

# BITCOIN OFFSHORING - BE YOUR OWN OFFSHORE BANK

By Dr. Ulrich Eder, PUGNATORIUS S.A., Panama. | This conference speech script was written for the Adopting Bitcoin 2023 conference in November 2023 in San Salvador. It highlights a limited selection of aspects of Bitcoin offshoring that are regularly addressed and analyzed by the advisory firm with Bitcoin millionaires and other high net worth clients in order to find a modern digital asset protection strategy for their specific needs. Those who fail to prepare are prepared to fail. This paper does not constitute legal, tax, or financial advice.

## A. Say goodbye to "Not your keys, not your Bitcoins"!

Imagine you intend to buy a **pleasure yacht** as the pinnacle of your luxury lifestyle. A "superyacht" starts with more than 24, 25 or 30 meters, but no more than 12 pax. There are approximately 5,000 superyachts in the world, and countless smaller ocean-going vessels, mostly in the Caribbean and Southeast Asia.

How would you own such a high-value asset? A simple rule would be "**not your flag, not your yacht**", meaning you have direct legal ownership. However, the yachting business is a mature industry and therefore there are sophisticated ownership structures. They take into account that the yacht operates in a complex regulatory, legal (e.g. labor laws), customs, VAT and other tax environment. The yacht is typically built, owned and operated in different jurisdictions.

Your Bitcoin wallet may have the same value as a pleasure yacht. It is subject to a comparable scope of challenging regulatory, legal and tax requirements. As a result, it makes perfect sense to think about an appropriate ownership structure. "Not Your Keys, Not Your Bitcoins" is a somewhat naive view against this background. In the following, I will argue for a rule that can be defined as "**Your Keys, But Not Your Bitcoins**". In other words, it makes more sense to hold Bitcoin through a separate legal entity in a Bitcoin-friendly (offshore) jurisdiction. Understand this before you need to.

By Dr. Ulrich Eder, PUGNATORIUS S.A., Panama. | Let's start with a provocation: The #1 meme of the Bitcoin community is outdated and promotes only the second best advice for a Bitcoin millionaire. For a high-value asset, more sophisticated ownership structures should be chosen. "Your Keys, But Not Your Bitcoins".

Empecemos con una provocación: El meme número 1 de la comunidad Bitcoin está anticuado y sólo promueve el segundo mejor consejo para ser millonario de Bitcoin. Para un activo de gran valor, deberían elegirse estructuras de propiedad más sofisticadas. "Sus claves, pero no sus Bitcoins".

## B. Standing the heat of digital surveillance

Bitcoin began as a quasi-anonymous payment system, although technically it is only pseudonymous. This has changed through three developments. **First**, the buying and selling process often requires personal identification. **Second**, this data is shared with government agencies. As a **third** consequence, advanced blockchain analytics enable the development of a closed network of identities and related transactions. As a result, a sophisticated blockchain surveillance industry now provides a transparent playing field for most jurisdictions.

There are three ways to regain anonymity: **First, the purchase of no-KYC Bitcoin; second, a regulatory environment that does not require exchanges and service providers to share their data; and third, a law that allows anonymity tools** such as mixers, etc. However, recent developments are moving in the opposite direction.

Currently, we can expect a rapid implementation of the **Crypto-Asset Reporting Framework (CARF)** and changes to the CRS (Common Reporting Standard) by and within the G20 countries. This

means a significant tightening of reporting requirements for Bitcoin, supported by blockchain analytics.

In Europe, and presumably in many other countries, preparations are underway to introduce and establish an **European Asset Registry**. This will include Bitcoin and other digital assets. There will be reporting obligations, separate from tax obligations. Even long-term Bitcoin holders won't be able to avoid registering their Bitcoins. Otherwise this would lead to criminal liability.

Under local tax regulations, the Bitcoin investor will sooner or later be required to report Bitcoin holdings, even if no taxes are due in the current fiscal year. These **taxpayer's Bitcoin reports** will be read by his local tax officer and can be exploited in various ways, including for criminal purposes.

Bitcoin privacy can be re-established through **anonymity tools**. These are mainly coin mixers and tumblers, PayJoins, CoinSwap and CoinJoins, and tools similar to the (ETH) TornadoCash smart contract. All of these tools and modules are likely to face strong resistance from governments, and using them may be in certain jurisdictions outright illegal.

As a logical consequence, anonymity may no longer be possible in the G20 area and other countries. Bitcoin fixes this, if offshoring **(1)** allows anonymous Bitcoin hodling, **(2)** avoids a regulatory pressure of reporting transaction data to the governments, and **(3)** allows anonymity tools. In that case, the Bitcoin millionaire has to decide, whether Bitcoin offshoring is worth the efforts.

By Dr. Ulrich Eder, PUGNATORIUS S.A., Panama. | In many jurisdictions, digital surveillance of bitcoin holders and transactions is possible and already the norm. The situation will soon worsen with the Crypto-Asset Reporting Framework (CARF) and the European Asset Register. Bitcoin offshoring aims to regain anonymity.

En muchas jurisdicciones, la vigilancia digital de los titulares de Bitcoins y sus transacciones es posible y ya es la norma. La situación empeorará pronto con el Marco de Información sobre Criptoactivos (CARF) y el Registro Europeo de Activos. La deslocalización de Bitcoin pretende recuperar el anonimato

### C. Bitcoin can't be banned - until they do.

The risk of a Bitcoin ban can be assessed and evaluated differently. It is important to understand that there are a variety of gradations in this regard. The **Bitcoin ban can come in different flavors**. There could be a ban on Bitcoin mining. Bitcoin on-ramps and off-ramps may be restricted or closed. The existence of Bitcoin can be seen as a disruptive competitor or destructive influence against CBDCs.

Going further, Bitcoin use could be banned if the coins are mixed with a tumbler or similar **anonymity tool**. The total ban, within geo-fenced areas and with or without a grace period, enforced as a criminal offense and punishable by fines, is just the worst case scenario.

The Bitcoin ban will be limited to **certain countries and territories** and will not be applicable law around the globe. Bitcoin fixes this when offshoring effectively and legally circumvents the ban.

By Dr. Ulrich Eder, PUGNATORIUS S.A., Panama. | The likelihood of a future Bitcoin ban is greater than zero. It may come in various forms and strengths. It will be geo-fenced and limited to certain jurisdictions. Bitcoin offshoring aims to circumvent such ban effectively and legally.

La probabilidad de una futura prohibición del Bitcoin es mayor que cero. Puede presentarse en varias formas y grados. Estará geocercada y limitada a determinadas jurisdicciones. El objetivo del bitcoin offshoring es eludir esta prohibición de forma eficaz y legal.

### D. The end of puppy protection by the taxman

We are currently witnessing an amazing development. The regulatory framework in which crypto asset service providers are allowed to operate is becoming **increasingly restrictive**. In addition, the

ability to exchange tax information is expanding across borders.

At the same time, the tax treatment of Bitcoin transactions remains **relatively low and generous**. There are partially privileged tax rates. Holding periods allow for complete tax exemption of Bitcoin profits. Restructurings, including cross-border ones, often do not constitute a tax event.

Trusting in the continuation of a lenient tax regime seems criminally naive. It is more likely that the case will be carefully prepared before it is closed. A bull market during the year 2024 could lead to a tightening of tax laws in connection with well orchestrated staged events. **The honeymoon period is over.**

The **toolbox of tax tightening** includes the reclassification of commodities into foreign currencies, the elimination of safe-haven holding periods, fictitious profit realization, the applicability of CFC taxation to Bitcoin wallets, some form of exit taxation, and even taxation of unrealized gains.

**The tools and modules are limitless.** There could be a special crypto income tax, a crypto capital gains tax, and a crypto transfer or sales tax. And finally, a special (crypto) wealth tax might gain popularity. To offshore Bitcoins might even be subject to a crypto exit tax in the future.

Bitcoin fixes this, if the offshoring reduces the current and future tax burden in a fully tax compliant manner. **Tax avoidance is allowed, tax evasion is not.**

By Dr. Ulrich Eder, PUGNATORIUS S.A., Panama. | Currently, Bitcoin taxation is generous and relatively modest. There is a high probability of a tightened tax environment and excessive Bitcoin taxation. The honeymoon period is over. Bitcoin offshoring is designed to avoid, not evade, such future taxation.

Actualmente, la fiscalidad del Bitcoin es generosa y relativamente modesta. Existe una alta probabilidad de que el entorno fiscal se endurezca y la fiscalidad de Bitcoin sea excesiva. El periodo de luna de miel ha terminado. El offshoring de bitcoins está diseñado para evitar, no para evadir, esos futuros impuestos.

## E. Protection against sanctions

We live in **sanctions-friendly times**. The restrictions of the past seem to have disappeared. Lists of unfriendly nations, lists of specially designated nationals and blocked persons, military conflicts without direct participation, economic wars, everything seems to be sufficient for sanctions. Even non-involved citizens of the sanctioned states encounter what used to be called piracy. Sanctions lead to seizure, confiscation and exploitation with limited effective legal protection.

Government agencies such as the Office of Foreign Assets Control (OFAC) of the U.S. Department of the Treasury and its counterparts in other countries implement sanctions by **targeting countries, regimes, individuals, and entities** that are considered threats to national security and foreign policy.

**Bitcoin confiscation** is a likely scenario, although it has not yet made big waves in the news. Only vague links to sanctioned jurisdictions and individuals are relevant. Accounts on exchanges can be directly seized and confiscated, self-custodian wallets can be blacklisted by exchanges in sanctioning jurisdictions. Purchases made with blacklisted Bitcoin can be declared void and ineffective.

The U.S. OFAC first announced in November 2018 that it would begin adding digital currency addresses associated with sanctioned actors to its **Specially Designated Nationals and Blocked Persons List (SDN List)**. For the first time, OFAC publicly identified digital currency addresses with which financial institutions are prohibited from transacting, marking one of OFAC's first forays into the cryptocurrency industry.

By Dr. Ulrich Eder, PUGNATORIUS S.A., Panama. | We live in sanctions-friendly times. They can harm honest and law-abiding Bitcoin millionaires if they keep their Bitcoins in the wrong place at the wrong time. Bitcoin offshoring wants to protect against sanctions.

Vivimos tiempos propicios a las sanciones. Pueden perjudicar a los millonarios de Bitcoin honrados y respetuosos con la ley si guardan sus Bitcoins en el lugar y el momento equivocados. Bitcoin offshoring quiere protegerse de las sanciones.

## F. Secure your Bitcoin wealth in paradise

Understanding the game-theoretic consequences of these **four threats to Bitcoin wealth**, it makes sense to consider Bitcoin offshoring. This requires a clarification of where is Bitcoin offshore, specifically the distinction between offshore and the blockchain space. With the blockchain as a location-free infrastructure, what is the significance of the locations of nodes and miners, wallets and exchanges, Bitcoin owners and private keys?

It is also relevant to ask for what aspects the **location of Bitcoin is relevant**. One criterion is the definition of Bitcoin profits as foreign income. The second relates to the applicable laws, and the third is the tax treatment. The crypto industry has its "The Code is the Law" statement, but not every jurisdiction agrees.

How is it possible to create "Offshore Bitcoin" **without moving residence abroad**? Is it enough to store the 24-word seed phrase in a bank safe deposit box in the Caribbean? Is it relevant if the Bitcoin investor takes his hardware wallet on a cruise ship trip? It is our opinion that the use of an offshore entity is necessary and sufficient to meet the offshoring requirements.

By Dr. Ulrich Eder, PUGNATORIUS S.A., Panama. | Bitcoin offshoring is not a self-explanatory concept. The relation between the location-free blockchain space and offshore, the mechanics of offshoring Bitcoin, and the recognition of offshore transfers need to be critically evaluated. "The Code is the Law" is not a globally accepted rule.

La offshoring de Bitcoin no es un concepto que se explique por sí mismo. Es necesario evaluar críticamente la relación entre el espacio blockchain sin localización y el offshore, la mecánica del offshoring de Bitcoin y el reconocimiento de las transferencias offshore. "El Código es la Ley" no es una norma mundialmente aceptada.

## G. How to transfer the Bitcoins (to) offshore

The first step in the offshoring process is the selection of an **appropriate offshore jurisdiction**. Typical legal requirements are a sound legal regime, ease of doing business and other general aspects. Taxwise, no or low taxes are preferred. Existing tax treaties, including TIEAs (Tax Information Exchange Agreements), must be taken into account. There are typically quantitative and qualitative aspects for a good or bad offshore location or jurisdiction.

As a Bitcoin offshore location, these aspects as well as additional criteria have to be reviewed in light of the specific requirements for a crypto location. **Bitcoin offshore is different from banking offshore or holding offshore**. In this context, how to conduct crypto business and Bitcoin mining will typically be irrelevant.

**Traditional offshore tax aspects** are a legally valid entity that is separate from the shareholder, the economic substance doctrine, the place of effective management rule, and, if applicable, the CFC controlled foreign corporation regime. There are no particular rules for this.

**Bitcoin tax aspects** for the selection of the offshore jurisdiction are the exit taxation of the offshoring process, the transfer taxation, the profit and wealth taxation offshore, as well as the applicability of the buy, borrow, die method.

By Dr. Ulrich Eder, PUGNATORIUS S.A., Panama. | The concept requires the Bitcoin transfer to a separate legal entity in a jurisdiction that qualifies for Bitcoin as offshore. This could be very different from offshoring bank accounts, real estate, and stock holdings.

El concepto requiere la transferencia de Bitcoins a una entidad legal separada en una jurisdicción que califique a Bitcoin como offshore. Esto podría ser muy diferente de offshoring cuentas bancarias, inmobiliarias, y participaciones bursátiles.



## H. The self-defense rug pull kill switch - is it legal?

Traditional offshore companies have a **bad reputation** today. There are risks that make them unattractive, especially for those concerned about their financial safety. There may be a legal requirement to involve a nominee, who sooner or later will play dirty. The offshore jurisdiction may develop in the wrong direction. The foreign courts could be inefficient, or some other unknown risk could arise offshore.

None of this matters to the Bitcoin investor if he has a "**kill switch**" in his hand. According to accounting and tax rules, the offshore company must legally own the Bitcoin, but what does this mean in practice? A legal entity can only hold the private keys of a Bitcoin wallet through a human being. The real holder of the private keys is as secret as the private keys themselves.

Imagine that the shareholder keeps the private keys without sharing them with the nominee directors, if any, or other participants. In the worst-case scenario, he would be able to "**pull the rug**" and transfer all your Bitcoin holdings out of the offshore company. Even if all hell breaks loose offshore, the kill switch leaves the Bitcoin investor free, independent and wealthy. But is this legally as well as ethically correct and good prudent advice?

By Dr. Ulrich Eder, PUGNATORIUS S.A., Panama. | The Bitcoin investor's rug-pull kill switch is a quick self-defense tactic with numerous legal and ethical considerations. The implementation as well as execution must follow a specific playbook.

El interruptor asesino ("kill switch") del inversor en Bitcoin es una táctica de autodefensa rápida con numerosas consideraciones legales y éticas. La aplicación y ejecución deben seguir un libro de jugadas específico.

## I. Successful Bitcoin offshoring is a one-shot deal

Bitcoin offshoring ultimately consists of the **cross-border transfer** of cryptocurrencies to an offshore entity. Traditional aspects to be considered are transfer pricing, the perfect time to transfer, transfer of profits or losses, as well as issues of transfer gain taxation.

With respect to the crypto nature of the transaction, there are **accounting and documentation requirements** to consider, a potential reporting obligation, and more. It is important to understand that the blockchain is immutable, and will not forget any mistakes made in the past.

**Tax considerations** include exit taxation in the home jurisdiction, tax holding periods, and transfer pricing rules. In the offshore jurisdiction, territorial taxation rules, transfer pricing rules and accounting standards are other important tax considerations. The possibility of future repatriation to the home jurisdiction and the repatriation tax situation should also be considered.

By Dr. Ulrich Eder, PUGNATORIUS S.A., Panama. | Bitcoin offshoring must take into account traditional industry standards as well as crypto specifics. Mistakes are immutably recorded on the blockchain. The wise Bitcoin millionaire learns from others' mistakes instead of doing them himself.

El offshoring de Bitcoin debe tener en cuenta las normas tradicionales del sector, así como las especificidades de las criptomonedas. Los errores quedan registrados de forma inmutable en la cadena de bloques. El sabio millonario de Bitcoin aprende de los errores de los demás en lugar de cometerlos él mismo.

## J. "Hard choices, easy life. Easy choices, hard life." - Bitcoin offshoring secrets

The above remarks deal with "**The need for Bitcoin offshoring**". It gives a rough overview regarding the motivation, aspects and considerations to offshore Bitcoin as a modern digital asset protection strategy.

More important are what we can call "**Bitcoin offshoring secrets**", the problems and solutions that arise during the process, and the things that you understand in the end, but need to implement in

the beginning. Crypto offshoring requires more than a combination of advanced crypto knowledge, solid offshore experience, and hands-on transaction support.

**If you do almost everything right, you will do it all wrong.** Making some "easy" choices, or rather "choosing not to decide" as a choice to rush, will definitely bite you in the end. Those who fail to prepare are prepared to fail. The immutable blockchain will never forget such mistakes.

**PUGNATORIUS S.A. is an owner-managed and fully independent niche advisory firm established in 2009 under the laws of Panama. Bitcoin Offshoring is one part of the consultancy firm's Modern Digital Asset Protection Strategy services.**

**PUGNATORIUS S.A. es una empresa de asesoría de nicho totalmente independiente y gestionada por sus propietarios, establecida en 2009 bajo las leyes de Panamá. Bitcoin Offshoring es una parte de los servicios de estrategia de protección de activos digitales modernos de la empresa de consultoría.**

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