Taxation of Crypto Assets

Edited by
Niklas Schmidt
Jack Bernstein
Stefan Richter
Lisa Zarlenga
Editors

Jack Bernstein is the Senior Tax Partner at Aird & Berlis LLP in Toronto and Chair of the firm’s International Tax practice. Jack is well known in international tax planning, mergers and acquisitions, corporate restructuring, reorganizations and financing. He is experienced in dealing with public and private corporations and has advised hedge funds, venture capital funds and real estate funds. He also has extensive experience in advising high-net-worth private clients on international, cross-border and domestic estate and tax planning. An authority on multijurisdictional matters and a prolific writer and speaker, Jack regularly contributes to leading tax publications globally, including Tax Notes International. He has been actively involved at a senior level in several international and Canadian tax organizations, including being a past Governor of the Canadian Tax Foundation, former Chair of the American Bar Association Foreign Lawyers Forum, former Global Co-Chair of the International Bar Association Taxation Committee, and former Member of Council of the International Fiscal Association (Canadian Branch). Jack is internationally recognized by leading legal publishers, including Chambers and Partners, Who’s Who Legal, The Legal 500, Best Lawyers, Martindale-Hubbell and Lexpert. As a result of his outstanding leadership and contributions to the field of tax law, Jack was honoured with the 2020 Ontario Bar Association Award for Excellence in Taxation Law. Email: jbernstein@airdberlis.com.

Stefan Richter has more than twenty years of experience in M&A and tax structuring consulting. He specializes in providing advice on corporate transactions, structuring and tax planning of token-based business models as well as tax-driven reorganizations in an international context. In addition, Stefan has longstanding experience in advising national and international law firms regarding their own ongoing and structural tax matters. Stefan formerly was a partner with Deloitte. He is a lecturer at the Bucerius Law School, a board member of the Hamburger Steuerdialog e.V., and a frequent speaker at tax conferences. Email: stefan.richter@smp.law.

Niklas Schmidt is a Tax Partner with WOLF THEISS in Austria. He has completed studies in Vienna, Barcelona, Munich and Oxford and has been admitted in Austria both as a lawyer and as a tax adviser. Before joining WOLF THEISS in the year 2000,
he had previously worked for several years at a ‘Big Four’ accounting firm and as a research assistant at the University of Vienna. Niklas has written various books (including a recent book on crypto assets and blockchains in German), is frequently engaged as a speaker at law conferences, is a member of several international legal organizations and networks and has top rankings in international directories. Currently, Niklas is a chair of the Private Client Tax Committee of the International Bar Association (IBA). Email: niklas.schmidt@wolftheiss.com.

Lisa Zarlenga is a Tax Partner at Steptoe & Johnson, LLP, where her practice focuses on corporate transactional and planning matters as well as tax policy issues. She advises clients on structuring tax-free and taxable acquisitions and dispositions. Drawing on her experience as Tax Legislative Counsel at the Treasury Department, she also helps clients advocate for and resolve tax policy issues before Treasury and the Internal Revenue Service involving proposed and pending regulations and other administrative guidance, and before Congress involving legislation. She has also assisted clients during the rulemaking process, including preparing comment letters and meeting with policymakers. Lisa has combined her policy and transactional backgrounds to advise clients on certain specialized tax issues, such as blockchain and digital currency. She advises clients on conducting digital currency transactions and conversions, token offerings, and different investment and entity structures. Lisa is a frequent speaker, and she is active in the Tax Section of the American Bar Association, currently serving as the chair of the Committee on Government Submissions. Email: lzarlenga@steptoe.com.
Contributors

Tomás Bailey is a Senior Associate in the corporate tax department at Matheson currently based in the firm’s London office. Tomás advises Irish and multinational clients on corporate and international tax, mergers and acquisitions, tax controversy and transfer pricing. Tomás advises clients in relation to tax-effective structures for inbound and outbound investment and has advised on numerous cross-border reorganizations. Tomás also advises on state aid in the context of taxation matters. Email: tomas.bailey@matheson.com.

Ákos Baráti is a lawyer and an economist. Ákos obtained his law degree at the Law Faculty of the University of Pécs in 2010. He obtained a Diploma in Economics at the Budapest Corvinus University in 2012. He is a certified tax advisor and a certified public accountant. Before joining Jalsovszky law firm in 2014 Ákos has gained more than four years of professional experience at international ‘Big4’ consulting firms, where his main areas of expertise were international tax planning and corporate tax advisory. In addition to tax planning, Akos assists his clients with regulatory matters. Email: abarati@jalsovszky.com.

Joachim M. Bjerke is a Partner in the law firm BAHR and heads the firm’s tax and VAT department. Joachim works with a broad range of national and international corporate tax questions, including transfer pricing, oil and gas taxation and structuring of M&A transactions. He is one of the leading advisers in Norway with respect to transfer pricing and his work spans from advisory services to dispute resolution. He has also written one of the few Norwegian books on transfer pricing. Together with BAHR-partner Jan B. Jansen he has written a book with an introduction to the Norwegian oil taxation regime, which is used as course material at the University of Oslo. Email: jmb@bahr.no.

Miri Bickel co-heads Shibolet & Co.’s tax practice. Miri is a dual-qualified accountant and lawyer, with particular expertise in international tax planning and transactions, blockchain and smart contracts, and international taxation of venture capital funds. Miri has extensive experience in all tax aspects relating to complex cross-border M&A,
corporate restructurings, financing, public offerings, employee stock option plans, hi-tech companies and their employees, underwritings, executive interests, and many other financial instruments. She is also recognized as a leading attorney in both civil and criminal tax litigation (income tax, real estate taxation and VAT), and regularly appears before the Appellate-level Courts. Email: m.bickel@shibolet.com.

Louis Botha ((BCom *cum laude*, LLB *cum laude*, LLM (Tax Law), University of Pretoria) is a Senior Associate in the Tax and Exchange Control practice of Cliffe Dekker Hofmeyr Inc. in South Africa. Louis’ experience includes the areas of corporate income tax, individual income tax, employees’ tax and the application of exchange control laws in the context of various transactions. Email: louis.botha@cdhlegal.com.

Emil Brincker (BCom *cum laude*, LLB *cum laude*, LLM *cum laude*, LLD, University of Stellenbosch, HDip (Tax) *cum laude*, University of Johannesburg) is a Director and National Head of the Tax and Exchange Control practice of Cliffe Dekker Hofmeyr Inc. in South Africa. Emil’s experience includes the areas of corporate finance, corporate reorganization and restructuring, exchange control, export finance, funding, general banking and commercial including derivative transactions, empowerment transactions, JSE Ltd and Takeover Regulations Panel, project finance and tax law, including income tax, tax controversy, VAT, stamp duties, PAYE, capital gains tax (CGT), and other fiscal statutes. Email: emil.brincker@cdhlegal.com.

Reuben Buttigieg is the Managing Director and Founder of Erremme Business Advisors, a business and management consultancy firm servicing local and international clients. Reuben also has a direct immersion in the Corporate Finance and consultancy services within the Firm. He holds an MBA from Warwick, is a Fellow Member of the Association of Chartered Certified Accountants and a Member of the Malta Institute of Management, Islamic Banking Institute and a Member in the Worshipful Company of International Bankers. Reuben holds the Presidential position within the Malta Institute of Management. The Institute represents among others Edinburgh Business School and the Chartered Institute of Taxation. Reuben has been the pioneer in the discussions on Islamic Finance in Malta and has prepared various papers and articles on the subject being published in esteemed research journals and participates regularly as a speaker in International Islamic Finance conferences. Reuben acts as a consultant on various Islamic Finance transactions in Malta and abroad. Reuben shares his knowledge and contributes to the academic society by lecturing Islamic Finance at the University of Malta and the Malta College for Arts, Science and Technology. Before establishing Erremme Business Advisers, Reuben worked with two of the Big Four accountancy and audit firms, namely, Ernst & Young (Malta and Milan) and KPMG. Reuben has conducted various corporate finance and due diligence assignments as well as audits and consultancy work both in Malta as well as in Milan. During the Euro Changeover process in Malta, Reuben was a member in the National Euro Changeover Committee and chaired the Pricing Task Force within the said committee which falls under the umbrella of the Ministry of Finance. Reuben has vast experience in the Euro changeover as he acted as consultant even during the changeover in first wave countries. Email: rmb@erremme.com.mt.
Juan Camilo Sánchez is a Principal Tax Associate with broad experience in international tax law and private equity transactions. He currently forms part of the Garrigues Digital group, a team specialized in advising start-ups and entrepreneurs in the technology and digital economy sectors. Email: juan.camilo.sanchez@garrigues.com.

Vivien Chan is the Founding and Senior Partner of Vivien Chan & Co., with over forty years of experience in M&A, information technology, intellectual property and related tax issues. Vivien was awarded the Lifetime Achievement Award in 2017 by the American Chamber of Commerce in Hong Kong and was recently recognized as WIPR Leaders 2019 of Trademark and Patent. She was also awarded the Bronze Bauhinia Star (BBS) in 2008 and Silver Bauhinia Star (SBS) in 2014 by the HKSAR Government for her outstanding contributions to Hong Kong. Vivien is a Justice of the Peace and is the Past President of the Inter-Pacific Bar Association. She also is a notary public, a notarial attesting officer in China, and an arbitrator at the China International Economic and Trade Arbitration Commission, Shanghai International Arbitration Center and the Shenzhen Arbitration Commission. Ms Chan received her law degree from King’s College, University of London, and is admitted as a solicitor in England and Wales, Hong Kong, Australia and Singapore. She is fluent in English, French, Mandarin and Cantonese. Email: vivchan@vcclawservices.com.

Maria Chang is a Senior Foreign Attorney in the Bae, Kim & Lee LLC firm’s tax practice group. Her main practice areas involve cross-border tax structuring, international trade and customs, tax dispute resolutions and general tax and customs-related advisory services. Prior to joining Bae, Kim & Lee LLC in 2009, Maria Chang worked at the Seoul office of PricewaterhouseCoopers from 2006 to 2009, specializing in various customs matters relevant to multinational clients. Email: maria.chang@bkl.co.kr.

Aseem Chawla is the Practice Leader at ASC Legal, Solicitors & Advocates in New Delhi. He is a Member of Bar Council of India and Fellow Chartered Accountant and certificate holder of Comparative Tax Policy & Administration from Harvard Kennedy School. He is a candidate for the prestigious ‘Vienna Certificate in Double Tax Treaties’ under the auspices of WU Vienna University of Economics and Business, Austria. He has extensive experience in advising on a variety of tax matters, including international tax, inbound and outbound structuring and cross-border tax issues, corporate and business advisory, exchange control and regulatory and money laundering laws. He is an accredited Trust & Estate Practitioner (“TEP”) and a member of the Society of Trust & Estate Practitioners (STEP), UK. Aseem is well regarded for estate planning, inheritance & family governance, trusts and private clients, including national and international clients, high net-worth individuals and trustees and family offices. He is also a Visiting Faculty at the Institute of Chartered Accountants of India (ICAI) on International Taxation, economic offences and money laundering laws. He is regularly invited to address various domestic and international forums and industry bodies. He is actively involved in the leadership capacities of various professional associations and industry chambers. He is the Vice-Chair of the South Asia/Oceana and India Committee, Section of International Law (ABA) and is an Officer at ABA International Tax Committee. He is the outgoing Secretary of the Taxes Committee of
The International Bar Association (IBA) and Vice-Chair of the Task Force for Legal Services of the Confederation of Indian Industry (CII). Aseem is the Chairman of the Financial Services & Taxation Committee of the Indo American Chamber of Commerce (IACC). Email: aseem@aseemchawla.com.

Michel Collet is a Partner of the international tax department of CMS Francis Lefebvre Avocats. He assists mainly multinational enterprises (MNEs), investment and sovereign funds and banks on cross-border transactions, financing, or restructuring. Michel also assists and represents high net worth individuals including international sportsmen and artists. He is a former officer of the International Bar Association (IBA). He is also an active member of the American Bar Association (ABA) and International Fiscal Association (IFA) and is in charge of taxation in the working group of the Association Francaise des Fiduciaires (French Association of French equivalent of Trustees). Michel was in charge of the New York office of the firm from 2002 to 2007. He also sits on the board of the Jeanine Manuel International School in Paris. Email: michel.collet@cms-avocats.com.

Marta Cura is a Research Associate in the Blockchain and Digital Assets practice group at SMP. She studied law at the University of Coimbra School of Law in Portugal and at Fordham University School of Law in New York, where she completed an LLM in International Business and Trade Law. She is an attorney admitted in the state of New York. Before joining SMP, she previously worked for international law firms in London, Lisbon, and Hamburg. Email: marta.cura@smp.law.

Roberto de Castro Mendonça is a Member of the Stibbe Luxembourg Tax practice. Roberto specializes in international tax planning, the tax aspects of public and private M&A, corporate reorganizations, intellectual property, structured and hybrid finance, as well as tax litigation. He is a correspondent and author at the International Bureau of Fiscal Documentation (IBFD). Email: roberto.decastromendonca@stibbe.com

Álvaro de la Cueva is a partner in the tax practice area, with extensive experience in the provision of advice on international tax matters to Spanish and foreign multinationals, and with a particular focus on the technology, telecommunications, and crypto assets industries. Email: alvaro.delacueva@garrigues.com.

Barney Cumberland, Partner, leads the taxation practice at Simpson Grierson. With twenty-two years of practice, Barney has accumulated a broad range of experience in all fields of New Zealand’s domestic and international tax law. He is a Member of the Taxes Committee of the International Bar Association, the New Zealand Branch of the International Fiscal Association and of the New Zealand Law Society Tax Law Committee. Email: barney.cumberland@simpsongrierson.com.

Bridget English is an English Qualified Associate in the London office of Gibson, Dunn & Crutcher and a member of the firm’s Tax Practice Group. Bridget is an experienced tax adviser with a broad practice. She advises on a wide range of domestic and cross-border matters, including in relation to mergers and acquisitions, private equity,
corporate reorganizations, real estate, corporate finance, and capital markets. Email: BEnglish@gibsondunn.com.

Ben Fryer is a Partner in the London office of Gibson, Dunn & Crutcher and a member of the firm’s Tax Practice Group. Ben is an experienced tax adviser with a broad practice. He advises on a wide range of domestic and cross-border matters and transactions, including in relation to banking, capital markets, corporate finance, corporate reorganizations, debt restructuring, mergers and acquisitions, private equity, real estate and structured finance. He also guides clients on general corporate tax planning and risk management matters. Email: BFryer@gibsondunn.com.

Stephanie Gabriel is a Senior Associate at Tiberghien. She assists in various aspects of national and international wealth and inheritance tax planning, covering both private and professional clients. Over the years she has developed a thorough knowledge in providing advice on asset structures, e.g., Cayman tax law and data exchange. She is also a member of the BATL and is the author of several articles on tax issues. Email: stephanie.gabriel@tiberghien.com.

André Geest is a Researcher at the Wharton School of the University of Pennsylvania and at the UCL Centre for Blockchain Technologies. At the Wharton School he is co-organizing the Reg@Tech working group and the Blockchain governance project. His research focus is on the governance and regulation of decentralized financial technologies and the transformation towards decentralized finance. Before joining the Blockchain and Digital Assets practice group of SMP, he was a research assistant at the Institute for Computer Science at the University of Innsbruck. Currently, he is pursuing a PhD degree at Ludwig Maximilian University in Munich researching at the interface of financial market regulation and DLT/Blockchain. Email: andre.geest@smp.law.

Angelo Gentile is a Partner at the Tax Group at Aird & Berlis LLP. His practice focuses on tax litigation and commodity tax, including goods and services tax/harmonized sales tax (GST/HST) and provincial sales taxes. Angelo excels at resolving tax disputes at the early stages of the tax dispute process, although where litigation is necessary, he has experience litigating in the Tax Court of Canada and the Federal Court of Appeal on a wide range of tax disputes. Email: agentile@airdberlis.com.

Gerd D. Goyvaerts is a Partner at Tiberghien. His tax practice covers professional and private estate taxation of the Belgian entrepreneur and high net-worth individuals, international corporate and private tax planning, death duties and estate planning and tax inspired migration from and into Belgium. He developed a special interest in tax issues relevant to Anglo-Saxon trusts, foundations and settlements and voluntary disclosure proceedings, anti-money laundering legislation and regulations especially in a world where banking secrecy is shrinking. He is a regular speaker on (inter)national seminars and author of various articles on tax issues in leading journals such as Tijdschrift voor Fiscaal Recht, Fiscale Actualiteit, Trusts & Trustees and Vermogensplanning in de Praktijk. He is a member of the IBA anti-money Laundering Action Group. Gerd is president of the Belgian Association of Tax Lawyers (BATL) and International
Contributors

Fellow at ACTEC and member to TIAETL. He is the former President and Vice President of the Tax Commission of AIJA (Association Internationale des Jeunes Avocats), where he is now an honorary member. Gerd is ranked as a ‘Band1 Private Wealth Lawyer’ in the Chambers HNW 2019/2020 rankings. Gerd is also mentioned as a ‘Global Leader’ in Tax Advisory and Private Clients by Who’s Who Legal 2019. Email: gerdd.goyvaerts@tiberghien.com.

**Gian Gualberto Morgigni** is a Senior Associate of the Tax and Tax Planning department at Chiomenti in Italy. He has completed his studies in Rome and Milan and has been admitted to the Italian Bar Association. He joined Chiomenti in 2011. Gian Gualberto focuses on family estate restructuring, taxation of business operations, taxation of financial transactions and corporate restructurings. He regularly advises clients on issues related to international taxation, M&A, private equity and financing operations. Gian Gualberto has authored several publications in tax matters and is a speaker at tax conferences and seminars. Email: giangualberto.morgigni@chiomenti.net.

**Benjamin J. Hamnes** is an associate in the law firm BAHR and is a part of the firm’s department for energy and natural resources. Benjamin works with both advisory services and dispute resolution in the field of national and international corporate tax and transfer pricing. He has previously worked at EY, where he specialized within the field of transfer pricing and intangible value chains. Email: beham@bahr.no.

**Anders Oreby Hansen** has more than twenty-five years of experience and has primarily represented US, EU, Scandinavian and other multinational groups and high net-worth individuals investing in or conducting business in Denmark. His experience covers assistance to international corporate clients on matters involving strategies and dispute resolution in relation to Danish transfer pricing issues, group restructurings, international taxation issues, M&A Real Estate and corporate consulting. His experience also covers partner-owned and family businesses. Anders furthermore has experience as an arbitration judge and as an expert witness on Danish tax legislation before the High Court in London. Anders is a member of the Danish Bar & Law Society, the Danish Tax Lawyers Association, ABA, IFA and the Danish Tax Scientific Society. He is also co-author/author of several books and numerous articles in Danish and international publications. His field of specialties include M&A Real Estate, group restructurings, transfer pricing, international taxation issues, corporate consulting and partner-owned and family businesses. Email: aoh@lundgrens.dk.

**Nils Harbeke** is the Head of Pestalozzi’s Tax Practice Group. He has a particular strength in cross-border tax work and tax work for international clients, both inbound and outbound. Prior to becoming a partner with Pestalozzi, Harbeke led a team of tax advisors at PwC. He has gained special experience and knowledge in tax work for regulated industries. He frequently works for leading Swiss and international financial institutions and life sciences companies. He is the co-chair of the Tax Chapter of the Zurich Bar Association and is recognized in Chambers, Legal500, Who’s Who Legal and Best Lawyers in Switzerland. On behalf of the Swiss Bar Association, Nils Harbeke...
was called to the Swiss government’s working group ‘Justitia 4.0’, an experts group set up to prepare a full digitization of the Swiss justice system. Nils Harbeke was awarded for outstanding academic achievements: ‘Best 3’ Swiss Certified Tax Experts graduates award and ‘Best 10 achieving law students’ in his year of graduation. Email: nils.harbeke@pestalozzilaw.com.

Yushi Hegawa is a Tax Partner at Nagashima Ohno & Tsunematsu. As a specialist in tax law, he has broad practical experience on all spectrum of Japanese taxation, such as tax-free reorganizations, tax-efficient mergers and acquisitions and financing/capital markets transactions, taxation of wealthy individuals, international taxation on inbound investment by foreign-owned businesses and outbound investment by Japanese businesses, and transfer pricing. He also represents many foreign-owned taxpayers before Japanese courts and tax tribunals in many tax controversy cases and has secured successful results. Mr Hegawa receives high market recognitions from media such as Chambers Asia-Pacific (Band 1), Legal 500 and Nikkei. Mr Hegawa received his LLB from the University of Tokyo and LLM from Harvard Law School, and is admitted to practice in Japan and New York. Email: yushi_hegawa@noandt.com.

Pál Jalsovszky is a lawyer and economist who specializes in tax planning and M&A. He founded his own law firm, Jalsovszky in 2005 and currently employs more than thirty people. The firm’s client base mainly consists of multinational and domestic small and medium-sized businesses, providing corporate, real estate and commercial law consulting services in addition to tax, tax structuring and tax litigation matters. Since 2019, the firm has been dealing with litigation as well. He gained his professional experience at international law firms. Pál obtained his degree at the Law Faculty of Eötvös Loránd University Budapest in 1997. Previously, he obtained an MA at the University of Economics in Budapest, and an LLM in International Taxation at Leiden University in 2002. He regularly publishes in various professional journals. Pál is recognized as leading tax lawyer by legal professional publications, such as Legal500 and Chambers Europe. He has been awarded as Tax Advisor of the Year 2012 by Best Lawyers. Since 2015, he has been a member of the Supervisory Board at the Budapest Festival Orchestra. Email: info@jalsovszky.com.

Louise Kotze (BCom cum laude, LLB cum laude, University of Pretoria) is an Associate in the Tax and Exchange Control practice of Cliffe Dekker Hofmeyr Inc in South Africa. Email: louise.kotze@cdhlegal.com.

Bradley Kruger is the Lead Partner of Ogier’s Corporate team in the Cayman Islands. He advises on IPOs, SPACs and M&A transactions, start-up businesses and fund formations. He is a member of the firm’s Digital, Blockchain and Fintech group, working with blockchain companies, token issuers, technology companies and cryptocurrency fund managers on a regular basis. Email: bradley.kruger@ogier.com.

Johan Leonard leads the Stibbe Luxembourg Tax practice. Johan specializes in national and international tax law, providing structuring and transactional advice to
investment funds, private equity firms, real estate conglomerates, financial institutions, and multinational groups. He also assists clients in the context of tax litigation and has broad experience in advising clients on the tax aspects of multi-jurisdictional transactions and restructurings. Johan holds a master’s degree in law from the Université catholique de Louvain and a Master of Laws (LLM) in International Taxation from New York University. Email: johan.leonard@stibbe.com.

Antti Lehtimaja is a Tax Partner and Head of the tax practice group at Krogerus. He completed his Master of Laws at the University of Helsinki in 1998 and was admitted to the Finnish Bar Association in 2003. Before joining Krogerus in 2010, he had previously worked for several years in the tax department of another leading Finnish law firm, completed one year of trainee service as a judge in a district court and worked at the Finnish Tax Administration as a corporate tax specialist as well as a presenting officer at the Central Tax Board, a body that gives advance tax rulings in Finland. He has written numerous taxation-related articles and lectures frequently. He is a member of both the International Bar Association (IBA) and the International Fiscal Association (IFA). Email: antti.lehtimaja@krogerus.com.

Ricardo Leon Santacruz is Sánchez Devanny’s Managing Partner. He is a tax attorney with more than twenty-five years of experience. He has a broad-based transactional tax practice focused on Mexican inbound and outbound tax planning and transfer pricing; tax treaties, their application and limitations; anticipation of anti-deferral and anti-abuse legislation; and overall Income Tax and VAT rationalization. His expertise allows him to structure tax-efficient domestic and cross-border acquisitions, mergers, reorganizations, spin-offs, redemptions, liquidations, post-acquisition integrations and business restructurings. Ricardo’s transfer pricing experience allows him to proactively advise clients on the design and implementation of intellectual property, financing, e-commerce, procurement and distribution of goods and performance of services transactions. His experience and sensitivity have afforded Ricardo prominent recognition in the market as a trusted private family advisor that can render guidance on tax optimization and multigenerational planning family governance. He is the Co-chair of the Taxes Committee of the International Bar Association. Email: rls@sanchezdevanny.com.

Alicia Lim was a trainee with GSM Law LLP and joined the firm as an associate after being called to the Singapore Bar in 2017. Email: alicia@gsmlaw.com.sg.

Wendy Lim is an Associate in MinterEllison’s national tax practice, specializing in income tax, capital gains tax, international tax, and employment tax. Wendy’s work spans a range of industries, including real estate, mining and financial services. In 2019, Wendy was the runner-up in the International Bar Association’s Taxes Committee Scholarship on the topic of whether corporate taxes should be based on residence, source or another concept. Email: Wendy.Lim@minterellison.com.

Foo Yong Lim was a trainee with GSM Law LLP and joined the firm as an associate after being called to the Singapore Bar in 2019. Email: yonglim@gsmlaw.com.sg.
David Dingfa Liu is an International Partner of Duan & Duan. His practice is focused on cross-border mergers and acquisitions, tax, customs and commercial matters affecting cross-border investment. He also represents high net-worth individuals in their estate and tax planning matters. Email: david.liu@duanduan.com.

Jorge Lopez Lopez has more than ten years of legal experience. His practice is primarily focused on national and international corporate tax issues as well as wealth management issues. He has experience in a variety of tax matters, including M&A, corporate restructurings, transfer pricing and audit management and defence. His experience also comprises tax litigation and the implementation of defence strategies before tax and judicial authorities. Jorge is a candidate for a Master of Laws (LL.M.) in International Taxation from the University of Florida and has a Master of Laws in Tax from the Universidad Panamericana. Email: jlopez@sanchezdevanny.com.

Margriet Lukkien is a Tax Partner and advises multinationals (especially North-American-based), financial institutions and sovereign wealth funds on Dutch corporate tax and dividend tax aspects and accompanying international tax aspects. Her expertise includes international structuring/restructuring taking into account the OECD and EU developments on BEPS. Margriet is an active member of the International Tax Affairs Section of the Dutch Association of Tax Advisers (NOB). In addition she has been an active member of the International Bar Association (IBA), since she won the 2010 IBA Taxation Scholarship. Margriet has been an officer of the IBA Taxes Committee since 2013, and she has taken up the role of co-chair of the IBA Taxes Committee for 2019 and 2020. Email: Margriet.Lukkien@loyensloeff.com.

Suvrat Mehta is a Litigation Associate at ASC Legal, Solicitors & Advocates, New Delhi, India. Mr Mehta is the Member of Bar Council of India and has over four years of experience in the field of Advisory and Litigation in Cybercrime, Data Protection Law, AI, Blockchain, Fintech, E-commerce, Financial & EOW crimes, Privacy Law, Trademarks, Copyright and Consumer & Electronic Evidence. He is the first Indian to have contributed in the Data Breach Investigation Report (DBIR), 2017, released by Verizon that presents findings from security incident investigations and has also showcased his research skills on various Indian Cyber Law books published. Email: suvrat.mehta@aseemchawla.com.

Ban Su Mei is a tax and private client lawyer in practice since 1999. After graduating from the National University of Singapore in 1998, she joined the Tax and Private Client department of a large Singapore law firm and eventually rose through the ranks to become equity partner before co-founding GSM Law LLP. Email: ban@gsmlaw.com.sg.

Alina Miyake is an Associate at Machado Meyer in São Paulo. Alina holds a bachelor’s degree from the Faculty of Law of the University of São Paulo (USP). She is specialist in tax law, more specifically on the provision of consultancy related to direct taxes and international taxation. Her practice encompasses tax planning, merger and acquisition
transactions, corporate restructurings in general, and international taxation. Email: amiyake@machadomeyer.com.br.

**Doron Mutai** leads Shibolet & Co.’s international tax practice. Doron specializes in all areas of income tax, with a focus on international tax, M&A transactions, taxation of activities in the capital markets, blockchain and smart contracts. Doron’s expertise relates to all aspects of Israeli income tax, while he has extensive knowledge of other tax systems as well. His vast experience in this field allows him to advise Israeli residents on the tax aspects of their activities in Israel and abroad, and to advise non-Israeli residents on their activities and investments in Israel. In this respect, Doron consistently advises non-Israeli multinationals that acquire Israeli hi-tech companies, non-Israeli banks that operate in Israel, companies of the Oil & Gas industry that operate in Israel’s Exclusive Economic Zone and hi-tech companies on their activities in Israel and abroad. Email: d.mutai@shibolet.com.

**Vikram Nagrani** is a Partner of Hassans International Law Firm, Gibraltar’s leading law firm for over two decades. Vikram has a profound knowledge in a range of core topics in distributed ledger technology (‘DLT’), which range from token issuances, security token offerings, and other DLT matters including licence applications under Gibraltar’s DLT Providers Regulations. He has also assisted with the development of the DLT regulatory framework in Gibraltar, including being involved in the drafting of Regulatory Guidance Notes to Gibraltar’s Distributed Ledger Technology Regulations and assisting with the draft regulatory framework for Tokens in Gibraltar. Vikram has co-authored two manuals on virtual currencies for the United Nations Office on Drugs and Crime, intended as training and educational material for law enforcement agencies and for regulators. He has attended the European Commission’s Blockchain Observatory and Forum, and is an inaugural member of the advisor board of the European Law Observatory of New Technologies. He has also contributed to various international events and initiatives as a speaker and is considered a thought leader in the space. Vikram is also very experienced in all aspects of corporate and commercial legal work, including large M&A transactions, and a variety of financing transactions and structures. He also advises high net-worth individuals and families on their wealth and estate planning structures as a fully qualified Trusts and Estate Practitioner and is a practising notary public. Email: vikram.nagrani@hassans.gi.

**Saam Nainifard** is an Associate in the Tax Group at Aird & Berlis LLP. He advises on all aspects of income taxation, with a particular focus on corporate taxation and reorganizations, mergers & acquisitions and international tax matters. Saam is also a member of the Blockchain group at Aird & Berlis LLP. He has a wide variety of experience in representing clients in the crypto asset space, including structuring foreign investments in crypto mining operations in Canada representing investors in tax disputes with the Canada Revenue Agency involving crypto asset transactions. Email: snainifard@airdberlis.com

**Elias Neocleous** is the Managing Partner of Elias Neocleous & Co LLC and a specialist in tax law, tax planning, and advanced business structuring. He completed his studies
at Oxford University in the UK and was called to the UK Bar in 1992 and to the Cyprus Bar in 1993. He has been a partner in the legacy firm since 1995. He has extensive experience in advising international organizations on tax and tax planning issues and is recognized as a leading tax advisor to high net-worth individuals. Elias is a frequent speaker at international events and has numerous publications to his credit. He is a member of several international legal and business networks including the International Tax Planning Association and is a highly rated lawyer in all key international directories. In addition, Elias is currently a board member of the Cyprus Investment Promotion Agency and the Honorary Consul of Portugal. Email: elias.neocleous@neo.law.

Raquel Novais is a Senior Tax Partner at Machado Meyer in São Paulo, Brazil. Raquel holds a bachelor's degree from Faculdade de Direito de Franca and a Master’s in Tax Law from Pontifícia Universidade Católica de São Paulo. She has ample experience in both domestic and international taxation, as well as tax controversy. Raquel’s practice is divided between tax consultancy and high-end technical tax conflicts settlement. She is frequently engaged as a speaker at tax law conferences, is a member of several international legal organizations and networks and has top rankings in several international directories. Email: rnovais@machadomeyer.com.br.

Raul-Angelo Papotti is a Partner and Head of the Tax and Tax Planning department at Chiomenti in Italy. He has completed his studies in Milan and Leiden and has been admitted to the Italian Bar Association. Before joining Chiomenti in 2007, Raul-Angelo has previously worked in a leading law firm in London. He advises Italian and international clients on tax law and tax planning, cross-border taxation and transfer pricing, M&A transactions, private wealth management, trusts and estate planning matters. His clients include leading global investment banks, Italian and foreign multinationals, and prominent high net-worth individuals, families and family offices. He is author of many publications on international tax matters and is a frequent speaker at domestic and international congresses. Raul-Angelo is a member of several international legal organizations and networks and he is ranked as a leading expert in international tax law in the foremost international legal guides such as Chambers, Legal 500 and Who’s Who Legal. Email: raul.papotti@chiomenti.net.

Leandro M. Passarella is a founder of Passarella Abogados, where he leads its tax practice. He obtained his law degree in 1995 with honours and his joint LLM degree and International Tax Program certificate at Harvard Law School in 1998, where he was also recognized for his thesis on the source rule of income from derivative financial instruments. After being a member and heading tax practices of other law firms, he founded his boutique tax law firm, Passarella Abogados, in 2010. Since then, both Leandro and his firm have received awards and recognitions by international tax publications. Leandro also participates as panel co-chair or speaker regularly in conferences of his specialty, with active participation at the International Bar Association. Since 2004, he has been a Professor of ‘Basic Income Taxation’ for the Master’s in Tax Law of Universidad Torcuato Di Tella (Buenos Aires, Argentina). Email: lmp@palegal.com.ar.
Pepijn Pinkse is a Tax Lawyer and Senior Associate, advising Dutch and foreign listed multinationals as well as large privately owned companies, on corporate income tax, mergers and acquisitions, reorganizations and IPOs. In the case of privately owned companies, he is also involved in advising the shareholders. He is a member of the Fintech Team and regularly advises clients across a range of financial technology fields, including payments, identity and security and data analytics. He also has a focus on initial coin offerings (ICOs), cryptocurrencies and distributed ledger technology (DLT) in the broad sense. Email: Pepijn.pinkse@loyensloeff.com.

Joanna Prokurat is a certified tax adviser with almost fifteen years of experience. She advises clients on Polish and international tax law, particularly on corporate income tax, VAT, international tax planning, tax optimization, and taxation of transactions. She specializes in tax advisory for new technology sector, including cryptocurrencies, gaming, fintech as well as tax optimization solutions for innovation taxpayers (including IP Box, R&D tax relief, R&D centres, etc.). Ms. Prokurat is completing her LLM in Poland. Email: joanna.prokurat@wardynski.com.pl.

Diogo Ortigão Ramos is a Partner and Head of Cuatrecasas’ tax practice in Portugal. He focuses his practice on EU, national and international taxation, particularly regarding M&A, buyouts, corporate restructuring, financial transactions, real estate investment structuring and transactions, and tax and customs litigation. He is a member of the Portuguese Bar Association (since 1989), the Portuguese Tax Association, the International Fiscal Association, the Portuguese Association of Tax Consultants, the International Bar Association and the American Bar Association, and has been acknowledged by the Portuguese Bar as a specialist tax lawyer. Diogo is a member of the European Tax Law Group, Tax Associates Meeting and of the Europe VAT Group, the members of which are renowned European law firms, leaders in their respective jurisdictions. He is the Portuguese representative of the Foreign Lawyers Forum of the American Bar Association. Diogo obtained his law degree from Universidade Lusíada (1989) and postgraduate degree in taxation from ISG – Business & Economics School (1995). Email: dortigaoramos@cuatrecasas.com.

Daniel Resas is an Associated Partner at the German law firm SMP where he is heading the firm’s Blockchain and Digital Assets practice group. He advises all range of clients on tokenization and blockchain-related business models, transactions and regulatory policy. In addition, he is a Senior Fellow at the Wharton School of the University of Pennsylvania and co-founder of regular international working groups on blockchain regulation/Decentralized Finance as well as blockchain governance hosted by the Wharton School. Email: daniel.resas@smp.law.

Michael Robinson is a Senior Associate of Ogier’s Corporate team in the Cayman Islands. He specializes in Cayman corporate matters and, in particular, mergers and acquisitions, restructurings, reorganizations, public listings, and migrations. He also advises technology companies, ICO/STO/IEO issuers and cryptocurrency funds and is a member of the firm’s Digital, Blockchain and Fintech group. Email: michael.robinson@ogier.com.
Monica Reyes Rodriguez is the Founding Partner in Reyes Abogados Asociados in Bogota, Colombia. She obtained a major in Law from Universidad del Rosario in Bogota, and specialized in taxes in the same university. She attended LLM courses in London School of Economics and obtained a diploma in International Tax Law at the Kennedy University in Switzerland. Ms. Reyes worked at the Colombian National Tax Administration and at Occidental Petroleum Inc. For ten years, she served as the Partner in charge of the fiscal practice in the Colombian law firm Brigard & Urrutia Abogados. Ms. Reyes has taught tax law master’s degree courses at Universidad del Rosario and Universidad Externado de Colombia and is currently teaching in Universidad de los Andes in Bogota. She is part of the Editorial Committee of the Magazine on Taxes published by Legis S.A. She was president of the Colombian Chapter of the International Fiscal Association and is a member of the Colombian Tax Law Institute and of the Tax Sections in the American Bar Association and the International Bar Association. Email: mreyes@reyesaa.com.

Daria E. Romanova specializes in Tax Law, currency regulations, complex evaluation of tax risks and consulting in tax planning. Daria has experience in legal consulting since 2009. Before joining AT Lawyers, she had been working with Russian law firm ‘FDP United Consultants’ where she specialized in legal support of budget investments in construction and development, VAT taxation, other complex tax issues and representation of clients in disputes with tax authorities. Daria holds a master’s degree (LLM in Maritime Law) awarded by the Oslo University, Norway. She has also graduated with honours from the Moscow State University. Email: romanova@atlawyers.com.

João Pedro Russo has been at Cuatrecasas since 2019, working in this firm’s tax practice. He focuses his practice on EU, national and international taxation, particularly regarding M&A, buyouts, corporate restructuring, financial transactions and transfer pricing. João obtained his law degree and postgraduate degree in Tax Law and Regulation of Financial Markets from Universidade de Lisboa (2013). Email: joao.russo@cuatrecasas.com.

Matthieu Sabonnadiere has been a Senior Associate with the international tax department of CMS Francis Lefebvre Avocats since 2019. He assists mainly MNEs on cross-border transactions, financing, restructuring and tax litigation. Before joining the firm, he practised during three years with Baker McKenzie Paris. He holds an LLM in International Taxation (class 2015) from New York University and Master’s in Corporate Taxation (class 2013) from Université Paris Dauphine. Email: matthieu.sabonnadiere@cms-avocats.com.

Gurbachan Singh is regarded as one of Singapore’s leading tax lawyers, who began his career as a Legal Officer with the Inland Revenue Authority of Singapore almost forty years ago. He was a Judicial Officer at the Subordinate Courts prior to joining private practice, and was Managing Partner of one of the largest firms in Singapore prior to founding GSM Law LLP. Email: guru@gsmlaw.com.sg.
Theodoros Skouzos, born in 1975, is a practising advocate, registered in the Athens Bar Association, Greece and Managing Partner of the law firm Iason Skouzos & Partners. He has published several articles in Greek and English about tax topics, and has participated in tax law panels at the IBA annual conference and other international conferences. He is a member of the International Tax Specialist Group (www.itsgnetwork.com) and chairman of the Tax Committee of the Hellenic Association of Law Firms. He is ranked as a leading Greek tax law practitioner in international directories. He graduated from the University of Northumbria at Newcastle in 1998 with an LLB and a License en droit from the Université d’Orléans in France, having completed the programme ‘LLB exempting with French Law’. In 1999 Theodoros was awarded the LLM in European Union Business Law by the University of Amsterdam. Email: tskouzos@taxlaw.gr.

Tapasi Sharma is a Research Associate at ASC Legal Solicitors & Advocates, New Delhi, India. Miss Sharma holds a merit degree in LLM in International Commercial Law from London, United Kingdom, and she is also a recipient of various accolades during her Masters in London. Miss Sharma is Member of Bar Council of India and has three years of post-qualification experience in both UK and India in the field of investigation, GDPR, research, commercial and taxation matters. Email: tapasi.sharma@aseemchawla.com.

Kevin Smith is a Partner in the Tax Practice of Matheson and is also a member of the Structured Finance and Derivatives Group. Kevin advises financial institutions, investment banks, investment managers and institutional investors on all tax aspects of financial services in Ireland, including securities transactions, debt capital markets, cross-border financing and derivative transactions. Kevin also advises many of the world’s largest aircraft leasing companies on tax aspects of carrying on aircraft leasing business in or from Ireland. Email: kevin.smith@matheson.com.

Nicholas Warren has a strong professional background with over sixteen years of work experience which complement his qualifications which include a Masters in Strategic Planning, a Bachelor of Commerce (B.Com.) Honours focused in Banking & Finance from the University of Malta, ACCA qualified as well as Certificates in Islamic Finance. Throughout his career he has focused his attention predominantly towards providing counsel, guidance and consultancy to international clients on the various possibilities presented by Malta as a Financial Services Centre. He commenced his passion for financial services as a manager with the Malta Financial Services Authority, focusing on Professional Investor Funds, UCITS Schemes and Investment Services Licence Holders (MiFID) and has also assumed management positions at two large fund management companies. He expanded his horizons in the fields of banking, payment services and financial institutions, capital markets as well as blockchain. Email: nicholas@fjvassallo.com.

Robert Yunan is a Special Counsel in MinterEllison’s national tax practice, specializing in income tax matters. He acts for taxpayer clients of all sizes and is adept at advising on transactions across all stages of the business life cycle, from establishment,
Restructuring and expansion to operation and exit. He has acted extensively for inbound and outbound medium-sized to large corporate entities, government and major international funds. His work involves assisting with capital gains tax, tax consolidation, international tax (including funding and repatriation) and executive remuneration. Yunan is also a qualified chartered accountant. **Email:** Robert.Yunan@minterellison.com
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1. COUNTRY GUIDES

1.1 United Kingdom

1.1.1 Applicable Tax Law, Guidance, and Case Law

(a) Which laws, regulations, and other administrative guidance exist dealing with crypto assets?

At present, the tax law of the UK does not explicitly address the taxation of crypto assets. Their taxation is therefore determined in accordance with the general body of UK tax law governing the taxation of income, gains and transactions (itself a combination of statute and case law). Her Majesty’s Revenue and Customs (HMRC), the UK tax authority, has, however, issued (non-binding) guidance setting out how it considers such laws apply to transactions involving crypto assets which are exchange tokens.1,2 Exchange tokens are intended to be used as a means of payment and include ‘cryptocurrencies’ like bitcoin. They do not provide the holder with any rights to any underlying property or access to goods or services. Their value is based on their use as a means of exchange or investment.2

In contrast to exchange tokens, the value of utility tokens and security tokens derives from the holder’s right to an underlying asset (or interest therein). Utility tokens provide the holder with (current or future) access to particular goods or services. They are issued by businesses or groups of businesses who commit to accepting the tokens as payment for the particular goods or services in question. Security tokens have some characteristics in common with traditional securities such as shares or notes; they provide the holder with a particular interest in a business, such as a share in the issuer’s profits or rights akin to debt instruments.3

1. HMRC policy papers ‘Cryptoassets: tax for individuals’ and ‘Cryptoassets: tax for businesses’ (both updated 20 Dec. 2019).
2. Exchange tokens are intended to be used as a means of payment and include ‘cryptocurrencies’ like bitcoin. They do not provide the holder with any rights to any underlying property or access to goods or services. Their value is based on their use as a means of exchange or investment.
3. In contrast to exchange tokens, the value of utility tokens and security tokens derives from the holder’s right to an underlying asset (or interest therein). Utility tokens provide the holder with (current or future) access to particular goods or services. They are issued by businesses or groups of businesses who commit to accepting the tokens as payment for the particular goods or services in question. Security tokens have some characteristics in common with traditional securities such as shares or notes; they provide the holder with a particular interest in a business, such as a share in the issuer’s profits or rights akin to debt instruments.
The guidance highlights that the tax treatment of exchange tokens is fact-specific. Nevertheless, HMRC confirms that exchange tokens are not considered to constitute currency or money, and would instead be considered assets in their own right. The specific tax treatment which may apply to these assets is considered in further detail below.

It is worth noting that HMRC has expressly stated that its ‘views may evolve further as the sector develops’, and so its contents are not necessarily definitive. The guidance also clarifies that, when assessing the tax treatment of crypto assets, terminology will not be determinative, and HMRC will ‘look at the facts of each case and apply the relevant tax provisions according to what has actually taken place’.

(b) Which court cases exist dealing with crypto assets?

At the date of writing, no judgements have been given in UK courts or tribunals specifically regarding the taxation of crypto assets. There is, however, one decision of the European Court of Justice (ECJ) regarding the value added tax treatment of certain transactions in bitcoins.4 This decision would be binding in the UK even after the end of the Brexit transitional period (during which the UK and the EU Member States have agreed to treat the UK as though it is a Member State of the EU), unless it is subsequently overruled by domestic UK legislation or the UK Supreme Court decides to depart from the ECJ’s decision.5 The UK Government has not given any indication that it intends to legislate on the subject.

1.1.2 Income and Capital Gains Taxes

(a) How are crypto assets classified for income and capital gains tax purposes?

As mentioned above, HMRC considers that exchange tokens constitute neither money nor currency. This means that specific UK tax rules relevant to such assets (such as the foreign exchange currency rules, the ‘disregard’ rules relating to exchange gains and losses, and rules governing designated currency elections) will not apply. Exchange tokens will therefore be taxed as assets in their own right.

Subject to certain exceptions (including those discussed below), the tax treatment of exchange tokens will depend on whether they are characterized as capital assets or non-capital assets (e.g. trading assets). Given that HMRC has noted in its

5. Any decision by the UK Supreme Court to depart from retained EU case law would be subject to the same rules which apply to Supreme Court departures from its own previous case law. In Jul. 2020, the UK Government launched a public consultation regarding the possibility of allowing lower UK courts and tribunals to depart from retained EU case law (as to which, see ‘Retained EU Case Law – Consultation on the departure from retained EU case law by UK courts and tribunals’, dated 2 Jul. 2020).
6. Crypto assets could be non-capital assets without necessarily being trading assets. For example, receipts in respect of a crypto asset could be characterized as ‘miscellaneous income’ (see further
guidance that it similarly considers that other crypto assets are neither currency nor money, it is expected that the same would generally be true of such crypto assets (although that point is not expressly dealt with in HMRC’s guidance).

Whether crypto assets are considered to be held by a taxpayer as non-capital assets (such that receipts in respect thereof are characterized as income subject to income tax or corporation tax) or capital assets (such that receipts in respect thereof would be subject to capital gains tax or corporation tax on chargeable gains) will be decided based on general principles. This is a fact-specific question, generally dependent on whether the taxpayer is carrying on a business in the nature of a trade vis-à-vis the crypto assets in question or holding the crypto assets as a capital asset (see further below).

Notwithstanding the above, in determining the applicable tax treatment, in some cases it would not be necessary to consider whether crypto assets are held by a taxpayer as capital assets or non-capital assets. For corporation taxpayers, specific tax regimes apply to certain kinds of assets, such as loan relationships, or intangible fixed assets. Broadly, assets within the scope of these special regimes are taxed by reference to the debits and credits recognized for accounting purposes in respect thereof in the taxpayer’s (GAAP-compliant) profit and loss statement, and the applicable tax treatment does not generally depend on the asset’s characterisation as a capital or non-capital asset.

HMRC considers that:

- Exchange tokens would not be within the scope of the special tax regime applying to loan relationships, because the exchange tokens would not constitute ‘loan relationships’ (i.e., ‘money debts arising from a transaction for the lending of money’). This is because arrangements governing the mere holding of exchange tokens do not, given the lack of a counterparty, give rise to a debt.
- Exchange tokens may, depending on the circumstances, constitute ‘intangible fixed assets’, and hence may fall to be taxed in accordance with the special tax regime applying thereto. Broadly, to be characterized as ‘intangible fixed assets’, crypto assets would need to be both:
  (i) Intangible assets for (generally accepted) accounting purposes.

Generally, crypto assets would not meet this test if they are held for sale
[12] In the ordinary course of business (i.e., inventory for accounting purposes).

(ii) Acquired or created by the company for use on a continuing basis in the course of the company's activities (effectively, a 'fixed' asset for accounting purposes). HMRC has confirmed that merely holding crypto assets, even in the course of the company's activities, would not be sufficient to meet this test.

Although not expressly stated in HMRC’s guidance, crypto assets which are stock in trade, and crypto assets held solely for investment purposes, should not, therefore, generally qualify as intangible fixed assets.

As mentioned above, the tax treatment of utility tokens and security tokens has not been addressed by HMRC. As with exchange tokens, it can be expected that the tax treatment will be fact specific and will depend on whether the circumstances are such that the crypto assets in question (i) meet the criteria for taxation under a special tax regime (such as the intangible fixed assets regime13) or failing which, (ii) fall to be taxed in accordance with the general capital/non-capital asset distinction described above. For these reasons, the responses to the questions below do not consider the position if HMRC were to take the view that such assets are characterized as anything other than: (i) capital assets (not subject to any special tax regime), (ii) non-capital assets (not subject to any special tax regime) or (iii) intangible fixed assets.

(b) What are the income/capital gains tax consequences of selling crypto assets against fiat currency?

The tax treatment of gains and losses from the sale of crypto assets against fiat currency depends on whether (i) (for corporation taxpayers) such crypto assets are 'intangible fixed assets' and (ii) if not (and for non-corporation taxpayers generally), whether they are capital or non-capital assets. HMRC does not consider that the holding of exchange tokens is a speculative venture akin to gambling (the proceeds of which are free from tax). It seems likely that HMRC would take the same view with utility tokens and security tokens.

Capital asset

Generally, if such assets are held as capital assets, then chargeable gains (or allowable losses) will arise on disposal. A chargeable gain will typically be taxable at a rate of 10% or 20% for individual capital gains taxpayers (depending on the amount of their taxable income in the relevant year) or 19% for corporation taxpayers. The chargeable gain (or allowable loss) will, broadly, be calculated as: (i) the consideration received

12. Finance leasing of intangible fixed assets is expressly brought within the regime by the Corporation Tax (Finance Leasing of Intangible Assets) Regulations 2002, even if the assets being leased are accounted for as financial assets. However, an exclusion applies where the lessee within the charge to income tax uses the assets in the course of a trade or business.

13. See supra n. 8.
for the disposal less (ii) the consideration paid for the crypto assets, and allowable incidental costs such as transaction fees and legal and valuation costs.\footnote{14} Where the crypto assets disposed of were mined, HMRC does not consider that the costs incurred in such mining can be deducted. Irrespective of whether a disposal is between related parties, if it is not on arm’s length terms, then the market value of the crypto assets disposed of will be substituted for the consideration received.\footnote{15} Individuals may be able to apply their capital gains tax annual allowance (of up to GBP 12,300 per person for the 2020/21 year) against any gain.

Capital losses can generally be offset against capital gains in the current period or carried forward for offset against capital gains in future periods (but not carried back to offset gains in past periods).\footnote{16} For corporation taxpayers, from April 2020, restrictions have been placed on the quantum of carried forward losses capable of offsetting capital profits in any period.\footnote{17}

Under UK capital gains tax rules, fungible assets are generally required to be ring-fenced and ‘pooled’ (i.e. effectively treated as a single asset) for the purposes of calculating the capital gain realized on their disposal. If any fungible assets forming part of the same ‘pool’ are sold, that is considered a part-disposal of the single asset that is the pool. Deductible costs in respect of fungible assets in the same pool (which would include acquisition costs, improvements costs and incidental disposal costs incurred) are considered on an aggregate basis, and an appropriate proportion of the deductible costs can be deducted in calculating the gain on disposal of any assets within the pool (i.e. a part-disposal of the single asset that is the pool).\footnote{18} Exceptions to this ‘pooling’ treatment may apply (for example, where fungible assets are acquired shortly after a disposal). HMRC considers that exchange tokens are fungible with other exchange tokens \textit{of the same kind}, but are not generally fungible (for example, bitcoins are fungible with other bitcoins, but not with ether or litecoins). Provided that exchange tokens of the same kind are in fact fully fungible, they should be considered part of the same pool for this purpose, even if they are held in different wallets. However, whether exchange tokens are so fungible would be a question of fact.

Trading asset

If crypto assets are held as trading assets, then any profit made on their disposal will form part of the taxpayer’s trading profit, and will be subject to corporation tax at a rate of 19\% or for sole traders and other income taxpayers, income tax at a rate of 20\%, 40\% or 45\% (depending on their total taxable profits for the period). Individuals can benefit from an annual allowance (of GBP 1,000 for the 2020/2021 tax year) below which trading (and miscellaneous) income would not be subject to tax.\footnote{19}

\footnotesize
\begin{itemize}
\item 15. Section 17 of the Taxation of Chargeable Gains Act 1992.
\item 19. Sections 783A–783A Income Tax (Trading and Other Income) Act 2005
\end{itemize}

In calculating the profits of the trade for a period, the starting point is the profit recognized in the (GAAP-compliant) accounts for that period.\textsuperscript{20} There is no market value override. Total taxable profits would be calculated by subtracting total deductible expenses (adjusted, for tax purposes, to add back any expenses not incurred wholly and exclusively for the purposes of the trade) from total income. Since April 2017, subject to certain restrictions (including as to quantum), corporation taxpayers can set off trading losses against other taxable profits or capital gains from current, past or future periods. For income taxpayers, (again, subject to certain restrictions) trading losses can be offset against other current year profits or capital gains and carried forward to offset against future trading or other profits (but cannot be carried back to offset against past profits).

A taxpayer need not necessarily trade \textit{in} crypto assets for them to constitute trading assets. Crypto assets used in the course of a taxpayer’s trade could, in some circumstances, be trading assets. For example, if a security token acquired by a taxpayer entitled the taxpayer to services which it intended to use in the course of its trading business (such that the expenditure on the token was incurred wholly and exclusively for the purposes of its trade), it is possible that the security token would constitute a trading asset.

\textbf{Intangible fixed asset}

For the purposes of the intangible fixed assets regime, tax broadly ‘follows the accounts’. A disposal will only be taxable if: (i) there is a ‘realisation’, which broadly requires that the asset ceases to be recognized on the balance sheet, or its balance sheet value is reduced (a ‘part-realisation’) and (ii) a profit (or loss, as applicable) is recognized in the taxpayer’s (GAAP-compliant) profit and loss statement.\textsuperscript{21} The amount taken into account for tax purposes is the difference between (i) the proceeds of the realisation (i.e. the amount recognized as the proceeds in the accounts, less the amounts recognized as incidental costs of realization), and (ii) the tax written down value of the asset prior to realisation. However, if the sale is between related parties, the realisation is, for such purpose, treated as having taken place at market value.\textsuperscript{22}

\textbf{(c) What are the income/capital gains tax consequences of exchanging crypto assets against other crypto assets?}

Such an exchange will, as a general matter, constitute a taxable event, involving both a disposal and an acquisition for each of the relevant taxpayers.

If the assets exchanged are capital assets, HMRC considers that such an exchange would constitute a ‘barter’ transaction.\textsuperscript{23} There would be a taxable disposal of crypto assets by both parties. This would be taxed as described in section 1.1.2(b) above, with

\textsuperscript{21} See Chapter 4 of Part 8 of the Corporation Tax Act 2009.
\textsuperscript{22} Section 845 of the Corporation Tax Act 2009.
\textsuperscript{23} HMRC Capital Gains Tax Manual, paragraphs CG12100 and CG78310.
the proviso that, for the purposes of calculating the taxable gain, the consideration received for the disposal would (if the bargain is at arm’s length) be the value, in pounds sterling, of the crypto assets received on the date of exchange. On a subsequent disposal of the assets acquired, the allowable acquisition cost would similarly be the value of the crypto assets disposed of, in pounds sterling, on the date of exchange. Holdover or rollover relief would not generally be available.24

The consequences of disposing of trading assets, and intangible assets, are discussed in section 1.1.2(b) above. On an exchange of intangible fixed assets, however, rollover relief may be available.25 As with a disposal, the tax consequences of acquiring trading or intangible fixed assets will depend on the impact the acquisition has in the profit and loss statement, and whether any debits recognized therein are incurred wholly and exclusively for the purposes of the trade. For intangible fixed assets, if the acquisition is capitalized for accounting purposes (i.e., reflected in the balance sheet), annual amortisation relief should also be available.

(d) If a distinction is made between business assets and non-business assets, when does trading in crypto assets lead to a trade or business?

As discussed in section 1.1.2(a) above, the tax treatment of crypto assets will often depend on whether the crypto assets are trading assets or capital assets. This would be the case, for example, where the crypto assets are not subject to any special tax regime, such as the intangible fixed assets regime. In such circumstances, it will be necessary to consider whether the taxpayer is carrying on a trade vis-à-vis the particular crypto assets.

Whether taxpayers are carrying on a trade vis-à-vis crypto assets will be determined based on UK case law, and in particular, an assessment of whether the so-called ‘badges of trade’ (i.e., indicia of trading) are present in the taxpayer’s activities. There is no bright-line test, and different indicia may weigh in different directions. Some of the factors to be considered are the degree and frequency of the taxpayer’s activities, the taxpayer’s level of organisation, the taxpayer’s motive, the commerciality of the transactions and the interval between purchase and sale.26

HMRC notes in the draft guidance that the approach in determining whether a taxpayer is trading in exchange tokens will be similar to that taken when considering whether a taxpayer is trading in shares and securities. Generally, it is considered more difficult to prove the existence of a trade in such assets.

HMRC considers that in the majority of cases, individuals will not be holding exchange tokens for trading purposes, and they will instead constitute capital assets.

24. Rollover relief might be available if the assets disposed of were capital assets used in the taxpayer’s trade, and the proceeds are reinvested in assets to be put to the same use (as to which, see section 152 of the Taxation of Chargeable Gains Act 1992).
(e) What are the income/capital gains tax consequences for an employee receiving wages or salaries in crypto assets?

Such earnings would generally be subject to tax as employment income, in the same way as cash earnings. The applicable income tax, employer’s national insurance contributions, and employee’s national insurance contributions payable in respect of such employment income would, broadly, be calculated based on the value of the crypto assets on the date of payment.

How such income tax and national insurance contributions will be accounted for to HMRC will depend on whether the crypto assets can be readily converted into their monetary value (so-called readily convertible assets). HMRC considers that, for exchange tokens, this will typically be the case. In such circumstances, a UK employer will need to account to HMRC for the applicable income tax and national insurance contributions, based on its best estimate of the value of the assets received. The employee will need to ‘make good’ or reimburse the employer within a certain period for the income tax and employee national insurance contributions (or such payment by the employer will itself be treated as similar to a taxable bonus payment to the employee).²⁷

If the crypto assets received could not, for whatever reason, be readily converted into their monetary value (such that they are not ‘readily convertible assets’), then the employee would have to report such earnings to HMRC as part of its self-assessment return, and pay the applicable income tax to HMRC itself. In such circumstances, for employer’s national insurance contribution purposes, the crypto assets would be treated as a ‘benefit in kind’, subject to slightly different rules (although the amount of the contribution payable would not typically differ).

The above applies equally if the crypto assets are provided by a third party by reason of the individual’s employment. However, in such a case, there are circumstances where the employer’s national insurance contributions may be payable by the third party, rather than the employer.

If the employee subsequently disposed of the crypto assets received, typically, any gain would be subject to capital gains tax. In calculating the gain, it would be expected that the value of the crypto assets used, on acquisition, for income tax purposes would be treated as the acquisition cost for capital gains tax purposes.

(f) What are the income/capital gains tax consequences for a merchant receiving payment in crypto assets?

If a person carrying on a trade accepts payments from its customers in crypto assets (being ‘money’s worth’), the tax consequences are the same as they would be if the customer had paid in fiat currency. The value of the crypto assets received (in pounds

sterling, on the date of receipt) would be a taxable trading receipt (even if not recognized in the taxpayer’s profit and loss statement).28

If the merchant subsequently disposed of the crypto assets received (e.g., in exchange for fiat currency) that would constitute another taxable transaction. Unless the taxpayer is trading in crypto assets, the crypto assets received from customers are unlikely to be held as trading assets (such as inventory). Instead, they are likely to be characterized as capital assets, such that their disposal would be subject to capital gains tax (see section 1.1.2(b) above). In such circumstances, the allowable acquisition cost would be the value of the services for which the crypto assets were provided as consideration (such services being ‘money’s worth’).29 which should generally equate to the value of the crypto assets brought into account for income tax purposes on receipt.

(g) What are the income/capital gains tax consequences of a loss of crypto assets?

Crypto assets may be lost if the private key associated with an address at which crypto assets are stored is lost.

For capital gains tax purposes, HMRC does not consider that there has been a disposal, as the crypto assets continue to exist. However, if a taxpayer can show that there is no prospect of recovering the key or accessing the crypto assets, the taxpayer can make a ‘negligible value’ claim. If successful, the taxpayer would be treated as having disposed of and re-acquired the relevant crypto asset, allowing the loss to be crystallized. Such a claim could only be made in respect of a ‘pool’ of fungible crypto assets (see section 1.1.2(b) above).

If the crypto assets lost are held as trading stock, the tax impact of the loss would generally depend on whether it resulted in the recognition of a debit or credit in the taxpayer’s profit and loss statement.30 For tax purposes, the loss of stock ‘in the normal course of trading’ would generally be allowed as a deductible expense. HMRC guidance specifically confirms that ‘the loss of stock-in-trade … by … negligence of an employee is, in the ordinary course of events, an allowable deduction.’ The same principle may apply where the crypto assets cannot be accessed because the key has been lost.31

If the crypto assets are intangible fixed assets, then the loss may be crystallized at the end of the accounting period if the value of the asset is written down in the balance sheet of the taxpayer (or the asset is removed from the balance sheet entirely), such that there is a realisation or part-realisation.

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(h) What are the income/capital gains tax consequences of a loss in value of crypto assets?

For capital gains tax purposes, a loss in value will not normally have any tax impact unless it is crystallized through a disposal. The exception is where a negligible value claim (discussed in section 1.1.2(g) above) can be made.

Where the crypto assets are held as trading stock or intangible fixed assets, a loss in value in the course of a taxable period will be crystallized at the end of the period, if the loss is reflected in the profit and loss statement for the period.

(i) What are the income/capital gains tax consequences of forks of crypto assets?

Blockchains are governed by a protocol which users of the chain (i.e., the holders of crypto assets) agree to abide by. When users want to make changes to that protocol, a ‘fork’ occurs. The changes are effectively a kind of software update.

A ‘soft fork’ occurs when all the users of the chain agree to adhere to the new changes. In that circumstance, no new asset is created, and there are no tax consequences.

In contrast, a ‘hard fork’ occurs when only a portion of the users of an existing blockchain wish to adhere to the proposed changes. They agree to create a second ‘branch’ of the original blockchain which would be subject to the revised protocol. In that circumstance, a new crypto asset, compatible with the new blockchain branch is created. Such holders retain the same number of crypto assets on the original blockchain. In addition, they receive an equal number of crypto assets on the new blockchain.

Broadly speaking, the fork itself does not create a taxable event. However, the new crypto assets and the old crypto assets are not fungible with each other. As a result, for capital gains tax purposes, a new ‘pool’ of assets would be created. HMRC considers that the value of the new crypto assets is derived from the value of the original crypto assets. The allowable costs available in respect of the latter must therefore be split between the two pools ‘on a just and reasonable basis’.32

If a person holds crypto assets on an exchange, they can only be disposed of if the exchange recognises the crypto asset. After a fork, if an exchange decides not to recognise the new or the original crypto assets such assets can become ‘trapped’, and their value reduced accordingly. In such circumstances, HMRC ‘will consider cases of difficulty as they arise’. Although not expressly confirmed by HMRC, in such circumstances, the taxpayer may be able to make a ‘negligible value’ claim (see section 1.1.2(g) above).

If the crypto assets are held as trading stock, the impact of the fork may be reflected in the ‘cost of goods sold’ figure in the profit and loss statement, and hence

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32. Sections 42(4) and 43 of the Taxation of Chargeable Gains Act 1992.
may impact the taxable profits for the period. If the crypto assets are intangible fixed assets, then whether the fork has any tax impact would depend on whether the fork gave rise to a debit or credit in the profit and loss statement for accounting purposes (e.g., because of a revaluation).

(j) What are the income/capital gains tax consequences of airdrops of crypto assets and are the tax consequences different if the airdropped tokens are unwanted?

An ‘airdrop’ occurs when a person receives crypto assets free of charge (e.g., as part of a marketing or advertising campaign). The airdropped crypto assets will generally have an infrastructure (e.g., a blockchain, or distributed ledger technology) which is new and operates independently of existing crypto assets. As such, it is not fungible with existing crypto assets. The tax consequences of an airdrop will not differ on the basis of whether the airdropped tokens are wanted or unwanted.

For capital gains tax purposes, the airdropped crypto assets will therefore need to form their own pool (which will include any other crypto assets of that specific kind already held, or subsequently acquired, by the taxpayer). The allowable acquisition cost when the airdropped crypto assets are sold should be nil. Irrespective of whether the taxpayer is trading in crypto assets, an airdrop would not be characterized as a taxable trading receipt unless it is in fact consideration for a service provided by the taxpayer in the course of their trade. However, the airdropped crypto assets may nevertheless be added to the taxpayer’s trading stock, and the proceeds of their subsequent disposal would be a taxable trading receipt.

The tax consequences of an airdrop of crypto assets treated as intangible fixed assets would generally depend on whether the airdrop had any impact on the taxpayer’s profit and loss statement or (for amortisation purposes) its balance sheet.

(k) What are the income/capital gains tax consequences of (solo, pool, and cloud) mining?

‘Miners’ are persons awarded crypto assets (or fees) in return for verifying additions to the ledger. Where the individual acts alone, this is described as ‘solo’ mining. Whether such mining constitutes a trade (such that the crypto assets awarded or fees received...
constitute taxable trading receipts) will depend on whether the badges of trade are present in the taxpayer’s activities (see section 1.1.2(d) above).

HMRC’s crypto asset guidance includes an example of a person using a home computer which has spare capacity to mine tokens, and concludes that this would not normally amount to a trade. In such circumstances HMRC considers that the taxpayer’s activities would be taxed as ‘miscellaneous income’ (being a charge to tax levied on certain income receipts which are not trading receipts). The fee received or the value of the token received (as applicable), less the costs incurred in mining, would be taxable. As mentioned above, an individual’s first GBP 1,000 of miscellaneous (and trading) income is tax-free. Any crypto assets received are likely to constitute capital assets. Their subsequent disposal would therefore be subject to capital gains tax.

Although not expressly stated in the HMRC guidance, the allowable acquisition cost for this purpose would likely be the market value of the mining services provided (which should, in an arm’s length transaction, be the value of the crypto asset, in pounds sterling, on the day of receipt). In this respect, HMRC has expressly stated that ‘capital gains tax does not need to be paid on the value of the tokens that [a taxpayer] has already paid income tax on’, but ‘capital gains tax would be chargeable ‘on the gain [the taxpayer makes after they have] received them’. Accordingly, allowable costs on the subsequent disposal cannot include costs which have already been deducted against profits for income tax, or mining costs. It is unclear whether the income tax or corporation tax paid on acquisition of the crypto asset (as applicable) may itself be deductible as an ‘incidental cost’ of acquisition.

In contrast, HMRC considers that ‘a taxpayer purchasing a bank of computers to mine tokens for an expected net profit (taking account of the cost of equipment and electricity) would probably constitute trading activity’. Although the taxpayer’s trade is the mining of crypto assets, rather than dealing in crypto assets, HMRC appears to contemplate that exchange tokens mined can form part of trading stock. The value of the tokens, in sterling, on the day of receipt would therefore constitute a trading receipt, while mining costs may be deductible if incurred wholly and exclusively for the purposes of the trade. The tax treatment on disposal of trading stock is discussed above.

The above treatment applies equally to cloud mining, where the miner does not own the equipment and software necessary to mine, but instead rents the computing

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36. HMRC Guidance ‘Check if you need to pay tax when you sell Cryptoassets’: https://www.gov.uk/guidance/check-if-you-need-to-pay-tax-when-you-sell-cryptoassets. Although not expressly stated, the same principle should, we consider, apply to corporation taxpayers subject to a miscellaneous income charge in respect of mining activity.

37. By way of analogy, when an employee disposes of employment related securities, any income tax charged on the disposal constitutes an allowable expense against the portion of the disposal proceeds subject to capital gains tax (as to which, see section 120 of the Taxation of Chargeable Gains Act). HMRC also accepts that both the stamp duty paid on the acquisition of shares and any irrecoverable value added tax on transaction expenses constitute deductible incidental expenses (see HMRC’s Capital Gains Tax Manual, paragraph CG15250 and Statement of Practice D7).
power from a provider. Any crypto assets mined (or fees received) would belong to the miner, rather than the provider. In such circumstances, the position described above would apply equally (albeit that the level of organisation required may be an indication of a trading activity). The rental costs incurred would constitute either a deductible trading expense, or an allowable deduction for capital gains tax purposes (as applicable).

Sometimes miners work collectively, distributing tasks among the group. This is referred to as ‘pool’ mining. The tax treatment of pool mining in particular has not been covered in the HMRC crypto assets guidance. Broadly, the position in such circumstances should be as described above - albeit that, again, the level of organisation would seem to indicate a trading activity. However, members of the pool may be ‘carrying on a business in common with a view to a profit’,38 such that the pool would constitute a partnership for UK tax purposes (even if not formally registered as such). If so, members of the pool would (as applicable) be taxed on their proportionate share of the pool’s profits (computed at the level of the partnership and attributed to the partners)39 and their portion of the pool’s capital gains (as though the members had each disposed of their proportionate interest in the relevant pool assets).40

(l) What are the income/capital gains tax consequences of staking crypto assets?

Transactions on a blockchain are validated by crypto asset holders participating in the chain. Such persons often compete to be chosen to validate transactions by ‘staking’ a portion of the crypto assets they hold; the more assets staked by a person, the more likely that the person will be chosen as a validator. No new crypto assets are created as part of the process, and validators instead receive a fee for their work. If a person is chosen as a validator and does not complete the validation work, or validates a fraudulent transaction, the crypto assets they have ‘staked’ are forfeited.

Staking is not dealt with in HMRC’s crypto asset guidance. However, validation activities are unlikely to constitute trading. The fees earned are therefore likely to be taxable as miscellaneous income (see section 1.1.2(k) above).

If the crypto assets staked were trading assets, then the tax consequences of the forfeiture would depend on whether, for accounting purposes, any debits or credits were recognized in the profit and loss statement. If the crypto assets staked were held as capital assets, then any forfeiture is likely to constitute a taxable disposal. Notwithstanding that the holder obtains no consideration, the taxable gain would likely be

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38. Section 1(1) of the Partnership Act 1890.
39. The computation of profits at the level of the partnership will differ depending on whether the pool member is an individual subject to income tax (as would typically be the case) or a corporate partner subject to corporation tax. For individual partners, see section of the 849 Income Tax (Trading and Other Income) Act 2005 and HMRC Business Income Manual, paragraph BIM82210. For corporate partners, see section 1259 of the Corporation Tax Act 2009 and HMRC’s Company Taxation Manual, paragraph CTM36510.
40. HMRC Statement of Practice D/12, as set out in HMRC Capital Gains Tax Manual, paragraph CG27170.
calculated as the market value of the assets forfeited less allowable costs (such as their acquisition cost). It seems unlikely that HMRC would consider the activity sufficiently speculative to constitute gambling (such that the forfeiture of capital assets would not have any tax consequences). If the crypto assets staked were intangible fixed assets, the forfeiture would likely result in the asset being removed from (or written down in) the taxpayer’s balance sheet, thereby leading to a ‘realisation’ or ‘part-realisation’ for tax purposes (the consequences of which are described in section 1.1.2(g) above).

What are the income/capital gains tax consequences of an indirect investment in crypto assets?

Investors may wish to gain exposure to crypto assets without directly holding crypto assets. Such investors could instead invest in the assets described below:

- Shares in companies investing in crypto assets:
  - Dividends received by UK corporation taxpayers are frequently exempt from corporation tax, but this should be examined on a case-by-case basis. Individuals benefit from an annual tax-free dividend allowance (GBP 2,000 for the 2020/21 tax year). Dividends received in excess of the allowance are subject to tax at reduced rates of 7.5%, 32.5% or 38.1% (depending on the taxpayer’s total taxable income for the year).
  - For UK corporation taxpayers, broadly, the disposal of shares may benefit from a participation exemption (the so-called ‘substantial shareholding exemption’) if the taxpayer has held at least 10% of the ordinary share capital in the investee company for at least a consecutive 12-month period in the six years prior to disposal, and the company is a trading company. If these conditions are not met, the disposal would generally be taxed in the same manner as a disposal of crypto assets. For individuals, the same tax treatment applies on the disposal of shares as the disposal of crypto assets (and, in limited circumstances, qualifying individuals may be able to reduce their capital gains tax liability under the business asset disposal relief (formerly, entrepreneurs’ relief) rules).

- Units in investment funds (in the form of open ended investment companies and/or authorized unit trusts) investing in crypto assets:

41. See HMRC’s Capital Gains Tax Manual, paragraph CG12100, which discusses ‘highly speculative transactions’.
42. A full discussion of the tax consequences of investing in such assets is beyond the scope of this chapter. The response accordingly represents a brief, high-level summary of the consequences of such investment, assuming that the assets are held as investment (rather than trading) assets.
45. Reorganization relief might be available in certain circumstances (subject to meeting certain conditions) if the shares were exchanged for shares in another company.
- For income taxpayers, income distributions will be taxed in the same way as dividends received from shares.\(^{46}\) For corporation taxpayers, special rules apply, such that the tax treatment of the distribution is dependent on the source of the funds being distributed: any portion of the distribution which itself derives from distributions received by the fund will be taxed in the hands of the corporation taxpayer in the same way as a dividend. However, any remaining portion of the dividend will be subject to withholding tax at a rate of 20% (without any entitlement to a refund or credit).\(^{47}\)

- On disposal, the capital gains tax treatment would generally be the same as that applying on the disposal of crypto assets.

- Bonds paying a return which tracks the performance of any crypto asset (or any basket of crypto assets):
  - If an income or corporation taxpayer’s return (i.e., interest or the redemption amount) tracks the performance of crypto assets impacting the performance of any part of the issuer’s business (e.g., crypto assets held by the issuer), interest may be treated as a distribution and taxed in the same way as a dividend on shares.\(^{48}\) However, the annual dividend allowance would not apply for individuals. If the interest tracked the performance of crypto assets which did not in any way impact the issuer’s business, interest should be respected as such\(^{49}\) (to the extent it represents a reasonable commercial return on the principal lent).

- On disposal, for income taxpayers, the capital gains tax treatment would generally (subject to certain limited exemptions)\(^{50}\) be the same as that applying on the disposal of crypto assets. For corporation taxpayers, the bond would likely constitute a 'loan relationship', and hence would generally be taxed on the basis of the amounts recognized in the profit and loss statement.

Generally, individuals can invest an amount each year (no more than GBP 20,000 for the 2020/2021 tax year) in certain kinds of 'individual savings accounts', including a 'stocks and shares individual savings account' (a 'stock ISA'). The above shares, units, and bonds could be placed in such a stock ISA. Distributions from investments in a stock ISA are tax-free, and no capital gains tax is payable on disposal of the relevant investments.

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\(^{46}\) Regulation 22 of the Authorised Investment Funds (Tax) Regulations 2006 (SI 2006/964).

\(^{47}\) Regulations 48–50 of the Authorised Investment Funds (Tax) Regulations 2006 (SI 2006/964).


\(^{49}\) For examples of securities likely to give rise to distribution treatment on this basis, see HMRC’s Company Taxation Manual, paragraph CTM15520.

\(^{50}\) Sections 116 and 117 of the Taxation of Chargeable Gains Act 1992.
How is income from crypto assets to be treated under double tax treaty law?

HMRC has not issued any guidance as to how it intends to treat crypto assets for the purposes of the double tax treaties to which the UK is party. Nevertheless, it seems likely that:

- Income from crypto assets would fall within the scope of (the relevant equivalent of) Article 7 of the OECD Model Convention. Article 7 provides that profits of an enterprise resident in a contracting state are taxable only in that state. However, if the enterprise carries on business in the other contracting state through a permanent establishment situated therein, the profits attributable to the permanent establishment may be taxed in the other state. The UK’s treaties generally do not diverge from this position. Whether activities in a state constitute a permanent establishment would be decided on the basis of general principles (a discussion of which goes beyond the scope of this chapter); there are no rules specific to crypto assets.

- The disposal of capital assets would be taxed pursuant to (the relevant equivalent of) Article 13(5) of the OECD Model Convention. Article 13(5) provides that gains from the alienation of moveable property are generally taxable only in the contracting state of which the alienator is resident at the time of disposal. One exception is where the alienated property is part of the business property of a taxpayer’s permanent establishment; in that circumstance, the jurisdiction in which the permanent establishment is located would have taxing rights. The UK’s treaties generally do not diverge from this position. However, some double tax treaties to which the UK is party give taxing rights to a contracting state in which the taxpayer was resident during a specified period prior to the alienation.51

What are the income/capital gains tax consequences of selling crypto assets in an ICO (initial coin offering) / STO (security token offering) / IEO (initial exchange offering)?

ICOs are a means of fundraising. They are not dissimilar to initial public offerings, except that tokens are offered, rather than shares. The tokens offered can be exchange tokens, utility tokens or security tokens. In consideration for the tokens offered, investors typically give the issuer tokens in other cryptocurrencies (rather than cash). IEOs are merely ICOs which take place on an exchange.

Irrespective of how such offerings are described, their terms may vary widely. Some offerings will involve the packaging together of existing crypto assets, whereas some will involve the creation of new assets (e.g. a bundle of contractual rights which the purchaser acquires). For some offerings, the obligations of the issuer will be complete once the assets being offered are transferred to the purchasers (as would

51. See HMRC’s International Tax Manual, paragraph INTM153150.
typically be the case in the context of exchange token offerings), whereas in other offerings the issuer will remain subject to future obligations owed to the purchaser, such as the obligation to perform certain future services (as would typically be the case in the context of utility token offerings).

HMRC’s guidance does not confirm how these offerings would be treated for tax purposes. As a result, the particular facts and circumstances, including the applicable contractual terms, would need to be analysed on a case-by-case basis. As part of this process, taxpayers may, for example, need to consider:

- Whether the offering involves a taxable disposal by the issuer (see sections 1.1.2(b) and (c) above). This could be the case if the offering involves either (i) the transfer of existing assets or (ii) the creation of new assets (e.g. the tokens) and their on-sale to subscribers (rather than the mere issuance of new assets to subscribers without any transfer).
- If there is a disposal:
  - What, as a legal matter, is being disposed of? This could, for example, be the token itself, the bundle of contractual rights to which the purchaser of the token is entitled or a right to an interest in underlying assets (as could perhaps be the case with certain security token offerings).
  - Whether the disposal constitutes the disposal of a capital asset or the disposal of a non-capital asset, such as a trading asset. This may depend, for example, on whether the issuance is a standalone issuance, or one of a series (such that the issuer could potentially be said to be trading in the tokens). If the offering involves the disposal of an interest in an underlying asset, the tax treatment would depend on the characterisation of the underlying asset, and the tax rules applicable to its transfer.
- The applicable accounting treatment. This would be particularly relevant where the assets being offered are within the scope of the special tax regimes mentioned above (e.g. the intangible fixed assets regime), such that their tax treatment is generally determined by reference to debits and credits recognized in the taxpayer’s (GAAP-compliant) profit and loss statement. For example, an offering which subjects the issuer to future obligations (such as certain utility token or security token offerings) could conceivably (depending on the circumstances and the applicable accounting treatment) give rise to the recognition of a liability in the issuer’s profit and loss statement.
1.1.3 Other Taxes

(a) What are the value added tax/sales tax consequences of selling crypto assets?

In *Hedqvist*, the ECJ held that the VAT exemption at Article 135(1)(e) of the VAT Directive, which broadly applies to transactions concerning legal tender, can apply to transactions in bitcoin (provided that bitcoins are accepted by the parties as a means of payment and are not used by the parties for other purposes). HMRC therefore takes the position that when exchange tokens are exchanged for goods and services, no VAT is due on the supply of the exchange token itself. However, this does not mean that the supply of the goods or services paid for in crypto assets would be exempt. Supplies subject to VAT which are paid for in exchange tokens would attract VAT in the normal way - with the consideration subject to VAT being the value of the exchange tokens, in pounds sterling, on the date the transaction takes place.

As a result of the above finding, the court in *Hedqvist* held that the service of exchanging bitcoin constituted an exempt supply under Article 135(1)(e). In the UK, HMRC has extended this slightly, by confirming that ‘a supply of any services required to exchange tokens for legal tender (or other exchange tokens) and vice versa, would be exempt’ (emphasis added). In a similar vein, arranging transactions in exchange tokens will be exempt from VAT, provided, broadly, that the arranger is acting in an intermediary capacity (i.e., bringing together someone seeking an exchange token service with someone providing that service).

HMRC has also confirmed that the receipt of bitcoin and similar exchange tokens in consideration for mining activities falls outside the scope of VAT, on the basis that (i) the activity does not constitute an economic activity for VAT purposes, because there is an insufficient link between any services provided and any consideration and (ii) there is no customer for the mining service.

HMRC does, however, note that the treatment set out in their guidance is ‘provisional pending further developments; in particular in respect of the regulatory and EU VAT positions’. This may perhaps indicate that, even after the end of the Brexit transitional period, the UK intends to keep step with the EU regarding the VAT treatment of transactions involving exchange tokens.

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52. See supra n. 4.
55. Under Item 1 of Group 5 of Schedule 9 to the Value Added Tax Act 1994, which applies to ‘the issue, transfer, receipt of, or any dealing with, money, any security for money or any note or order for the payment of money’.
56. Under Item 5 of Group 5 in Schedule 9 to the UK Value Added Tax Act 1994, which applies to ‘the provision of intermediary services in relation to any transaction comprised in (amongst other categories) item 1 ... (whether or not any such transaction is finally concluded) by a person acting in an intermediary category’.
57. See HMRC’s VAT Finance Manual, paragraph VATFIN7200.
As mentioned above, HMRC’s guidance covers neither (i) the VAT treatment of utility tokens or service tokens nor (ii) ICOs, IEOs and STOs. As with direct taxes, the treatment will likely turn on the relevant contractual terms and circumstances, and what exactly is being provided between the parties. Matters which may need to be considered include:

- Whether the offering could be considered to involve the provision of goods or services subject to VAT.
- If so, whether an exemption from VAT may apply. For example, depending on the circumstances, it is conceivable that certain offerings could perhaps benefit from exemptions applying to the provision of certain financial services,\(^{58}\) such as the UK VAT exemption applying to ‘the issue, transfer or receipt of, or any dealing with, money, any security for money or any note or order for the payment of money’.\(^{59}\)
- If VAT is payable, when it may be required to be accounted for. It may be necessary to consider, for example, whether subscription for a token could be characterized as a prepayment for the future delivery of goods or services subject to VAT (as could perhaps be the case for certain offerings of utility tokens). If so, the ‘tax point’, triggering the obligation to account for the relevant VAT to a tax authority, may be accelerated.\(^{60}\)

(b) Are payments in crypto assets subject to withholding taxes?

In the UK, the payment of normal company dividends does not attract withholding tax. However, subject to certain exemptions, payments which do attract withholding tax include (i) payments of UK source interest on debts intended to remain outstanding for one year or more;\(^{61}\) (ii) certain ‘annual payments’ made by non-individuals pursuant to contractual obligations, which are income, and ‘pure profit’, in the hands of the recipient\(^{62}\) and (iii) certain royalty payments.\(^{63}\)

HMRC has not made any statement regarding the withholding tax position if such payments are made in crypto assets, and in particular in exchange tokens. However, it is reasonable to assume that the same withholding tax principles would apply, notwithstanding that payment was made in ‘money’s worth’ rather than cash. For the purposes of calculating the amount to be withheld and accounted for to HMRC, it seems likely that HMRC would consider that the amount paid would be the value of the crypto assets, in pounds sterling, on the date of payment.

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59. In light of HMRC’s view that exchange tokens do not constitute money, this particular exemption is unlikely to be available for exchange token offerings.
The UK tax code contains specific rules where, broadly, payments subject to withholding tax are satisfied through the issuance of bonds. These rules require a certain portion of the bonds to be withheld, and enable the person withholding to satisfy its obligation to account to HMRC by transferring the bonds to HMRC. In the absence of equivalent rules to accommodate crypto assets, it should be assumed that HMRC would require the obligation to account to be satisfied in cash.

(c) Does payment of compensation in crypto assets give rise to payroll tax consequences?

Please see section 1.1.2(e) above.

(d) Do transactions with crypto assets trigger any transfer taxes?

UK stamp duty applies on transfers of stock or marketable securities (and interests in partnerships holding stock or marketable securities). UK stamp duty reserve tax (SDRT) applies to agreements to transfer ‘chargeable securities’ (which is, broadly, defined similarly). HMRC considers it unlikely that exchange tokens currently existing would constitute either stock or marketable securities, or chargeable securities. If that is the case, transactions in exchange tokens themselves should not be subject to such transfer taxes. However, HMRC has noted that this would need to be considered on a case-by-case basis, by reference to the characteristics and nature of the particular exchange token. Unsurprisingly, transactions in exchange tokens themselves will not be subject to UK stamp duty land tax (which broadly applies to transfers of interests in UK land).

However, transactions where exchange tokens are given in consideration for stock or marketable securities, chargeable securities, or interests in UK land, would need to be considered separately. When calculating a stamp duty charge, HMRC has stated that exchange tokens given in consideration for stock or marketable securities will not be counted as part of the consideration subject to stamp duty, as they do not fall under the meaning of ‘money’, ‘stock or marketable securities’, or ‘debt’ for stamp duty purposes. The transfer may therefore escape charge entirely (depending on whether any other ‘stampable consideration’ is given). In contrast, for SDRT and stamp duty land tax, any consideration in the form of ‘money’s worth’ will be subject to charge. This will include exchange tokens (with the charge calculated by reference to their value, in pounds sterling, on the date of the transaction).

HMRC has not considered in its published guidance to date the stamp duty, SDRT or stamp duty land tax implications of transfers of (or agreements to transfer) other crypto assets such as utility tokens or security tokens. Care would need to be taken, in

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particular, regarding the transfer of security tokens granting interests in, or rights over, stock or marketable securities, chargeable securities or UK land.

\[(e) \] Are firms operating in the crypto space subject to digital service taxes?

A new UK digital services tax took effect from 1 April 2020.\(^{68}\) The tax applies to online search engines, social media platforms, and online marketplaces. Transactions in crypto assets, and those providing services in respect thereof, should not therefore generally be within scope. In any event, the charge only applies to businesses generating global annual revenue of more than GBP 500 million from such activities (in circumstances where at least GBP 25 million of such revenue derives from UK users). These thresholds are unlikely to be exceeded by crypto businesses.

\[(f) \] Are crypto assets subject to gift, inheritance, estate, or wealth taxes?

The UK does not have wealth taxes. However UK inheritance tax may apply to the estate of a deceased person, certain lifetime gifts and certain trust arrangements.\(^{69}\) Subject to certain exceptions, these taxes will mainly be of relevance to individuals.

In some circumstances, assets outside the UK may escape charge (e.g., if the individual is not domiciled in the UK).\(^{70}\) However, HMRC’s position is that (i) exchange tokens are assets for this purpose and (ii) subject to the terms of any relevant double tax treaty,\(^{71}\) their situs is wherever the holder is resident. Inheritance tax cannot, therefore, be circumvented by investing in assets on a non-UK exchange.

Broadly, inheritance tax only applies to the assets of a person’s estate if the value of the estate (excluding assets which will pass to the person’s spouse, civil partner or charities) exceeds GBP 325,000.\(^{72}\) Any excess is subject to tax at a rate of 40%.

For inheritance tax purposes, lifetime gifts do not generally attract a charge at the time of transfer. However, the value of gifts made in the last three years prior to death will count towards the GBP 325,000 threshold mentioned above (as will a proportion of the value of gifts made in the last four years prior to that). Certain lifetime gifts constitute ‘exempt gifts’, including any gifts to a spouse or charity, gifts out of income, and any gifts of less than GBP 250.\(^{73}\) In addition, each person has an annual allowance of GBP 3,000.

\(^{68}\) Part 2 of the Finance Act 2020.

\(^{69}\) Where assets are placed in a discretionary trust, or a trust subject to a contingency, a charge of up to 6% will apply when the assets are removed from the trust, or if later, on each ten-year anniversary of the trust (see further Part 3 of Chapter 1 of the Inheritance Tax Act 1984). Depending on the circumstances, these provisions may capture commercial trust and escrow arrangements.

\(^{70}\) Section 6(1) of the Inheritance Tax Act 1984.

\(^{71}\) The UK has double tax treaties covering inheritance tax with the Republic of Ireland, the Netherlands, France, Sweden, Italy, Switzerland, India, Pakistan, South African and the US.

\(^{72}\) Sections 4 and 7–9 of the Inheritance Tax Act 1984. This limit can be increased to GBP 500,000 (for the 2020–2021 tax year) if the assets include the deceased’s home, which is to pass to his/her children or grandchildren.

Lifetime gifts of crypto assets which are capital assets may also give rise to a capital gains tax charge. This is because such gifted assets will generally be treated as having been disposed of for their market value.74 Exemptions apply for gifts to spouses and civil partners75 and gifts to charities.76 Relief from the charge may also be available for gifts of capital assets which are business assets.77

A gift of crypto assets which constitute trading assets or intangible fixed assets would not generally give rise to a tax charge, as it would not be expected to generate a credit in the donor’s profit and loss statement.78 Subject to the fulfillment of certain conditions, a donation of crypto assets which are trading assets to charity may in fact generate tax relief capable of being offset against taxable profits.79 Equivalent relief would not be available in respect of a gift of crypto assets which are intangible fixed assets.

(g) Are crypto assets subject to exit tax?

UK exit charges apply where (i) a company ceases to be resident in the UK or (ii) a non-resident company ceases to carry on a trade in the UK through a permanent establishment. Broadly, the intent is to bring certain unrealized profits or gains into the charge to tax.

Exit charges apply in respect of (among other categories of assets) the company’s capital assets, trading stock and intangible fixed assets. The exit charge would, therefore, apply to any crypto assets held by the taxpayer. How the charge is calculated will vary slightly as between the relevant assets. Broadly, the effect will be to bring into the charge to tax (i) any difference between the base cost of capital assets and their market value;80 (ii) the market value of closing trading stock;81 and (iii) the difference between the carrying value and market value of intangible fixed assets.82 Subject to certain conditions, the payment of the exit charge can be deferred, and paid in instalments.83 At the end of the Brexit transactional period, these deferment provisions (which derive from EU law)84 will be retained, unless specifically repealed or amended.

77. Gift holdover relief effectively allows the recipient to take over the donor’s capital gains tax position in respect of the asset, without a charge arising for the donor (see further section 165 of the Taxation of Chargeable Gains Act 1992).
78. However, where the gift is to a related party, transfer pricing rules may be in point, and (for intangible fixed assets) a market value override would apply in calculating the profit on realization (as to which, see sections 845–849 of the Corporation Tax Act 2009).
79. Gift holdover relief effectively allows the recipient to take over the donor’s capital gains tax position in respect of the asset, without a charge arising for the donor (see further section 165 of the Taxation of Chargeable Gains Act 1992).
82. Schedule 3ZB to the Taxes Management Act 1970.
83. EU Council Directive (EU) 2016/1164 laying down rules against tax avoidance practices that directly affect the functioning of the internal market (known as ATAD).
by the legislature. The British government has not given any indication that it intends to do so.

Exit charges do not apply to any other category of taxpayer.

(h) Can mining trigger gambling tax?

In the UK, any rewards from gambling activities are not subject to tax. HMRC has not made any statement as to whether mining activities may constitute gambling. However, in light of HMRC’s statement that investment in exchange tokens would not be characterized as gambling, it seems unlikely that HMRC would be willing to adopt a different approach for mining.

1.1.4 Compliance and Documentation Obligations

(a) What documentation requirements exist for taxpayers regarding crypto assets and are there best practices in recordkeeping to support representations made in tax returns?

There are no legislative documentation requirements specific to crypto assets. The overriding obligation on taxpayers is to keep records (in hard copy or digital form) sufficient to support the position taken in their tax returns. How long the records must be kept for varies as between different categories of taxpayer. Generally, for any tax return:

- relating to income or gains:
  - of individuals not carrying on a business, it is 22 months from the end of the period to which the return relates;
  - of individuals trading (or in partnership), it is five years from 31 January following the end of the period to which the return relates; and
- of companies, it is six years from the end of the accounting period to which the return relates;
- relating to VAT, it is six years from the end of the relevant reporting period; and
- relating to employee income tax withholding (so-called ‘Pay As You Earn’ or ‘PAYE’ withholding) and employee and employer national insurance contributions, it is three years from the end of the relevant reporting period.

85. See ‘Cryptoassets: tax for individuals’, referred to in supra n. 1.
Breach of these obligations will generally result in a fine of up to GBP 3,000, and more practically, may impact the amount of tax ultimately payable if the taxpayer’s position in the return cannot be substantiated.

For individuals, HMRC has, however, provided guidance regarding record keeping obligations in the context of transactions in exchange tokens. The guidance notes that crypto asset exchanges may only keep records for a limited period of time or may no longer be in existence by the time a person is required to submit their tax return to HMRC. It therefore stresses that the onus is on the taxpayer to keep records of each crypto asset transaction, and that these must include ‘(a) the type of crypto asset; (b) the date of the transaction; (c) whether the assets were bought or sold; (d) the number of units [subject to the transaction]; (e) the value of the transaction in pounds sterling; (f) the cumulative total of investment units held; and (g) bank statement and wallet addresses’.

In addition, guidance applying to both individuals and businesses specifies that for capital gains tax purposes, individuals and businesses must keep records of the ‘allowable cost’ for any pool (see further section 1.1.2(b) above).

Noting the requirement that profits, gains and losses must generally be reported to HMRC in pounds sterling, and that many crypto asset exchanges do not use pounds sterling, HMRC has confirmed the following:

- for transactions which do not have a value in pounds sterling (e.g. where one kind of exchange token is exchanged for another), an appropriate exchange rate must be established to convert the transaction into pounds sterling;
- reasonable care should be taken to arrive at an appropriate valuation for transactions using a consistent methodology; and
- records should be kept of such valuation methodology.

(b) What is the evidentiary burden of supporting tax positions when a digital wallet address is lost or shared with other persons?

As discussed above, for capital gains tax purposes, where an exchange token is lost (e.g. because the key to the wallet in which the token is held has been lost), taxpayers may be able to make a negligible value claim. The claim will need to state (i) the asset which is the subject of the claim, (ii) the amount for which the asset should be treated as disposed of (which may be GBP 0) and (iii) the date that the asset should be treated as disposed of. Appropriate valuations may have to be agreed with HMRC.\(^7\)

When, as a result of such loss, the taxpayer submits a tax return claiming a deductible expense in respect of trading or intangible fixed assets, or makes a negligible value claim in respect of capital assets, the burden of proof is no different than that which applies to any other return in which such expense or relief is claimed; the burden of proof falls on the taxpayer to establish that the conditions for the deduction or relief have been met. The applicable standard of proof is the balance of probabilities.

\(^7\) See HMRC’s Capital Gains Tax Manual, paragraph CG13120P onwards.
(c) Are crypto asset exchanges and wallet providers subject to reporting obligations?

Crypto asset exchanges and wallet providers are not subject to any specific obligation to report information regarding their customers to HMRC. However, HMRC has powers to compel the provision of information relating to UK taxpayers from exchanges and wallet providers (see section 1.1.4(a) for individual taxpayers recordkeeping obligations).

If such exchanges and providers are themselves within the scope of UK tax, standard reporting obligations applicable to UK taxpayers would apply.

(d) Are taxpayers holding crypto assets subject to reporting obligations apart from the filing of income tax/capital gains tax returns?

UK taxpayers holding crypto assets would not be subject to any particular additional filing obligations.

If a UK taxpayer is merely holding crypto assets, this would not generally have to be reported in tax returns until the holding of, or transactions in, such assets had an impact on the amount of capital gains/losses or income/expenses to be reported in such returns.

Similarly, if exchange tokens were (i) used to pay for goods or services subject to VAT, (ii) given in consideration for an acquisition of an interest in UK land subject to stamp duty land tax, or (iii) given as employment remuneration, then the usual reporting obligations relevant to such transactions would apply (irrespective of the form of payment).

(e) Are crypto asset exchanges and wallet providers subject to CRS/FATCA reporting?

Broadly, pursuant to FATCA/CRS reporting requirements, ‘financial institutions’ (being ‘investment entities’, ‘depositary institutions’ and ‘custodial institutions’) are required to conduct due diligence on certain customers who have ‘financial accounts’ with them, and report on the same to tax authorities. The information reported is then automatically exchanged between tax authorities.

HMRC has not given any indication as to its views on whether crypto exchanges or wallet providers would constitute financial institutions for the purposes of CRS/FATCA reporting. As a result, the particular services offered by a crypto asset exchange or wallet provider, and the nature of the crypto assets in respect of which such services are provided, would need to be analysed on case-by-case basis.

88. See the International Tax Compliance Regulations 2015 (as amended) (SI 2015/878).
1.1.5 Civil and Criminal Tax Enforcement

(a) What powers do the tax authorities have to compel the disclosure of information by third parties, such as exchanges or wallet providers, and have these been used in the past?

HMRC can compel third parties to provide information and documents about UK taxpayers if such information is ‘reasonably required for the purpose of checking the taxpayer’s tax position’.\textsuperscript{89} Such obligation is limited to information or documents in the ‘possession or power’ of the third party.\textsuperscript{90} However, HMRC’s requests need not be limited to specific documents, and can require third parties to create new documents. In the absence of consent from the relevant taxpayer, HMRC would need judicial approval to make such a ‘third-party request’.\textsuperscript{91} Broadly, for approval to be granted, the relevant tribunal must be satisfied that HMRC has reasonable grounds for making the request. Third parties who do not comply can be subject to daily penalties and in some cases, tax-based penalties.

Indeed, it has been reported that HMRC has sent such third-party notices to certain crypto asset exchanges.\textsuperscript{92} In response to a freedom of information request from a crypto asset publication, HMRC is reported to have said that ‘These exchanges can retain information on their clients and the transactions that they have completed. These transactions may result in potential tax charges and HMRC has the power to issue notices requiring exchanges to provide this information.’

(b) What measures have the tax authorities undertaken in the past to ensure crypto tax compliance?

HMRC has published guidance (described above) clarifying how certain existing UK tax laws apply to exchange tokens. Beyond that, it is not known what (if any) additional steps HMRC has taken to ensure crypto tax compliance.

As mentioned above, it has been reported that HMRC has asked cryptocurrency exchanges, including Coinbase, CEX.IO, and eToro, for details about their customers’ transaction history.\textsuperscript{93} However, this has not been confirmed, because HMRC is generally subject to privacy obligations regarding steps taken in respect of specific taxpayers.\textsuperscript{94} Although HMRC does have the power to publish information regarding deliberate tax defaulters,\textsuperscript{95} it is not possible to ascertain, from the details published, whether any such defaults relate to the holding of, or transactions in, crypto assets.

\textsuperscript{89}. See paragraph 2 of Schedule 36 of the Finance Act 2008.
\textsuperscript{90}. See paragraph 18 of Schedule 36 of the Finance Act 2008.
\textsuperscript{91}. See paragraph 3 of Schedule 36 of the Finance Act 2008.
\textsuperscript{93}. Ibid., coindesk.com.
\textsuperscript{94}. See section 19 of the Commissioners for Revenue and Customs Act 2005 and HMRC’s Compliance Handbook, paragraph CH207323.
\textsuperscript{95}. See section 94 of the Finance Act 2009.
More generally, if HMRC was to introduce specific measures targeting cryptocurrency compliance, this would typically be preceded by a public consultation. In this respect, nothing has been announced to date. However, a 2018 report from the ‘Cryptoassets Taskforce’ of HM Treasury, the UK Financial Conduct Authority and the Bank of England notes that ‘both [HM Treasury and HMRC] recognise the risks of tax avoidance and evasion arising from the increased use of crypto assets and are continuing to review the range of enforcement tools and approaches at HMRC’s disposal.’

(c) Are the tax authorities cooperating with tax authorities in other jurisdictions on enforcement?

In order to ensure compliance by taxpayers holding crypto assets, HMRC has a number of means available to request information from abroad (e.g., from foreign tax authorities in respect of crypto asset exchanges and other providers of services in respect of crypto assets located outside the UK):

- Over 100 of the double tax treaties to which the UK is party contain (an equivalent of) Article 26 of the OECD Model Convention, providing for the exchange of information between contracting states’ competent authorities.
- The UK is party to a number of bilateral ‘Tax Information Exchange Agreements’ with certain jurisdictions with which the UK does not have a tax treaty, including Bermuda, BVI, Guernsey, Jersey and the Isle of Man.
- The UK has, together with 136 other jurisdictions, signed up to the OECD Convention on Mutual Administrative Assistance in Tax Matters, which facilitates the exchange of information between signatory states.

Broadly, for HMRC to request information pursuant to the above instruments, the information would need to be foreseeably relevant to the administration and enforcement of the UK’s laws concerning the taxes covered therein.

In addition, during the Brexit transitional period, the UK has remained subject to, and benefitted from, the rights and obligations of EU Member States regarding the collection and exchange of certain information which may be relevant from a tax perspective. Specifically, as with other EU Member States, the UK has been required to: (a) collect, and automatically exchange, information regarding beneficial ownership collected pursuant to anti-money laundering processes and (b) implement legislation requiring information regarding certain cross-border arrangements (including, but not limited to, those with a main benefit of obtaining an EU tax advantage) to be

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reported to, and exchanged between, the tax authorities of EU Member States.\textsuperscript{98} Once the transitional period has ended, the UK’s obligations to collect this information, and provide it to EU Member States, will be retained as part of domestic UK law, unless expressly repealed by the UK Government. It is not yet clear whether EU Member States will grant the UK reciprocal access to such information they have collected. Nevertheless, information could still be requested from EU Member States under the multilateral and bilateral agreements mentioned above.

It is not publicly known whether HMRC has exercised its powers under the above instruments to seek information regarding UK taxpayer’s holdings of crypto assets, and if so, whether HMRC has been successful in gaining access to such information.

\textsuperscript{98} The International Tax Enforcement (Disclosable Arrangements) Regulations 2020 (25/2020). Originally, such information would have been reported to HMRC from Jul. 2020 and exchanged between the tax authorities of EU Member States from 31 Oct. 2020. However, in light of the COVID-19 pandemic, certain Member States, including the UK, agreed to defer the dates for first reporting, and first exchanges between tax authorities, by six months.