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HOLDING CRYPTOCURRENCY – IS YOUR WALLET HOT?

Consider Whether Your Assets Are Insured Under a Homeowner's or Commercial Policy

Many individuals and businesses hold some amount of cryptocurrency. Since the first Bitcoin was "mined" in 2009, nearly 10% of Americans have invested in cryptocurrency according to a recent survey. And, along with the rise in prevalence of virtual currencies in recent years has come a surge in cryptocurrency theft, with one Ponzi scheme defrauding cryptocurrency investors out of \$2.9 billion dollars in 2019. Those who invest in, use and hold cryptocurrency should protect their assets. Sometimes that includes insurance, but individuals may have difficulty obtaining coverage for their cryptocurrency.

Bitcoin is just one cryptocurrency built on the technology called the blockchain. Other virtual currencies include Ethereum, Ripple, Litecoin, Monero, and ZCash.

INDIVIDUAL CURRENCY OWNERS AND HOMEOWNER'S INSURANCE

Homeowner's insurance protects the insureds against the loss of certain property. For example, a thief breaks

into your home and steals your television. That loss will likely be a covered loss of property under a standard homeowner's policy. But, are owners of cryptocurrency insured if a thief hacks their computer and steals their virtual currency? Is that a covered loss?

Part of the answer relates to the question – what is cryptocurrency? Are these virtual currencies a security, money, property, a commodity, or something else?

The Securities and Exchange Commission's position is that cryptocurrency is, or at least can be, a "security," cautioning that "issuers [of virtual currencies] cannot avoid the federal securities laws just by labeling their product a cryptocurrency or a digital token." On the other hand, the IRS has issued Notice 2014-21, identifying cryptocurrency as "property" for federal income tax purposes. Still a third possibility is that cryptocurrency, which can be used to purchase goods and services, is properly classified as money.

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With the uncertain classification of cryptocurrency in mind, could it be covered by homeowner's insurance? We are unaware of any homeowners' insurance policies that specifically address the loss of cryptocurrency. Thus, the loss may not be covered or it would be silently covered if the currency is classified as something else that the policy does name as a covered loss.

At least one court, however, has ruled that cryptocurrency may be covered by homeowner's policies. In *Kimmelman v. Wayne Insurance Group*, No. 18-CV-1041 (Sept. 25, 2018), an insured submitted a claim under his homeowner's policy for approximately \$16,000 in stolen bitcoin. The insurer took the position that cryptocurrency was "money" and covered under the policy. However, the policy had a sublimit of \$200 for monetary losses under the policy. When the insurer refused to pay the full \$16,000 claim, the insured brought suit alleging breach of contract and bad faith. The insurer then moved for judgment on the pleadings. The Ohio trial court denied the insurer's motion for judgment on the pleadings, relying on IRS ruling 2014-21, and holding that cryptocurrency is property, not money, and therefore the loss was covered and was not subject to the \$200 monetary loss limit.

While it remains to be seen whether Kimmelman will ultimately prevail on his claim after appeals, the court's ruling

nevertheless suggests that absent an effective exclusion, cryptocurrency losses may be covered as property under homeowner's policies.

COMMERCIAL INSURANCE FOR BUSINESSES OWNING VIRTUAL CURRENCY

For businesses, there are different considerations and other types of insurance available, including commercial crime policies and standalone cyber insurance policies.

A commercial crime policy may cover the actual cash value of the loss resulting from a cryptocurrency theft. However, insureds should read their commercial crime policies carefully before a loss if the loss of cryptocurrency is something they wish to insure against. The standard ISO commercial crime form broadly excludes losses involving digital, crypto, and other types of electronic currency. The ISO form does, however, include an optional endorsement that specifically covers virtual currency. The ISO form also deals with the murky issue of how cryptocurrency, which is extremely volatile, should be valued. It provides that loss is measured according to the market value on the date the insured discovered the loss.

Regardless of whether a business has crime insurance, they should also purchase

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This publication is a summary of legal principles. Nothing in this article constitutes legal advice, which can only be obtained as a result of a personal consultation with an attorney. The information published here is believed accurate at the time of publication, but is subject to change and does not purport to be a complete statement of all relevant issues.

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a standalone cyber policy that covers a cryptocurrency loss caused by a cyber-attack (among the many other reasons for purchasing cyber insurance). There is no standard cyber policy, therefore insureds should consider whether there is coverage under their policy for the cash value of stolen cryptocurrency since some policies may not cover cryptocurrency losses.

IS YOUR WALLET HOT?

Another consideration is how the owner stores the cryptocurrency – “hot” storage vs. “cold” storage. Cryptocurrency stored using “hot” storage is stored or accessed online, and therefore more vulnerable to theft by hacking or ransomware attacks.

On the other hand, currency stored using “cold” storage is stored offline (for example, on a flash drive). Cold storage is vulnerable to physical destruction or old-fashioned theft but less likely to be compromised via a cyber-attack. Some owners will have a third party hold their cryptocurrency in a digital hot wallet. If that is your storage decision, consider asking whether the holder of the cryptocurrency is insured.

Owners should consider the relative advantages of their storage choices and how the risks align with their insurance program. Businesses should consult with their risk manager and a trusted broker to obtain insurance that best fits their needs.