
VALUING CRYPTOCURRENCY, NFTS, AND OTHER DIGITAL ASSETS IN A DIVORCE: AN ANALYSIS FOR CALIFORNIA FAMILY LAW PRACTITIONERS

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INTRODUCTION

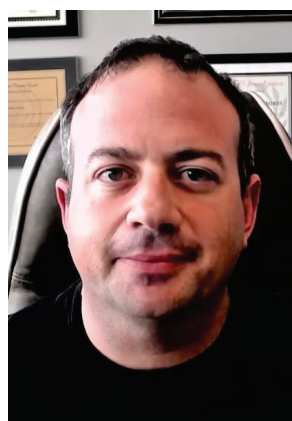
In the past decade, the financial landscape has witnessed a transformative evolution with the rise of digital assets. Cryptocurrencies like Bitcoin and Ethereum have transitioned from the fringes of the tech world into mainstream acceptance, gaining not only in value but also in popularity. Parallel to this phenomenon is the emergence of Non-Fungible Tokens (NFTs), representing unique digital items, ranging from digital art to virtual real estate. With this proliferation of digital wealth, California family law practitioners are now faced with the increasingly complex challenge of valuing and dividing these assets in the event of a divorce.

The valuation and division of traditional assets, such as real estate, stocks, and bonds, have well-established legal precedents. However, the decentralized, intangible, and often volatile nature of digital assets poses fresh challenges. For well-established and widely traded cryptocurrencies, determining the current value can be a straightforward task. However, for less popular or less liquid tokens,¹ accurate valuation can be far more intricate, requiring a deeper understanding of market dynamics and trading platforms. NFTs and other digital assets, with their unique characteristics, add another layer of complexity due to their inherent subjectivity in valuation.

THE IMPERATIVE OF UNDERSTANDING DIGITAL ASSET VALUATION IN FAMILY LAW

It is neither reasonable nor necessary to expect family law attorneys to be able to independently value digital assets. However, it is crucial for them to grasp the fundamental principles of their valuation for the following reasons:

- 1. Assets Subject to Division:** Cryptocurrencies, NFTs, and other digital assets are real assets with real value. Accordingly, these assets, just like most others acquired during marriage, are subject to division in divorce proceedings.
- 2. Judicial Mandate:** Courts have a clear directive when it comes to valuing and dividing community property: they have a nondelegable duty to provide specific findings regarding the nature and value of all community assets (unless divided in kind).² Accordingly, it is the responsibility of family law attorneys to ensure that digital



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assets are accurately represented and valued in divorce proceedings.

- 3. Proliferation and Acceptance of Digital Assets:** The digital asset domain has experienced meteoric (albeit punctuated) growth. With global adoption of digital assets soaring, it is no longer a realm exclusively for the tech elite. From retail investors to institutional stakeholders, digital assets have penetrated mainstream financial conversations and transactions.
- 4. Significant Financial Stakes:** As the market capitalization of the digital asset space grows, so does the individual investment of many parties. In many divorce proceedings, the value embedded in digital assets may represent a significant portion, or even the majority, of marital assets. Failing to appropriately recognize and value these holdings could result in substantial financial oversight.
- 5. Challenges and Nuances:** The inherent volatility, the varied marketplaces, and the sometimes opaque nature of ownership for digital assets mean valuation can be complicated. Being well-versed in these intricacies ensures that you can advocate effectively for your clients.

DIGITAL ASSET VALUATION CHALLENGES

Some of the significant challenges faced when valuing cryptocurrencies, NFTs, and other digital assets include volatility, liquidity concerns, ownership verification, and subjectivity of certain assets.

Volatility

Volatility in the digital asset realm introduces distinct challenges for valuation. Many digital assets, particularly cryptocurrencies, can experience pronounced fluctuations, not just day-to-day, but even hour-to-hour. This intense intra-day volatility amplifies the importance of selecting the right “valuation time” for family law practitioners. Unlike many traditional assets, which may gradually fluctuate over extended periods, the rapid value changes of digital assets underscore the occasional need for a valuation at a precise moment in time. It’s not necessarily just about picking the right valuation date—the exact moment within that day may become relevant in accurately and equitably assessing value. Further complicating matters, digital assets, being relatively novel, lack the long-standing historical pricing trends that guide traditional asset valuations, making future price predictions based on past movements all the more complex.

Liquidity

Liquidity concerns are another component of the valuation challenge when dealing with digital assets. Major cryptocurrencies like Bitcoin and Ethereum typically boast significant liquidity, allowing for straightforward conversions to cash. However, this may not be the case for less popular or newer tokens. Their limited liquidity may mean that the simple act of listing or attempting to trade the asset can materially impact its price. For instance, if someone tries to sell a sizable amount of a less popular token, it can cause a sharp decline in the token’s value due to the scarcity of buyers. Additionally, the valuation of a digital asset can vary between trading platforms. This discrepancy arises from differences in trading volume, regional regulations, and accessibility on each platform. Consequently, the same asset might fetch different prices on separate platforms, adding another layer of uncertainty to the valuation process.

Ownership Verification

Ownership verification of digital assets presents its own challenges, with nuances depending on the mode of ownership. Digital assets can be owned via an exchange or held in noncustodial manners. When assets are owned through an exchange, the exchange platform typically holds the private keys, providing the user access to their assets via the platform’s infrastructure. In such cases, ownership is often proven through account access and associated records on the exchange.

Conversely, with noncustodial ownership, individuals directly possess their digital assets without third-party intervention, holding their private keys in personal wallets, whether digital, hardware, or paper-based. This form of ownership makes ownership verification more challenging

because noncustodial wallets are not inherently tied to an individual’s identity and lack associated personal identification information. Moreover, if private keys to a noncustodial wallet are lost, the digital assets in that wallet become inaccessible, which introduces complications for valuation and division, including possible burden-shifting responsibilities of accounting for losses.³

Distinct Nature

The inherent nature of certain digital assets further complicates their valuation process. NFTs exemplify this challenge. Distinct from cryptocurrencies, which have values influenced largely by market dynamics, NFTs are, by their very name (i.e., “Non-Fungible” Tokens), unique. This nonfungibility means that each asset is distinct, making direct comparisons or valuations based on similar sales a complex endeavor. It is somewhat analogous to real estate, where, despite broad market trends, each property’s value is influenced by its unique characteristics, location, and condition. With NFTs, factors like rarity, the reputation of the artist, and prevailing market demand play pivotal roles. Moreover, the constantly evolving landscape of digital assets, marked by emerging platforms, technologies, and coins, further shifts valuation dynamics, necessitating continuous adaptation and a deep analysis of the current ecosystem.

VARIED VALUATION APPROACHES: FROM CRYPTOCURRENCIES TO NFTS AND BEYOND

Valuation methods differ depending on the nature of the digital asset being valued (e.g., cryptocurrency vs. NFT).

Well-Known Cryptocurrencies

Cryptocurrencies with large trading volumes (e.g., Bitcoin, Ethereum, Solana, Matic, and many others) are the easiest to value, with numerous reputable exchanges (e.g., Coinbase, Binance, and Kraken) providing real-time pricing data based on actual buy and sell orders on their platforms. These prices are generally the most reliable indicator of current market value for major cryptocurrencies.

Niche Tokens

Lesser-known or less liquid tokens are trickier to value. Many of these tokens do not have substantial trading volumes and are not traded on major exchanges. Instead, they are often traded on decentralized finance (DeFi) platforms (e.g., Uniswap), which operate differently than traditional exchanges. On these DeFi platforms, liquidity is often provided by community members, and trading volumes might be considerably lower than on major exchanges. One unique challenge here is that the act of listing a substantial quantity of such a token for sale can itself impact its price due to the limited liquidity. This “slippage” effect can lead to significant price variations in a short time. Additionally, factors like the token’s utility, its total and circulating supply, and any external market influences should be considered. Given these complexities, consultation with crypto experts—and ideally with DeFi

specialists when possible—is essential when the valuation of lesser-known or less liquid tokens comes into play.

NFTs

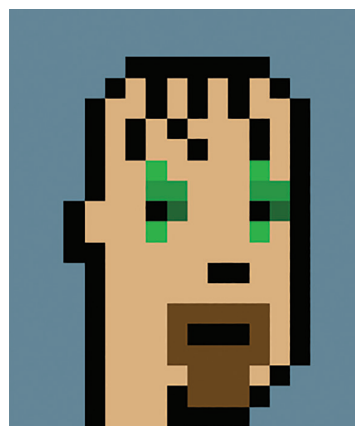
The valuation of NFTs is a nuanced process that demands an understanding of both the digital asset market—including art, collectibles, and other categories—and the specific attributes of the NFT in question. One of the primary methods to ascertain an NFT's value lies in examining its sales history. Platforms like OpenSea, Rarible, and Magic Eden provide historical sales data for NFTs, giving insight into what buyers have been willing to pay for a particular piece or a similar one.

Comparable sales, akin to how real estate is valued, can also offer a framework. For instance, if a digital artwork by a particular artist sold for a specific price, other works by the same artist might have a comparable value range. Yet, given the uniqueness of each NFT, factors like rarity come into play. A very distinct NFT could command a higher price than one with similar variants.

In the realm of valuing NFTs that are part of a series or collection, two terms frequently surface: “floor price” and “traits.” The “floor price” represents the minimum current price at which a particular NFT (or a type of NFT within that collection) is listed for sale in the market. It offers a baseline value, reflecting the lowest price point sellers are currently willing to accept, indicative of general market sentiment for that collection. “Traits,” meanwhile, refer to specific attributes or characteristics of an NFT within the series. For example, in a collection like CryptoPunks, traits could denote features like accessories, facial hair, or glasses. The rarity and desirability of certain traits can significantly influence an NFT's value within the series, with those boasting rarer traits often fetching higher prices. Understanding both floor prices and traits is essential for a nuanced perspective on the valuation of NFTs within a series or collection.



CryptoPunk #9314 has a Beanie, which is a very rare trait: only 44 of the 10,000 CryptoPunks have this. This CryptoPunk was last sold on June 30, 2023 for 178Ξ.⁴ There are currently (as of September 26, 2023) 10 CryptoPunks with Beanies listed for sale; the cheapest of these is listed for 176.90Ξ⁵ (~\$280,000).



CryptoPunk #9475 is the cheapest CryptoPunk currently (as of September 26, 2023) listed for sale, at 45.50Ξ (~\$72,000).⁶ Accordingly, the current “floor price” for CryptoPunks is 45.50Ξ.

For NFT artwork, the reputation and sales history of the artist or creator is paramount. A digital artwork by Beeple, for example, shattered records by selling for \$69 million at a Christie's auction. Such high-profile sales have a cascading effect on the valuation of other NFTs by the same artist. Furthermore, the narrative or story behind the NFT can add value. An NFT marking a significant event or cultural phenomenon might see increased interest and valuation.

Additionally, many NFTs come with the potential for future royalties. Smart contracts built into the NFT can ensure that original creators receive a percentage of sales whenever the NFT is resold, adding a potential revenue stream for the holder and influencing its initial valuation.

Websites and platforms can aid in this complex valuation process. Beyond the aforementioned OpenSea, Rarible, and Magic Eden, sites like wgmi.io and rarity.tools provide analytics and valuation metrics. Evaluating NFTs is as much an art as it is a science, combining hard data with subjective attributes in a rapidly evolving digital marketplace.

It is worth noting that there are online services designed to provide a comprehensive overview of all digital assets within a wallet or exchange account. By simply inputting a wallet address, users can gain insights into the current estimated values of both cryptocurrencies and NFTs held within. For exchange accounts, users might be prompted for login credentials, facilitating an assessment of the entire portfolio's worth on that platform. However, a word of caution: while these services provide quick and consolidated views, they might not always offer pinpoint accuracy, especially for less liquid or niche assets. Their estimates are based on current market data, and given the volatility and dynamism of the digital asset space, real-time valuations can differ. It is advisable to use these services only as a reference point, supplementing their insights with deeper research and analysis.

Beyond NFTs

Beyond cryptocurrencies and NFTs, the digital realm comprises a spectrum of assets, each with its own valuation intricacies. Some digital assets revolve around virtual goods or digital collectibles that might not be categorized as NFTs, such as a rare skin in a popular online game, which may command a premium due to its enhanced functionality or its status as a symbol of prestige among players. Similarly, the value of digital collectibles or virtual goods in apps and platforms can be influenced by their rarity, utility, and the overall user demand within their specific digital ecosystem.

Multiple Valuation Dates

Valuation of digital assets is further complicated when claims of breach of fiduciary duty arise. When calculating remedies under California Family Code section 1101, subdivision (g) for a breach of fiduciary duties, “[t]he value of the asset shall be determined to be its highest value at the date of the breach of the fiduciary duty, the date of the sale or disposition of the asset, or the date of the award by the court.” This requires determining the value of the subject asset at multiple historical points. Given the characteristic volatility of digital assets in general, and the added difficulties of valuing certain varieties—such as less-liquid tokens, NFTs, or platform-specific virtual goods—calculating multiple historical values of these assets will rarely be straightforward.

CONCLUSION

As the digital frontier continues to expand, its intersection with the realm of family law, especially in divorce proceedings, grows increasingly pronounced. The era where assets were primarily tangible—homes, vehicles, and savings—is gradually giving way to an age where portfolios are diversified with cryptocurrencies, NFTs, and other digital holdings. Understanding and accurately valuing these digital assets is not just a luxury but a necessity for practitioners wishing to navigate modern divorce landscapes effectively.

Yet valuation is just the tip of the iceberg. Once ascertained, the division of these assets poses its own set of challenges. Unlike traditional assets or even some cryptocurrencies, certain digital assets cannot be easily split. Take NFTs, for instance. Their intrinsic uniqueness and indivisibility mean that they cannot be halved or quartered, but rather, one party typically retains the asset while the other might receive compensatory value or other assets in return.

In light of these complexities, the call to action for legal professionals is clear. Continued education is paramount. Collaborating closely with digital asset experts and financial consultants will be instrumental in navigating this emerging and rapidly evolving digital frontier. As the digital asset domain evolves, so too must our approaches and strategies, ensuring fairness, accuracy, and foresight in every decision.

- 1 The terms “token” and “cryptocurrency” are often used interchangeably in many contexts, but there are nuanced differences between them. At its core, a cryptocurrency is a digital form of currency that uses cryptography for security and operates independently of a centralized authority. Many blockchains have a native cryptocurrency that serves as an incentivization mechanism and medium of exchange within the network. For example, Bitcoin (on the Bitcoin blockchain) and Ether (on the Ethereum blockchain) are both cryptocurrencies. On the other hand, a token represents a digital asset issued on an existing blockchain. The Ethereum blockchain is widely known for its ERC-20 token standard, which allows for the easy creation and distribution of new tokens. While these tokens utilize the underlying blockchain for security and validation, they are not essential to the blockchain’s basic functioning. They can represent a wide range of assets and use-cases, from governance rights to access to specific services. For purposes of this article, the distinction between cryptocurrency and token is not critical.
- 2 *In re Marriage of Micalizio* (1988) 199 Cal.App.3d 662, 672–73 (“the court must make specific findings concerning the nature and value of all community assets of the parties unless property is divided in kind”); *In re Marriage of Cream* (1993) 13 Cal.App.4th 81, 88 (“the court possesses no authority to divide the community estate between the parties other than equally, and cannot delegate its responsibility to fix the fair market value of the community estate where assets are not divided in kind”).
- 3 When a nonmanaging spouse makes an initial showing regarding the existence and value of missing community assets under the control of the managing spouse, the burden shifts to the managing spouse to either counter that showing or prove the proper disposition or reduced value of those assets. A managing spouse who fails to meet this burden can be charged with the value of the assets as presented by the nonmanaging spouse. *In re Marriage of Margulis* (2011) 198 Cal.App.4th 1252. A spouse who loses the private keys of a noncustodial wallet, and thereby loses the ability to access that wallet and the digital assets therein, could easily become subject to the burden-shifting mandate of *Margulis*.
- 4 *CryptoPunks: Details for Punk #9314* <<https://cryptopunks.app/cryptopunks/details/9314>> (as of Sept. 26, 2023).
- 5 Ξ is the symbol for Ether (the native cryptocurrency of the Ethereum blockchain), which is the original, and still most common, cryptocurrency used for NFT transactions.
- 6 *CryptoPunks: Details for Punk #9475* <<https://cryptopunks.app/cryptopunks/details/9475>> (as of Sept. 26, 2023).