for equitable distribution of property is merely the recognition that each spouse contributes something to the establishment of the marital estate even though one or the other may actually acquire the property. Therefore, when the parties become divorced, each spouse should receive his or her fair share of what has been accumulated during the marriage.”).

<sup>21</sup> § 50-20(c) (indicating that a court may determine that an equal division of property is not equitable); *Albritton v. Albritton*, 109 N.C. App. 36, 41–42 (1993) (“[A] trial court may consider all the factors listed in [N.C. Gen. Stat. § 50-20(c)], and find that an equal division of the marital assets would not be equitable under the circumstances.”).

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Carolina's equitable distribution statute lists several factors that courts must take into account when determining how to split property fairly, including all assets and debts of each party, any fraudulent conduct to conceal assets from the opposing party, and any other factor that the court deems to be "just and proper" for equitable distribution proceedings.<sup>22</sup>

*C. Equitable Distribution Proceedings*

In an equitable distribution proceeding, a court requires the parties to complete an inventory listing all property owned by either spouse.<sup>23</sup> The inventory asks parties to list all marital and separate property, and to estimate the value of each asset.<sup>24</sup> In addition to using an inventory, parties may also use various other methods of discovery, such as depositions, interrogatories, and requests for production of documents.<sup>25</sup> During this time, if there is danger that a spouse may attempt to waste or convert marital property in order to conceal it from equitable distribution, the opposing party may ask the court for an injunction to prevent that spouse from engaging in fraudulent conduct.<sup>26</sup>

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<sup>22</sup> § 50-20(c).

<sup>23</sup> § 50-21(a) ("Within 90 days after service of a claim for equitable distribution, the party who first asserts the claim shall prepare and serve upon the opposing party an equitable distribution inventory affidavit listing all property claimed by the party to be marital property and all property claimed by the party to be separate property, and the estimated date-of-separation fair market value of each item of marital and separate property. Within 30 days after service of the inventory affidavit, the party upon whom service is made shall prepare and serve an inventory affidavit upon the other party."). Each county in North Carolina may have slightly different Equitable Distribution Inventory Affidavits. These affidavits ask for a detailed listing of property, according to the type of asset it is, that is owned individually and jointly by each spouse. A sample inventory is available at <http://www.nccourts.org/Courts/CRS/Policies/LocalRules/Documents/744.pdf>.

<sup>24</sup> A sample instruction on how to complete an equitable distribution inventory is available at <http://www.nccourts.org/Courts/CRS/Policies/LocalRules/Documents/744.pdf>.

<sup>25</sup> 3 SUZANNE REYNOLDS, *LEE'S NORTH CAROLINA FAMILY LAW* § 12.132 (5th ed. 2002).

<sup>26</sup> N.C. GEN. STAT. § 50-20(i) (2013).

Once the court receives an inventory of assets, the court determines if each item of property is separate, marital, or divisible.<sup>27</sup> Separate property is property a spouse acquires before marriage or property received as a gift or inheritance during marriage.<sup>28</sup> Marital property is property a spouse acquires during the marriage and prior to separation, excluding property that is separate.<sup>29</sup> Divisible property is a third type of property recognized only in North Carolina.<sup>30</sup> Divisible property is property received during the separation that is the result of efforts made to acquire the property during the marriage or the result of passive forces that affect the value of marital property.<sup>31</sup> Passive forces include interest, inflation, and market forces.<sup>32</sup> In North Carolina, a spouse claiming that property is divisible must show the forces behind the change in value.<sup>33</sup> Once a spouse has identified these forces, North Carolina courts will presume that the change in value between the

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<sup>27</sup> ABRAMS ET AL., *supra* note 9, at 474.

<sup>28</sup> § 50-20(b)(2).

<sup>29</sup> § 50-20(b)(1).

<sup>30</sup> 3 REYNOLDS, *supra* note 25, § 12-51. North Carolina created this third category of property to remedy the problems that arose when marital property was valued on the date of separation. This left separated spouses unable to claim property that was not distributed until after separation, but was the result of pre-separation labor. To ensure that courts were consistently considering post-separation property that was the result of pre-separation labor, the North Carolina legislature amended its equitable distribution statute to include divisible property. *Id.*

<sup>31</sup> N.C. GEN. STAT. § 50-20(b)(4) (2013) (defining four categories of divisible property as “[a]ll appreciation and diminution in value of marital property and divisible property of the parties occurring after the date of separation and prior to the date of distribution,” “[a]ll property, property rights, or any portion thereof received after the date of separation, but before the date of distribution that was acquired as a result of the efforts of either spouse during the marriage and before the date of separation,” “[p]assive income from marital property received after the date of separation including, but not limited to, interest and dividends,” and “[p]assive increases and passive decreases in marital debt and financing charges and interest related to marital debt”).

<sup>32</sup> 3 REYNOLDS, *supra* note 25, § 12-52.

<sup>33</sup> *Id.* § 12-52(c)(iv) (“[A] spouse claiming that income from marital property received after the date of separation and before the date of distribution is divisible must establish the forces that generated the income.”).



date of separation and the date of distribution is divisible property.<sup>34</sup>

The third step of the equitable distribution process is to assign value to each piece of property.<sup>35</sup> Marital property is valued on the date of separation, whereas divisible property is valued on the date of distribution to take into account any appreciation or depreciation in value that occurs between these dates.<sup>36</sup> The party seeking to define an asset as marital or divisible bears the burden of proving its value.<sup>37</sup> Without credible evidence of the value, the court has no obligation to determine the value of the asset.<sup>38</sup>

Lastly, the court equitably distributes the marital and divisible assets.<sup>39</sup> The court will typically presume an equal division of marital property to be equitable.<sup>40</sup> However, a spouse can ask the court for an unequal division of property if an unequal division is more equitable.<sup>41</sup> North Carolina courts examine several factors to determine when an unequal distribution of property may be more equitable.<sup>42</sup> Factors include the income and dependency of each spouse, contributions that each spouse made to obtaining marital property that did not result in actual title to the property, acts to expand or waste marital property after the date of separation and

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<sup>34</sup> See *Wirth v. Wirth*, 193 N.C. App. 657, 661 (2008) (“Under the plain language of the statute, all appreciation and diminution in value of marital and divisible property is presumed to be divisible property *unless* the trial court finds that the change in value is attributable to the postseparation actions of one spouse.”); see also *Romulus v. Romulus*, 215 N.C. App. 495, 502 (2011) (“Based upon the statutory presumption that post-separation appreciation to marital property is divisible, defendant had the burden of proof to rebut this presumption for the trial court to be able to find that the postseparation appreciation in [defendant’s] dental practice was defendant’s separate property.”).

<sup>35</sup> ABRAMS ET AL., *supra* note 9, at 474.

<sup>36</sup> N.C. GEN. STAT. § 50-21(b) (2013).

<sup>37</sup> 3 REYNOLDS, *supra* note 25, § 12-56.

<sup>38</sup> *Id.*

<sup>39</sup> ABRAMS ET AL., *supra* note 9, at 471.

<sup>40</sup> N.C. GEN. STAT. § 50-20(c) (2013).

<sup>41</sup> *Id.*

<sup>42</sup> *Id.*

prior to the date of distribution, and “any other factor which the court finds to be just and proper.”<sup>43</sup>

*D. Fraudulent Behavior in Equitable Distribution*

During equitable distribution proceedings, parties can engage in fraudulent behavior, attempting to prevent courts from dividing certain assets the parties wish to hold onto after divorce. Parties to a divorce can hide assets from their spouses and courts through a variety of means. They can transfer funds to family or friends to hold until a judge finalizes the divorce. A spouse can also falsify documents to make the record appear as though he or she has already sold the asset and thus the court cannot distribute it.<sup>44</sup>

However, parties caught attempting to hide assets from equitable distribution may face serious repercussions. The North Carolina Rules of Civil Procedure require that parties filing pleadings verify that their pleadings are truthful.<sup>45</sup> Failure to provide truthful pleadings can lead to heavy sanctions.<sup>46</sup> Although

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<sup>43</sup> *Id.*

<sup>44</sup> *Newsome v. Newsome*, No. COA12-10, slip op. at 5–6 (N.C. Ct. App. Aug. 7, 2012) (affirming that in an equitable distribution proceeding, the trial court properly considered the plaintiff’s attempt to hide marital property by falsifying documents and testimony in an attempt to hide assets from being divided by the court).

<sup>45</sup> N.C. GEN. STAT. § 1A-1, Rule 11 (2013).

<sup>46</sup> § 50-21(e) (“Upon motion of either party or upon the court’s own initiative, the court shall impose an appropriate sanction on a party when the court finds that: (1) The party has willfully obstructed or unreasonably delayed, or has attempted to obstruct or unreasonably delay, discovery proceedings, including failure to make discovery pursuant to [North Carolina General Statute] 1A-1, Rule 37, or has willfully obstructed or unreasonably delayed or attempted to obstruct or unreasonably delay any pending equitable distribution proceeding, and (2) The willful obstruction or unreasonable delay of the proceedings is or would be prejudicial to the interests of the opposing party.”). Sanctions may include, but are not limited to, payment of reasonable fees and damages incurred as a result of the obstruction of justice. *Id.* (“The sanction may include an order to pay the other party the amount of the reasonable expenses and damages incurred because of the willful obstruction or unreasonable delay, including a reasonable attorneys’ fee, and including appointment by the court, at the offending party’s expense, of an accountant, appraiser, or other expert whose services the court finds are necessary to secure in order for the discovery or other equitable distribution proceeding to be timely conducted.”).

a court cannot divide marital property unequally solely due to fraudulent conduct or conduct intended to disturb or delay the equitable distribution process, it may assign an unequal division of property if the offending conduct causes additional expenses for the non-offending party.<sup>47</sup> Thus, courts can take into consideration attempts to hide marital assets when determining an equitable division of property.<sup>48</sup>

The development of virtual currencies that users can obtain, keep, and transfer anonymously—such as Bitcoin—make discovering marital property more difficult for divorcing spouses. Without the ability to discover how much property each party to a marriage truly holds, family courts may not be able to determine a division of property that is truly equitable.

### III. UNDERSTANDING BITCOIN

Satoshi Nakamoto, a pseudonym for an unknown individual,<sup>49</sup> first introduced Bitcoin in 2009.<sup>50</sup> Bitcoin is not backed by any

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<sup>47</sup> 3 REYNOLDS, *supra* note 25, § 12-133.

<sup>48</sup> N.C. GEN. STAT. § 50-20(c)(11a) (2013) (stating that courts shall consider “acts of either party to maintain, preserve, develop, or expand; or to waste, neglect, devalue or convert the marital property or divisible property, or both, during the period after separation of the parties and before the time of distribution”); *see Albritton v. Albritton*, 109 N.C. App. 36, 38–43 (1993) (finding that trial court did not commit reversible error when it divided property unequally but equitably based on the fact that the plaintiff held a checking account in her own name, closed the account prior to separation, used the money towards a purchase of a home under her sister and brother-in-law’s name, and later had the title of the new home transferred back to her); *see also Newsome*, No. COA12-10, at 5–6, (finding that trial court did not err when factoring in plaintiff’s attempt to hide marital assets into its determination that equitable distribution in this case required unequal distribution of property); *Ikechukwu v. Ikechukwu*, No. COA09-46, slip op. at 33 (N.C. Ct. App. Nov. 3, 2009) (using evidence of the plaintiff hiding marital assets as a factor in determining that an unequal distribution of marital assets would be most equitable).

<sup>49</sup> Nikolei M. Kaplanov, Student Article, *Nerdy Money: Bitcoin, The Private Digital Currency, and the Case Against Its Regulation*, 25 LOY. CONSUMER L. REV. 111, 115 n.21 (2012) (“The name Satoshi Nakamoto is likely a pseudonym since his or her identity is unknown.”); Ruokey Yang, *When Is Bitcoin A Security Under U.S. Securities Law?*, 18 J. TECH. L. & POL’Y 99, 101–02 n.9 (2013)

government-issued tender.<sup>51</sup> Instead, its value derives from supply and demand.<sup>52</sup> The value of Bitcoin depends on the price at which a seller is willing to sell his or her bitcoin and the price at which a buyer is willing to buy a bitcoin.<sup>53</sup> Thus, its value is volatile.<sup>54</sup>

Bitcoin's creator built the system upon a peer-to-peer network system that eliminates the need for a third-party intermediary.<sup>55</sup> Traditional transactions, such as wiring funds from one bank account to another, typically require third-party intermediaries such as banks to ensure that no one spends the same currency more than once.<sup>56</sup> However, in the Bitcoin network, users work together to validate transactions and ensure that the same bitcoins are not being spent in multiple transfers.<sup>57</sup>

#### A. *Bitcoin Transactions*

Bitcoin users purchase Bitcoin software to create a virtual wallet.<sup>58</sup> The wallet stores public and private keys that are used in

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(“Adding to the mysteries of Bit[c]oin and its lack of proper disclosure is the fact that the name of the author is actually a psydonym.”).

<sup>50</sup> Kaplanov, *supra* note 49, at 115; Yang, *supra* note 49, at 101.

<sup>51</sup> Lawrence Trautman, *Virtual Currencies Bitcoin & What Now After Liberty Reserve, Silk Road, and Mt. Gox?*, 20 RICH. J.L. & TECH. 13, 3–4 (2014), available at <http://jolt.richmond.edu/v20i4/article13.pdf> (defining virtual currency as “a medium of exchange circulated over a network, typically the Internet, which is not backed by a government”).

<sup>52</sup> *Frequently Asked Questions*, BITCOIN, <https://bitcoin.org/en/faq> (last visited Oct. 19, 2014) [hereinafter *Frequently Asked Questions*].

<sup>53</sup> *Id.*

<sup>54</sup> *Some Things You Need to Know*, BITCOIN, <https://bitcoin.org/en/you-need-to-know> (last visited Oct. 18, 2014) [hereinafter *You Need To Know*].

<sup>55</sup> Kaplanov, *supra* note 49, at 119.

<sup>56</sup> *Id.*

<sup>57</sup> See Derek A. Dion, Note, *I'll Gladly Trade You Two Bits on Tuesday for a Byte Today: Bitcoin, Regulating Fraud in the E-economy of Hacker-Cash*, 2013 U. ILL. J.L. TECH. & POL'Y 165, 167 (2013) (“Bitcoin was designed to reduce the transaction costs that are created when third parties validate transactions and mediate disputes. It solved this problem using a system where all of the other users work together to validate transactions, creating a public record of the chain of custody of each Bitcoin.”).

<sup>58</sup> Brad Jacobsen & Fred Pena, *What Every Lawyer Should Know About Bitcoins*, 27 UTAH BAR J. 40, 40 (2014). There are four types of wallets: mobile wallets, desktop wallets, online wallets, and hardware wallets. *How to Store*

later transactions.<sup>59</sup> The public key is like an electronic mail address.<sup>60</sup> It is disclosed when the user receives bitcoins from another user.<sup>61</sup> The user transferring his or her bitcoins uses his or her private key to sign transactions and verify that his or her bitcoins are now being transferred to the new user.<sup>62</sup>

Bitcoin software records transactions in groups called blocks.<sup>63</sup> Bitcoin miners then confirm the transactions in the blocks to ensure that no one has already spent the transferred bitcoins.<sup>64</sup> Confirmation is done through a process called Bitcoin mining. Once confirmed, the blocks are added onto a form of public ledger called a block chain.<sup>65</sup>

Users can accumulate bitcoins in multiple ways. First, users can buy them directly from a person they know or a person near them who has bitcoins.<sup>66</sup> This allows users to exchange cash directly or determine their own form of payment. Second, users can also receive bitcoins as payment for goods and services.<sup>67</sup> Third, users can buy into a Bitcoin exchange.<sup>68</sup> A Bitcoin exchange is a third-party intermediary that will let buyers exchange cash payments for bitcoins and will allow current bitcoin owners to

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*Your Bitcoins*, COINDESK (July 22, 2014), <https://www.coindesk.com/information/how-to-store-your-bitcoins/> [hereinafter *Store Your Bitcoins*]. For access to software that are compatible with each type of wallet, see *Choose Your Bitcoin Wallet*, BITCOIN, <https://bitcoin.org/en/choose-your-wallet> (last visited Oct. 21, 2014).

<sup>59</sup> *Store Your Bitcoins*, *supra* note 58 (“[Y]ou don’t technically *store* bitcoins anywhere. What you store are the secure digital keys used to access your public bitcoin addresses and sign transactions. This information is stored in a bitcoin wallet.”).

<sup>60</sup> Kaplanov, *supra* note 49, at 117.

<sup>61</sup> *How Does Bitcoin Work?*, BITCOIN, <https://bitcoin.org/en/how-it-works> (last visited Oct. 18, 2014) [hereinafter *How It Works*].

<sup>62</sup> Kaplanov, *supra* note 49, at 117.

<sup>63</sup> Jacobsen & Pena, *supra* note 58, at 41.

<sup>64</sup> See Kaplanov, *supra* note 49, at 118 (“[B]itcoin relies on other means to prevent double spending, including a timestamp server and a block chain to sequence all of the transaction records.”).

<sup>65</sup> *How It Works*, *supra* note 61.

<sup>66</sup> *Frequently Asked Questions*, *supra* note 52.

<sup>67</sup> *Id.*

<sup>68</sup> *Id.*

exchange their bitcoins for cash.<sup>69</sup> Finally, users can obtain bitcoins through a process called Bitcoin mining.<sup>70</sup>

A person engages in Bitcoin mining by downloading Bitcoin mining software.<sup>71</sup> Using the software, the miner inputs a transaction block that needs confirmation along with the most recent block transactions at the end of the most recent block chain.<sup>72</sup> The software then uses a mathematical algorithm to confirm the transactions and adds a new block onto the chain.<sup>73</sup> As an incentive for Bitcoin mining, the miner who correctly adds a new block to the block chain receives bitcoins.<sup>74</sup> However, because only twenty-one million bitcoins will ever be created,<sup>75</sup> the number of bitcoins a miner receives for his or her work decreases over time.<sup>76</sup> Currently, miners receive twenty-five bitcoins for each verified block.<sup>77</sup> In 2017, miners will receive 12.5 bitcoins for each verified block.<sup>78</sup> The amount of bitcoins rewarded for each successful block added will continue to decrease by half every four years.<sup>79</sup>

#### B. *Appeal of Bitcoin*

Using Bitcoin has many advantages. Transactions are almost instantaneous.<sup>80</sup> Even transferring bitcoins between wallets of users in different countries with different currencies can be done quickly.<sup>81</sup>

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<sup>69</sup> Dion, *supra* note 57, at 168.

<sup>70</sup> *Frequently Asked Questions*, *supra* note 52.

<sup>71</sup> Jacobsen & Pena, *supra* note 58, at 41.

<sup>72</sup> *Id.*

<sup>73</sup> *Id.*

<sup>74</sup> *How Bitcoin Mining Works*, COINDESK (March 6, 2014), <http://www.coindesk.com/information/how-bitcoin-mining-works/>.

<sup>75</sup> *Frequently Asked Questions*, *supra* note 52.

<sup>76</sup> Anthony Volastro, *CNBC Explains: How To Mine Bitcoins On Your Own*, CNBC (Jan. 23, 2014, 1:48 PM), <http://www.cnb.com/id/101332124#>.

<sup>77</sup> *Id.*

<sup>78</sup> *Id.*

<sup>79</sup> *Id.*

<sup>80</sup> *Frequently Asked Questions*, *supra* note 52.

<sup>81</sup> Sarah Gruber, Note, *Trust, Identity, and Disclosure: Are Bitcoin Exchanges the Next Virtual Havens for Money Laundering and Tax Evasion?*, 32 QUINNIPIAC

Transactions are also cheaper because the peer-to-peer network system eliminates the need for a third-party intermediary, who may require a transaction fee.<sup>82</sup> Rather than have a third party confirm the transaction, users verify each other's transactions through mining.<sup>83</sup>

Bitcoin's anonymity also appeals to many individuals.<sup>84</sup> Bitcoin transactions are recorded on a public ledger.<sup>85</sup> The recorded transactions are associated with the public key generated from a Bitcoin wallet.<sup>86</sup> However, the wallets themselves are not associated with a user's personal identification information, rendering these transactions virtually anonymous.<sup>87</sup>

Bitcoin is particularly attractive to users who want to engage in criminal activity.<sup>88</sup> Characteristics that make digital currencies, such as Bitcoin, advantageous to conducting criminal activity include anonymity and the ability of transactions to be conducted quickly regardless of the distance between users.<sup>89</sup> Use of digital currency has been linked to criminal activity such as the hiring of assassins, sale of cyber services used to hack businesses, sale of child pornography, sale of technology used to steal intellectual property, sex trafficking, drug trafficking, and counterfeiting identification documents such as passports.<sup>90</sup>

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L. REV. 135, 141–42 (2013); *see also Bitcoin For Individuals*, BITCOIN, <https://bitcoin.org/en/bitcoin-for-individuals> (last visited Oct. 20, 2014) (“Bitcoins can be transferred from Africa to Canada in 10 minutes.”).

<sup>82</sup> *Bitcoin for Individuals*, *supra* note 81 (“There is no bank to slow down the process, level outrageous fees, or freeze the transfer.”).

<sup>83</sup> Jacobsen & Pena, *supra* note 58, at 41.

<sup>84</sup> *See* Gruber, *supra* note 81, at 144 (“[T]o some, the resulting privacy of users is Bitcoin’s biggest attraction.”).

<sup>85</sup> *Id.*

<sup>86</sup> Dion, *supra* note 57, at 168.

<sup>87</sup> *Id.* (“Addresses contain no information about the user, but the public keys’ signature can be used to trace transactions. Thus, a Bitcoin can be traced through every address that held it; however, the ownership of each address remains anonymous.”).

<sup>88</sup> Trautman, *supra* note 51, at 4 (listing factors that the United States Secret Service has indicated for why digital currencies are attractive to criminals).

<sup>89</sup> *Id.* at 7.

<sup>90</sup> *Id.* at 5–7.

#### IV. AN ASSET YET TO BE CLASSIFIED: VARYING APPROACHES TO CATEGORIZING BITCOINS

Courts, legislatures, and executive entities have considered the legality of Bitcoin in case law, statutes, and regulations. Based on government actions and declarations to date, Bitcoin is unlikely to become an illegal form of currency.<sup>91</sup> If courts or other government entities wanted to declare Bitcoin illegal, they could have resorted to a host of constitutional and statutory provisions. Article I, Section 8 of the United States Constitution states that Congress has the power to coin and regulate currency.<sup>92</sup> Courts have interpreted this provision to mean that Congress can prohibit the circulation of any currency that it did not create.<sup>93</sup> Without the ability to prohibit counterfeit currency, Congress' constitutionally-granted power to regulate money in the United States would be "futile."<sup>94</sup>

The government could also have resorted to federal counterfeiting statutes that prohibit the creation of money that resembles dollars.<sup>95</sup> Legislatures created these statutes for the

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<sup>91</sup> See *United States v. Ulbricht*, No. 14-cr-68 (KBF), 2014 U.S. Dist. LEXIS 93093, at \*66–72 (S.D.N.Y. July 9, 2014) (rejecting defendant's claim that Bitcoin is not money sufficient to satisfy a criminal charge of money laundering); see also *SEC v. Shavers*, No. 4:13-CV-416, 2013 U.S. Dist. LEXIS 110018, at \*4–5 (E.D. Tex. Aug. 6, 2013) (rejecting the argument that Bitcoin is not money).

<sup>92</sup> U.S. CONST. art. I, § 8.

<sup>93</sup> *Veazie Bank v. Fenno*, 75 U.S. 533, 549 (1896) ("Congress may restrain, by suitable enactments, the circulation as money of any notes not issued under its own authority.").

<sup>94</sup> *Id.* ("Without this power, indeed, [Congress'] attempts to secure a sound and uniform currency for the country must be futile.").

<sup>95</sup> 18 U.S.C. § 471 (2012) ("Whoever, with intent to defraud, falsely makes, forges, counterfeits, or alters any obligation or other security of the United States, shall be fined under this title or imprisoned not more than 20 years, or both."); § 473 ("Whoever buys, sells, exchanges, transfers, receives, or delivers any false, forged, counterfeited, or altered obligation or other security of the United States, with the intent that the same shall be passed, published, or used as true and genuine, shall be fined under this title or imprisoned not more than 20 years, or both."); § 486 ("Whoever, except as authorized by law, makes or utters or passes, or attempts to utter or pass, any coins of gold or silver or other metal, or alloys of metals, intended for use as current money, whether in the resemblance of coins of the United States or of foreign countries, or of original



“protection of all currency and obligations of the United States.”<sup>96</sup> Being a currency, even of original design, that can “do damage to the value of the U.S. dollar and American monetary policy,”<sup>97</sup> Bitcoin may be in violation of these counterfeiting statutes.

Rather than declaring Bitcoin an illegal or counterfeit form of currency, courts and legislatures have focused on how to classify Bitcoin as an asset.<sup>98</sup> On this point, different government entities have developed various categorizations.<sup>99</sup>

#### A. *Judicial Interpretation at the Federal Level*

Recent court decisions seem to be trending towards classifying Bitcoin as currency. In *United States v. Ulbricht*,<sup>100</sup> the famous *Silk Road* case,<sup>101</sup> the court declared that Bitcoin was money for the

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design, shall be fined under this title or imprisoned not more than five years, or both.”).

<sup>96</sup> *United States v. LeMon*, 622 F.2d 1022, 1024 (10th Cir. 1980).

<sup>97</sup> *Dion*, *supra* note 57, at 172.

<sup>98</sup> *See United States v. Ulbricht*, No. 14-cr-68 (KBF), 2014 U.S. Dist. LEXIS 93093, at \*66–72 (S.D.N.Y. July 9, 2014) (rejecting defendant’s claim that Bitcoin is not money sufficient to satisfy a criminal charge of money laundering); *SEC v. Shavers*, No. 4:13-CV-416, 2013 U.S. Dist. LEXIS 110018, at \*4–5 (E.D. Tex. Aug. 6, 2013) (rejecting defendant’s argument that Bitcoin is not money and instead declaring that an investment in Bitcoin is akin to an investment in money).

<sup>99</sup> *See Ulbricht*, 2014 U.S. Dist. LEXIS 93093, at \*69–70 (comparing Bitcoin to money because, broadly defined, money is an object used to buy things, and the ability to use bitcoins to purchase items is the only reason Bitcoin has value); *Shavers*, 2013 U.S. Dist. LEXIS 110018, at \*5 (declaring that an investment in Bitcoin is akin to an investment in money); I.R.S. Notice 2014-21, 2014-16 I.R.B. 938–40 (declaring Bitcoin to be property, not currency).

<sup>100</sup> No. 14-cr-68 (KBF), 2014 U.S. Dist. LEXIS 93093 (S.D.N.Y. July 9, 2014).

<sup>101</sup> *See Ruth Reader*, *Still Don’t Get Bitcoin? This New Documentary Is For You*, VENTUREBEAT (Oct. 3, 2014, 8:44 AM), <http://venturebeat.com/2014/10/03/still-dont-get-bitcoin-this-new-documentary-is-for-you/> (reviewing a documentary, *The Rise and Rise of Bitcoin*, that walks through the history of Bitcoin, including the shutdown of Silk Road and Mt. Gox, a Bitcoin exchange); *see also Deep Web: The Untold Story of Bitcoin and Silk Road to Make World Premiere in 2015 on Epix*, MARKETWATCH (Sept. 30, 2014), <http://www.marketwatch.com/story/deep-web-the-untold-story-of-bitcoin-and-silk-road-to-make-world-premiere-in-2015-on-epix-2014-09-30> (announcing the release of a 2015 documentary

purpose of satisfying a criminal charge of money laundering.<sup>102</sup> In this case, the defendant, Ulbricht, created and administered a website called Silk Road to facilitate the sale of illegal narcotics.<sup>103</sup> Visitors to the site paid for transactions only in bitcoins.<sup>104</sup> Authorities discovered the criminal scheme and charged Ulbricht with participation in narcotics trafficking, computer hacking and money laundering conspiracies, and maintenance of a criminal enterprise.<sup>105</sup> The defendant attempted to dismiss the money laundering charge against him, claiming that Bitcoin was not technically money and thus the State could not charge him with money laundering.<sup>106</sup> The court rejected Ulbricht's argument<sup>107</sup> and declared Bitcoin to be money, comparing it to dollars and Euros.<sup>108</sup> It pointed to evidence that Bitcoin, like cash, can be used to pay for goods and services and can be exchanged for other currency.<sup>109</sup>

Similarly, in *United States v. Faiella*,<sup>110</sup> another *Silk Road* case, authorities charged the defendant with operating an unlicensed money transmitting business.<sup>111</sup> Like Ulbricht, Faiella moved to dismiss this charge.<sup>112</sup> He claimed that the United States could not charge him with operating an unlicensed money transmitting business because bitcoins do not qualify as money.<sup>113</sup> The court rejected this argument, holding that "Bitcoin clearly qualifies as 'money' or 'funds' under these plain meaning definitions. Bitcoin can be easily purchased in exchange for ordinary currency, acts as

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that will examine hidden content in the World Wide Web, focusing on the rise of Bitcoin and the arrest of the founder of Silk Road).

<sup>102</sup> *Ulbricht*, 2014 U.S. Dist. LEXIS 93093, at \*72.

<sup>103</sup> *Id.* at \*1.

<sup>104</sup> *Id.* at \*3.

<sup>105</sup> *Id.* at \*1-2.

<sup>106</sup> *Id.* at \*68-69.

<sup>107</sup> *Id.* at \*72.

<sup>108</sup> *Id.* at \*68.

<sup>109</sup> *Id.* at \*70.

<sup>110</sup> No. 14-cr-243 (JSR), 2014 U.S. Dist. LEXIS 116114 (S.D.N.Y. Aug. 18, 2014).

<sup>111</sup> *Id.* at \*1.

<sup>112</sup> *Id.*

<sup>113</sup> *Id.* at \*1-2.

a denominator of value, and is used to conduct financial transactions.”<sup>114</sup>

In *Securities and Exchange Commission v. Shavers*,<sup>115</sup> the defendant-appellant challenged the court’s subject matter jurisdiction pursuant to the Securities Act of 1933 and the Securities Exchange Act of 1934.<sup>116</sup> Shavers claimed that his actions in soliciting lenders to invest in Bitcoin did not constitute conduct governed by the Acts because Bitcoin is not money and, therefore, investing in it is not an investment in a security.<sup>117</sup> The court rejected the defendant’s argument here as well. The court determined that Bitcoin is money:

It is clear that Bitcoin can be used as money. It can be used to purchase goods or services, and . . . used to pay for individual living expenses . . . . [I]t can also be exchanged for conventional currencies, such as the U.S. dollar, Euro, Yen, and Yuan. Therefore, Bitcoin is a currency or form of money, and investors wishing to invest in [Bitcoin Savings and Trust] provided an investment of money.<sup>118</sup>

Thus, the court considered an investment in Bitcoin equivalent to an investment in money and subject to the Securities Acts of 1933 and the Securities Exchange Act of 1934.<sup>119</sup>

## B. *Statutory Classifications*

States have varying approaches to classifying Bitcoin. Several states have declared that Bitcoin is money and can therefore be governed by state statutes that regulate monetary transactions.<sup>120</sup> The North Carolina Commission of Banks, North Carolina’s primary financial regulatory agency, has proposed treating Bitcoin as money within the scope of the North Carolina Money Transmitters Act.<sup>121</sup> This Act mandates entities engaged in money

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<sup>114</sup> *Id.* at \*3.

<sup>115</sup> No. 4:13-CV-416, 2013 U.S. Dist. LEXIS 110018 (E.D. Tex. Aug. 6, 2013).

<sup>116</sup> *Id.* at \*1.

<sup>117</sup> *Id.* at \*4.

<sup>118</sup> *Id.*

<sup>119</sup> *Id.* at \*6.

<sup>120</sup> See *infra* notes 121–31 and accompanying text.

<sup>121</sup> Taylor Tyler, *North Carolina Taking Different Approach to Regulating Virtual Currencies, No BitLicense Required*, COINFINANCE (Aug. 26, 2014, 10:00 AM), <http://www.coinfinance.com/news/north-carolina-taking-different-approach->

transmissions to register and receive a license from the state.<sup>122</sup> Monetary transmissions include “[t]he sale or issuance of payment instruments or stored value” and “[t]he act of engaging in the business of receiving money or monetary value for transmission within the United States or to locations abroad by any and all means, including payment instrument, wire, facsimile, or electronic transfer.”<sup>123</sup> A spokeswoman for the North Carolina Commission of Banks further specified that “[a]t a minimum, any entity that receives virtual currency for transmission to a third party or holds funds incidental to the transmission of virtual currency to a third party will be expected to apply for a license.”<sup>124</sup> Even companies that are not physically located in North Carolina are bound by the licensure requirement.<sup>125</sup> Bitcoin transactions are monetary transmissions because Bitcoin issues virtual currency, which holds value<sup>126</sup> and can be used as payment instruments.<sup>127</sup> Additionally, users can transfer bitcoins to other users and third parties within the United States or abroad.<sup>128</sup>

Likewise, California has also opened the door to recognizing digital currencies, such as Bitcoin, as legal money by passing Assembly Bill No. 129.<sup>129</sup> This amendment repeals an act that prohibited the issuing or placing into circulation of any currency that was not the “lawful money of the United States.”<sup>130</sup> Prior to

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to-regulating-virtual-currencies#.U\_zQFMBd7Ss.reddit; *see also* Money Transmitters Act, N.C. GEN. STAT. § 53-208 (2013).

<sup>122</sup> § 53-208.3(a).

<sup>123</sup> § 53-208.2(a)(11).

<sup>124</sup> Tyler, *supra* note 121.

<sup>125</sup> § 53-208.3(c) (“For the purposes of this Article, a person is considered to be engaged in the business of money transmission in this State if that person makes available, from a location inside or outside of this State, an Internet website North Carolina citizens may access in order to enter into those transactions by electronic means.”).

<sup>126</sup> *See, e.g., Frequently Asked Questions, supra* note 52 (“Bitcoins have value because they are useful as a form of money.”).

<sup>127</sup> *See id.* (stating that bitcoins can be used to purchase goods and services).

<sup>128</sup> *See* Gruber, *supra* note 81, at 141 (stating that bitcoins can be transferred instantaneously to users anywhere in the world).

<sup>129</sup> Assemb. B. No. 129, 2013-24 Sess. (Cal. 2014).

<sup>130</sup> *Id.*

this repeal, Bitcoin was prohibited because it is not currency distributed by the United States.<sup>131</sup> With this new bill, even though Bitcoin is not distributed by the United States government, the circulation of bitcoins will not be prohibited in California.

In contrast to North Carolina's and California's treatment of Bitcoin as currency, the Internal Revenue Service ("IRS") issued a notice in March of this year declaring that Bitcoin will not be treated as currency.<sup>132</sup> Rather, the IRS categorizes Bitcoin as property.<sup>133</sup> The Service defined virtual currency as a "digital representation of value that functions as a medium of exchange, a unit of account, and/or a store of value."<sup>134</sup> While the IRS conceded that "[i]n some environments, it operates like 'real' currency," the Service nonetheless concluded that Bitcoin "does not have legal tender status in any jurisdiction."<sup>135</sup> Real currency is "the coin and paper money of the United States or of any other country that is designated as legal tender, circulates, and is customarily used and accepted as a medium of exchange in the country of issuance."<sup>136</sup> Thus, because Bitcoin is a virtual currency and does not have legal tender status, Bitcoin is not real currency.<sup>137</sup>

Texas followed in the footsteps of the IRS when its Department of Banking published a memorandum in April of this year declaring that the state would not recognize Bitcoin as money.<sup>138</sup>

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<sup>131</sup> See Trautman, *supra* note 51, at 48 ("Bitcoin is not backed by a government or legal entity.") (quoting Nicholas Plassaras, *Regulating Digital Currencies: Bringing Bitcoin Within the Reach of the IMF*, 14 CHI. J. INT'L L. 377, 383 (2013)).

<sup>132</sup> I.R.S. Notice 2014-21, 2014-16 I.R.B. 938-40.

<sup>133</sup> *Id.*

<sup>134</sup> *Id.*

<sup>135</sup> *Id.*

<sup>136</sup> *Id.*

<sup>137</sup> *Id.*

<sup>138</sup> Supervisory Memorandum – 1037 from Charles G. Cooper, Banking Commissioner, Tex. Dep't of Banking, to All Virtual Currency Companies Operating or Desiring to Operate in Texas (Apr. 3, 2014), *available at* <http://www.dob.texas.gov/public/uploads/files/consumer-information/sm1037.pdf> ("Cryptocurrencies as currently implemented cannot be considered money or monetary value under the Money Services Act.").

Rather, Texas would recognize Bitcoin transactions as exchanges of goods.<sup>139</sup>

## V. PROPOSED CATEGORIZATION AND REGULATION OF BITCOIN

Defining a clear categorization for Bitcoin can potentially help equitable distribution proceedings in two ways. First, it will establish that Bitcoin is a form of asset that needs to be reported on equitable distribution inventories. Second, depending on how Bitcoin is categorized, the asset may be subject to certain government regulations that will allow Bitcoin transactions to be more transparent and easier to discover.

### A. *Benefits of Classifying Bitcoin*

Clarification of Bitcoin's asset type will reduce confusion regarding if and how spouses should report bitcoins on equitable distribution inventory affidavits.<sup>140</sup> Equitable distribution inventory affidavits ask divorcing parties to list their assets according to the category of the asset.<sup>141</sup> For example, the section to list investments may be different from the section to list cash. Without a clear definition of how to categorize Bitcoin, parties may not know where to report bitcoins or even if bitcoins are reportable assets. Additionally, some affidavits require submission of statements and other documents as evidence of the asset's existence and value.<sup>142</sup> Because Bitcoin transactions are recorded on a public ledger and records are not associated with the Bitcoin owner's identification, parties who do not have access to their spouse's Bitcoin wallet may be deterred from reporting the asset. Establishing a bright line rule will preclude individuals who own bitcoins from claiming ignorance of the need to report these assets and will encourage divorcing parties to report when their spouse is holding bitcoins.

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<sup>139</sup> *Id.*

<sup>140</sup> A sample equitable distribution inventory affidavit is available at <http://www.nccourts.org/Courts/CRS/Policies/LocalRules/Documents/744.pdf>.

<sup>141</sup> *Id.* (asking parties to categorize and report assets in charts specified for each category of property).

<sup>142</sup> *Id.*

Additionally, by defining a clear categorization for Bitcoin, the government can apply existing regulations to monitor Bitcoin transactions. Existing regulations could help parties better discover the assets their spouses hold and the value of those assets. This transparency will help courts determine the accurate value of *all* marital and divisible property and determine a division of property that is equitable.

*B. Classification of Bitcoin as Cash for Equitable Distribution Proceedings*

Government entities have proposed various classifications of Bitcoin. Some analogize the asset to cash.<sup>143</sup> If the federal and state governments classified Bitcoin as cash, Bitcoin would be relatively unregulated. Cash transfers happen every day without monitoring. However, if someone were to remove a large amount of cash from a bank account, the withdrawal or transfer would be traceable through bank statements. Unlike cash though, unregulated Bitcoin transactions are untraceable, making it impossible to tell even the amount of currency that a party once held. No amount of forensic accounting could show if a party had transferred or withdrawn bitcoins in order to prevent the court from equitably distributing them upon divorce. It is even unnecessary to withdraw a large sum of traditional currency to purchase bitcoins because the mining process allows bitcoins to be obtained without a spouse ever finding out.<sup>144</sup>

*C. Classification of Bitcoin as Personal Property for Equitable Distribution Proceedings*

An alternative to treating bitcoins as cash would be to treat them as personal property or commodities with inherent value. Treating bitcoins as personal property would still leave transactions of the asset relatively unregulated and untraceable. Exchanges of goods and purchases of personal property often

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<sup>143</sup> See, e.g., Kaplanov, *supra* note 49, at 153 (“A better characterization of the bitcoin technology is nothing more than storing cash under a mattress . . .”).

<sup>144</sup> See *Frequently Asked Questions*, *supra* note 52 (stating that one method of obtaining bitcoin is through mining).

occur without leaving traceable documents, such as receipts, and often do not require the purchaser or seller to report the transaction to any government authority, such as the IRS. For example, purchases at a neighbor's yard sale or purchasing an item from a friend is not often reported on to the government and may not even leave behind receipts to be traced. Additionally, treating bitcoins as personal property would not reflect that bitcoins do not have inherent values<sup>145</sup> and their value is volatile.<sup>146</sup>

Recognition that Bitcoin does not have an inherent value and that its value fluctuates can have important implications for equitable distribution. If Bitcoin is valued on its date of purchase and its value decreases or increases significantly by the date of distribution, the party attempting to hide his or her bitcoins could be significantly gaining or losing if the current value of the Bitcoin is not being taken into account in the equitable distribution proceeding.

#### D. *Classification of Bitcoin as Security for Equitable Distribution Proceedings*

The Securities Exchange Act of 1934 has defined the types of assets that are considered securities:

Any note, stock, treasury stock, security future, security-based swap, bond, debenture, certificate of interest or participation in any profit-sharing agreement or in any oil, gas, or other mineral royalty or lease, any collateral-trust certificate, preorganization certificate or subscription, transferable share, *investment contract*, voting-trust certificate, certificate of deposit for a security, any put, call, straddle, option, or privilege on any security, certificate of deposit, or group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option, or privilege entered into a national securities exchange relating to foreign currency, or in general, any instrument commonly known as a "security"; or any certificate of interest or participation, temporary or interim certificate for, receipt for, or warrant or right to subscribe to or purchase, any of the foregoing; but shall not include currency or any note, draft, bill of exchange, or banker's acceptance which has a maturity at the time of issuance of not

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<sup>145</sup> See *id.* ("The price of a bitcoin is determined by supply and demand.").

<sup>146</sup> *You Need To Know*, *supra* note 54.



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exceeding nine months, exclusive of days of grace, or any renewal thereof of the maturity of which is likewise limited.<sup>147</sup>

Bitcoin is a security because it falls under the purview of an investment contract.<sup>148</sup> An investment contract is “[a] contract in which money is invested in a common enterprise with profits to come solely from the efforts of others.”<sup>149</sup>

First, the purchase of bitcoins may serve as an investment. Users can sell bitcoins for either a profit or loss when their value appreciates or depreciates.<sup>150</sup> Even mining bitcoins is an investment of money because miners pay for the electricity and computing power necessary for mining.<sup>151</sup>

Second, an investment into Bitcoin is a common enterprise.<sup>152</sup> There are multiple ways to define a common enterprise.<sup>153</sup> A common enterprise could mean that (1) multiple users pool their interests and money together in a common venture and all users encounter the same risks and rewards of their investment, (2) investors’ returns depend on promoters’ actions, or (3) “gains or losses of both the promoters and the investors are correlated.”<sup>154</sup>

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<sup>147</sup> Securities Exchange Act of 1934, 15 U.S.C. § 78(c)(10) (2012) (emphasis added).

<sup>148</sup> See *infra* notes 149–66 and accompanying text.

<sup>149</sup> BLACK’S LAW DICTIONARY 954 (10th ed. 2014); see also SEC v. W.J. Howey Co., 328 U.S. 293, 301 (1946).

<sup>150</sup> Todd P. Zerega & Thomas H. Watterson, *United States: Regulating Bitcoins: CFTC vs. SEC?*, MONDAQ (Jan. 2, 2014), <http://www.mondaq.com/unitedstates/x/283878/Commodities+Derivatives+Stock+Exchanges/Regulating+Bitcoins+CFTC+vs+SEC>.

<sup>151</sup> Yang, *supra* note 49, at 109–10 (arguing that the first element of an investment contract, an investment of money, is met when individuals mine for bitcoins because individuals are putting their money into paying for electricity and computers in hopes of receiving a return of bitcoins).

<sup>152</sup> *Id.* at 112; see also Zerega & Watterson, *supra* note 150 (“An investment of money in Bitcoin could have ‘commonality’ from multiple sources. The ‘investors’ in Bitcoin share in the appreciation or depreciation of Bitcoin. Moreover, the ‘investors’ in Bitcoin share in the benefits of Bitcoin’s programming and cryptography, which are essential to the ability to sell Bitcoins in the future.”).

<sup>153</sup> Yang, *supra* note 49, at 111–12.

<sup>154</sup> *Id.*

Under all three definitions, Bitcoin is a common enterprise.<sup>155</sup> Bitcoin users buy into the currency and, when the value of Bitcoin fluctuates, all Bitcoin users share in the asset's appreciation or depreciation of value.<sup>156</sup> Owners of bitcoins also depend on promoters for appreciation in the value of their bitcoins because promoter companies, such as the Bitcoin Foundation, attract new investors to buy into Bitcoin.<sup>157</sup> Given there is a finite number of bitcoins, the higher the demand for—and lower the supply of—bitcoins, the more each individual bitcoin is worth.<sup>158</sup> Likewise, promoters depend on the investors, and the gains and losses of both parties are correlated.<sup>159</sup> Some promoters take transaction fees when facilitating the exchange of Bitcoin for other assets, such as currency.<sup>160</sup> If the value of Bitcoin declines and individuals are no longer interested in purchasing bitcoins, promoters will have fewer transactions to conduct, and thus, less fees that they can collect.<sup>161</sup> Conversely, if the value of Bitcoin appreciates and more individuals purchase bitcoins, promoters will conduct more transactions and collect more fees.<sup>162</sup>

Lastly, profits from any appreciation of the value of bitcoins come solely from the efforts of others because supply and demand

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<sup>155</sup> See *id.* at 111–14 (finding that Bitcoin meets the different definitions of common enterprise because (1) users of Bitcoin share common risks and rewards, (2) Bitcoin Foundation serves as a promoter that helps attract new Bitcoin users to make Bitcoin investments more valuable, and (3) promoters' losses and gains are correlated with investors' losses and gains because when investors' bitcoins are worth less, the promoter receives less in transaction fees).

<sup>156</sup> Zerega & Watterson, *supra* note 150.

<sup>157</sup> Yang, *supra* note 49, at 112–13 (“[T]he promoter spends considerable effort attracting new participants who are then incentivized to recruit additional participants because the additional participants make their original investment in BitCoin more valuable since the enterprise feeds off of a common trust, whether or not that trust is misplaced.”).

<sup>158</sup> *Frequently Asked Questions*, *supra* note 52.

<sup>159</sup> Yang, *supra* note 49, at 113–14.

<sup>160</sup> *Id.* at 113 (noting that Bitcoin Foundation, a chief promoter of Bitcoin, and the promoter's commercial entities, such as Mt. Gox, took transaction fees when conducting transactions between Bitcoin and real currency).

<sup>161</sup> *Id.* at 114.

<sup>162</sup> *Id.*

by the public determines the value of a bitcoin.<sup>163</sup> The greater the demand for bitcoin and the fewer the supply of bitcoins, the more bitcoins will be worth.<sup>164</sup> Conversely, the opposite is also true.<sup>165</sup> Thus, the value of Bitcoin depends upon other users' use of bitcoins and the ability of Bitcoin miners to verify transactions and mine more bitcoins.<sup>166</sup>

#### *E. Benefits of Classifying Bitcoin as a Security*

Classifying Bitcoin as a security will best serve the true purpose of equitable distribution statutes. First, defining Bitcoin as a security will subject the asset to regulations by securities regulating entities, such as the Securities and Exchange Commission ("SEC") and state regulatory commissions, which will help parties better discover the number of bitcoins their spouse owns. Second, defining Bitcoin as a security, and more specifically an investment, will reflect the fluctuating value of the digital currency.<sup>167</sup>

##### *1. Discovering Bitcoin*

Classifying Bitcoin as a security will subject the asset to rules that would facilitate one spouse discovering and valuing the other spouse's bitcoins. First, an individual would be required to report the income earned from the purchase and sale of Bitcoin investment on income tax filings.<sup>168</sup> When a party is investigating a spouse's assets, he or she could ask for copies of income tax returns and examine the filings to determine if his or her spouse

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<sup>163</sup> See *Frequently Asked Questions*, *supra* note 52 ("The price of a bitcoin is determined by supply and demand.").

<sup>164</sup> *Id.*

<sup>165</sup> *Id.*

<sup>166</sup> Zerega & Watterson, *supra* note 150.

<sup>167</sup> See *You Need To Know*, *supra* note 54 ("The price of a bitcoin can unpredictably increase or decrease over a short period of time due to its young economy, novel nature, and sometimes illiquid market. Consequently, keeping your savings with Bitcoin is not recommended at this point. Bitcoin should be seen like a high risk asset, and you should never store money that you cannot afford to lose with Bitcoin.").

<sup>168</sup> See INTERNAL REVENUE SERV., FORM 1040 INSTRUCTIONS 20 (2013), available at <http://www.irs.gov/pub/irs-pdf/i1040.pdf> (instructing that generally all income must be reported).

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has made investments of which the party is not aware. If a spouse has previously profited from selling bitcoins, this profit would prompt a spouse or his or her attorney to inquire further as to whether the opposing spouse has any more bitcoins.

Additionally, as a security, Bitcoin could be subject to the rules and regulations promulgated by entities charged with securities regulation. Increased regulation could require more documentation of Bitcoin transactions, which would leave more traceable documents that a divorcing spouse could investigate to determine if his or her spouse holds bitcoins.

If the federal government recognizes Bitcoin as a security, the SEC could bring Bitcoin transactions under the purview of existing legislation, particularly the Securities Act of 1933 and the Securities Exchange Act of 1934.<sup>169</sup> A major problem that arises with regulating Bitcoin under these statutes is that Bitcoin lacks a central authority.<sup>170</sup> Without a principal that monitors the issuance of Bitcoin, identifying who would be required to comply with the requirements of the statutes would be unclear.

For instance, under the Securities Act of 1933, corporations must register their securities.<sup>171</sup> Usually, the central authority

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<sup>169</sup> 15 U.S.C. §§ 78a–78pp (2012).

<sup>170</sup> *But see* Yang, *supra* note 49, at 112–13 (arguing that BitCoin Foundation, one of Bitcoin’s primary promoters, is in fact the centralized agency that controls Bitcoin).

<sup>171</sup> § 77e(a) (2012) (“Unless a registration statement is in effect as to a security, it shall be unlawful for any person, directly or indirectly (1) to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to sell such security through the use or medium of any prospectus or otherwise; or (2) to carry or cause to be carried through the mails or in interstate commerce, by any means or instruments of transportation, any such security for the purpose of sale or for delivery after sale.”); *id.* § 77f (“Any security may be registered with the Commission under the terms and condition hereinafter provided, by filing a registration statement in triplicate, at least one of which shall be signed by each issuer, its principal executive officer or officers, its principal financial officer, its comptroller or principal accounting officer, and the majority of its board of directors or persons performing similar functions (or, if there is no board of directors or persons performing similar functions, by the majority of the persons or board having the power of management of the issuer), and in case the issuer is a foreign or Territorial person by its duly authorized representative in the United States; except that

issuing the security is the entity that must register with the SEC.<sup>172</sup> However, because of Bitcoin's decentralization, the entity "issuing" the security is unclear. Multiple miners are acquiring new bitcoins through the mining process rather than buying the assets from a central authority. However, as miners find more bitcoins, the problem of having thousands of miners issuing bitcoins may become smaller as mining becomes less prevalent among the public and more concentrated in groups of users.

As miners add more blocks to the block chain of transactions, the algorithms become more complicated and take greater computing resources.<sup>173</sup> To address these increasing difficulties with mining, groups of miners have united to form mining pools.<sup>174</sup> Miners in mining pools share their computing resources and receive a share of the award when a block is successfully mined.<sup>175</sup> Currently, the biggest mining pool, Ghash.io, controls over thirty percent of the Bitcoin mining power, and if its power continues to grow, Ghash.io could monopolize the mining industry and make verifying other miners' blocks impossible.<sup>176</sup> Although the company has recently stated it will not monopolize the Bitcoin mining power,<sup>177</sup> it theoretically could obtain a monopoly over mining bitcoins and distributing them out to the public. This would be

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when such registration statement relates to security issued by a foreign government or political subdivision thereof, it need be signed only by the underwriter of such security.”).

<sup>172</sup> See § 77f.

<sup>173</sup> *Bitcoin Mining Pools*, BITCOINMINING.COM, <http://www.bitcoinmining.com/bitcoin-mining-pools/> (last visited Oct. 21, 2014).

<sup>174</sup> *Id.*

<sup>175</sup> *Id.*

<sup>176</sup> Pete Rizzo, *Ghash.io: We Will Never Launch a 51% Attack Against Bitcoin*, COINDESK (June 16, 2014, 8:06 PM), <http://www.coindesk.com/ghash-io-never-launch-51-attack/> (“Should Ghash.io reach and maintain 51% of the bitcoin network, the mining pool would theoretically be able to perform certain actions uncontested, such as double spending individual bitcoins, preventing transaction confirmations and obstructing other miners and mining pools from profiting from valid blocks.”).

<sup>177</sup> *Id.* (stating that Ghash.io has announced that they will not engage in an attack against Bitcoin).

similar to a corporation authorizing and issuing shares to the public.

In addition to regulating miners, the SEC could also regulate entities that operate as Bitcoin exchanges.<sup>178</sup> The SEC defines exchange to mean “any organization, association, or group of persons, whether incorporated or unincorporated, which constitutes, maintains, or provides a market place or facilities for bring together purchasers and sellers of securities.”<sup>179</sup> Under this definition, Bitcoin exchanges are exchanges because they are entities that allow buyers and sellers of bitcoins to come together.

Even Bitcoin users who simply buy and use bitcoins without engaging in mining could be regulated by the SEC as issuers of securities. An issuer is any person “who issues or proposes to issue any security.”<sup>180</sup> When purchasing items with bitcoins or selling portions of bitcoins, a Bitcoin user is providing bitcoins to the public and is thus issuing a security.

By allowing the SEC to regulate Bitcoin users, miners, and Bitcoin exchanges, the SEC could help Bitcoin transactions become more transparent and easier to discover. The law could require individuals and entities using Bitcoin to register with the SEC. The SEC could also require certain exchanges to disclose certain reports to account holders. Parties who suspect their spouses of engaging in Bitcoin transactions could take notice of whether their spouses receive letters or emails from Bitcoin mining companies, exchanges, or the SEC. Additionally, if a party knows his or her spouse owns Bitcoin, but needs to prove the value of the Bitcoin,<sup>181</sup> he or she can present the family court with the mining company’s or Bitcoin exchange’s annual reports made to the SEC detailing the entity’s finances.

If Bitcoin transactions by some users do not fall under federal securities laws’ purview, the state could also step in with its own regulations. The North Carolina General Assembly enacted the

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<sup>178</sup> See *supra* notes 68–69 and accompanying text for more information on Bitcoin exchanges.

<sup>179</sup> 15 U.S.C. § 78c(a)(1) (2012).

<sup>180</sup> § 77b(a)(4).

<sup>181</sup> See *supra* notes 31–38 and accompanying text.

North Carolina Securities Act to govern security transactions within the state.<sup>182</sup> Like federal securities regulations, the North Carolina Securities Act requires individuals who are offering or selling securities to register with the state.<sup>183</sup> Similar to searching for documents related to federal securities registration, parties who suspect their spouse of using Bitcoin may be able to find indication that their spouse is holding this type of asset by searching for correspondence between their spouse and the state regarding Bitcoin registration.

## 2. *Reflection of Bitcoin's Volatile Value in Equitable Distribution*

An investment contract is also defined as “[a] transaction in which an investor furnishes initial value or risk capital to an enterprise, a portion of that amount being subjected to the risks of the enterprise.”<sup>184</sup> Categorizing Bitcoin as an investment contract signals that its value fluctuates and that the amount of value put into purchasing bitcoins can appreciate or depreciate. In North Carolina in particular, the change in value of an asset has a large impact on determining how to divide property equitably. When a property’s value does not change between the date of separation and date of distribution, the property is purely marital property and will be valued on the date of separation.<sup>185</sup> However, when the value of an asset changes between the date of separation and the date of distribution of property, the court will consider the change in value as divisible property and value the asset on the date of distribution.<sup>186</sup> For instance, if the value of a couple’s bitcoins fluctuates between the date of separation and the date of distribution, the appreciation or depreciation in value will be considered divisible property and will be valued on the date of distribution.<sup>187</sup>

Recognizing the inherent volatility of the Bitcoin market, consider a case where the value increases significantly in the two

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<sup>182</sup> N.C. GEN. STAT. § 78A (2013).

<sup>183</sup> § 78A-24.

<sup>184</sup> BLACK’S LAW DICTIONARY 954 (10th ed. 2014).

<sup>185</sup> N.C. GEN. STAT. § 50-21(b) (2013).

<sup>186</sup> *Id.*

<sup>187</sup> *Id.*

years between the date of separation and date of property distribution. In this scenario, the court awards one spouse (Spouse A) the total sum of the bitcoin, and in exchange, the other spouse (Spouse B) receives something of equal value, according to the value of the bitcoins at the time of separation. Because the bitcoins have appreciated in value by the date of distribution, Spouse A will gain significantly more from the property division than Spouse B. On the other hand, if the court considered bitcoins as securities and considered their change in value, the court could classify the change in value of the bitcoins as divisible property and value the assets on the date of distribution. This categorization would allow consideration of any appreciation in the bitcoins' value, ensuring a more equitable distribution of property. Likewise, this method also allows courts to consider any depreciation of bitcoins' value.

## VI. CONCLUSION

Divorces are difficult and cumbersome. In contentious divorces, property division can be a long and bitter process. In their efforts to divide property more fairly, North Carolina and most other states have adopted equitable distribution statutes. However, the anonymity and lack of regulation behind digital currency threatens the ability of courts to actually enforce a fair and equitable distribution of property.

Developing a clear classification for Bitcoin is one of the first steps that the state can take to decrease the ability of spouses to hide assets in Bitcoin. If Bitcoin is formally classified, divorcing spouses who fail to report bitcoins on their marital asset inventory affidavit cannot excuse their behavior by claiming they did not know they had to report it.

Bitcoin can be classified in many ways: cash, security, personal property, or even counterfeit currency. This Recent Development suggests that classifying Bitcoin as a security will best effectuate the purpose of equitable distribution. By labeling Bitcoin a security, the government can regulate Bitcoin through the Securities and Exchange Commission and state legislatures, such as the North Carolina General Assembly. Increased regulations requiring more documentation of Bitcoin transactions will aid



lawyers, courts, and spouses in finding hidden assets and incorporating these assets' values when making equitable distribution calculations. Additionally, categorizing Bitcoin as a security, more specifically an investment contract, is more reflective of the instability of Bitcoin's value and will allow courts to consider Bitcoin's fluctuating value in determining when and how to appraise the asset. This is especially important in North Carolina where marital property will be valued on the date of separation unless a divorcing party can show the asset's value has changed between date of separation and date of distribution. Determining the accurate value of each party's assets will help courts order a truly equitable division of property.

New technologies, especially ones with the potential to threaten financial stability, can be frightening. However, "in a supportive and regulated environment . . . , these technologies can grow to something great."<sup>188</sup> As digital currency continues to become increasingly anonymous,<sup>189</sup> enacting and enforcing regulations will prove to be no easy task. Nonetheless, it is a task that courts and legislatures must face to ensure that divorcing parties are receiving an equitable distribution of property.

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<sup>188</sup> Kye White, *ATO Guidance On GST Treatment Of Bitcoin At The Top Of Agenda As Senate Inquiry Is Officially Announced*, STARTUPSMART (Oct. 2, 2014), <http://www.startupsmart.com.au/government-and-regulation/ato-guidance-on-gst-treatment-of-bitcoin-at-the-top-of-senates-agenda-as-inquiry-is-officially-announced.html> (quoting Holger Arians) (internal quotation marks omitted).

<sup>189</sup> A new application, Dark Wallet, has been developed to increase the privacy and anonymity behind Bitcoin transactions. While Bitcoin is anonymous, it is not private because each transaction's public transaction number traces transactions back to the Bitcoin wallet's identification. Dark Wallet seeks to make each transaction anonymous and private. For a discussion on how Dark Wallet is attempting to make digital currency transactions even more difficult to trace and impossible for government to regulate, see Andy Greenberg, *Dark Wallet Aims To Be The Anarchist's Bitcoin App Of Choice*, FORBES (Oct. 31, 2013, 9:40 AM), <http://www.forbes.com/sites/andygreenberg/2013/10/31/darkwallet-aims-to-be-the-anarchists-bitcoin-app-of-choice/>; Andy Greenberg, *'Dark Wallet' Is About to Make Bitcoin Money Laundering Easier Than Ever*, WIRED (Apr. 29, 2014, 6:11 PM), <http://www.wired.com/2014/04/dark-wallet/>.