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IBA Annual Conference – Tax Implications of Cryptocurrency & Blockchain

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Regulatory Environment

- Some jurisdictions have taken steps to restrict the cryptocurrency market – E.g., China, Iran
- Others permit cryptocurrency markets to operate with varying degrees of regulatory oversight
- Focus has mostly been limited to ICOs and cryptocurrency exchanges in the context of AML/CFT regulations
- Cryptocurrency regulation guidelines by International Financial Action Task Force on AML/CFT supported by G20



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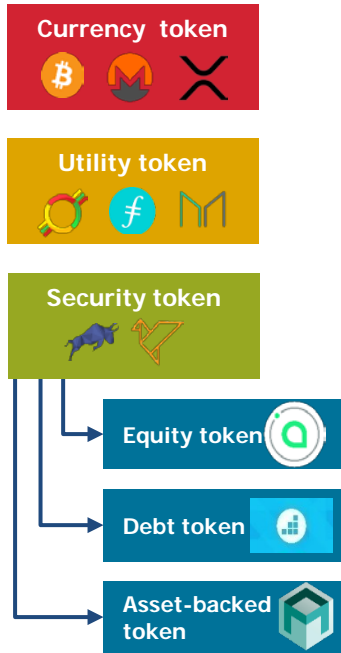


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Tax Implications of Cryptocurrency and Blockchain – Token classification

Regulatory



Tax / GAAP

Business assets	Aspects
Fixed asset	Intangible assets Participations
Current asset	Currencies Receivables Right of use
Equity	Shares Other Equity
Debt	Loan
Private assets	Aspects
Investment	Short term or long term
Trade	



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Cryptocurrencies - Uses of Crypto

Uses	Activities
<p>Payments</p> <ul style="list-style-type: none"> • salary, bonus; employee benefits (e.g. phantom stock building) • for goods & services • royalties • interest, dividends, derivative benefits • rent 	<p>Supplies</p> <ul style="list-style-type: none"> • work • sales • IP / licensing • capital • surrender of use
<p>Products digitalization & sales</p> <ul style="list-style-type: none"> • smart contracts application • tokens for specific applications • vouchers 	<p>Procurement</p> <ul style="list-style-type: none"> • of goods and services vs. spending of crypto
<p>Raising capital</p> <ul style="list-style-type: none"> • debt instruments / borrowing • ICOs (derivative benefits concepts) • share issues • charities 	<p>Financing</p> <ul style="list-style-type: none"> • lending • growth & project funding • equity funding • donations



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Uses	Activities
<p><i>Exposure transfers & value storing</i></p> <ul style="list-style-type: none"> • equity / debt linked tokens • asset backed currencies (e.g. gold coin) • basket-linked tokens • insurance linked tokens • exchange & hedging • crypto investment funds 	<p><i>Investment / speculation</i></p> <ul style="list-style-type: none"> • capital markets • precious metals • commodities • underwriting risk • trading
<p><i>Crypto-specific</i></p> <ul style="list-style-type: none"> • crypto ATMs & exchanges • rewards for contributions to the community • air drops 	<p><i>Crypto-specific</i></p> <ul style="list-style-type: none"> • exchange • mining / staking; forks



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Tax Authorities Concerns

Summary of Concerns

- Characteristics of cryptocurrency that lead to tax authorities' concerns
- Underreporting
- Tax evasion
- Non-tax crimes



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Tax Authorities Concerns

Characteristics of Cryptocurrency

- Characteristics of cryptocurrency that lead to tax authorities' concerns:
 - Anonymous/Pseudonymous – Each transaction is recorded on the blockchain, but data is not directly linked to identifying information.
 - Peer-to-peer payment system makes it easy to conduct cross-border transactions with no exchange rate fees and no regulatory oversight.
 - Acceptable mode of payment in criminal transactions.
 - According to 2015 Europol report, bitcoin was used in over 40% of illicit transactions in the European Union.



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Tax Authorities Concerns

Underreporting

- Taxing authorities believe there is significant underreporting of gains related to cryptocurrency transactions.
 - E.g., US Internal Revenue Service claims only 802 people declared a capital gain or loss related to bitcoin in 2015, but Coinbase summons yielded more than 13,000 transactional records exceeding \$20,000.
- Tax information reporting.
 - Reporting by intermediaries – E.g., cryptocurrency exchanges, payment processors, ATM network providers.
 - Transactional reporting.
 - Aggregate proceeds reporting.
 - Reporting by account holders – E.g., reporting foreign bank accounts and foreign investments.
 - Automatic exchange of information.



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Tax Authorities Concerns

Underreporting

- Tax audits
 - Some jurisdictions are actively auditing cryptocurrency transactions – E.g., Canada Revenue Agency has added standard cryptocurrency audit questions; US Internal Revenue Service announced compliance campaign and began sending out letters.
 - Tools at tax authorities' disposal.
 - Summons authority – E.g., Coinbase summons in US.
 - Third-party tracing companies – E.g., Chainalysis.
 - Criminal investigations/raids - E.g., Korea, Japan.



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Tax Authorities Concerns

Tax Evasion – Enforcement Efforts

- International coordination
 - Joint Chiefs of Global Tax Enforcement (known as the J5) – targets transnational tax crime through increased enforcement collaboration.
 - Comprises the Australian Criminal Intelligence Commission and Australian Taxation Office, the Canada Revenue Agency, the Netherlands Fiscale Inlichtingen- en Opsporingsdienst, UK HM Revenue & Customs, and US Internal Revenue Service Criminal Investigation.
 - Conducting at least 50 joint investigations.
- Regulations creating greater government oversight – E.g., banning anonymous transactions, KYC/AML rules, and best practices for cryptocurrency.



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Tax Authorities Concerns

Non-tax Crimes

- Non-tax crimes
 - E.g., money laundering, terrorist financing, scam ICO's, pump and dump schemes, Ponzi schemes, fraud, and hacking/theft.
 - Enforcement examples – FBI's shut-down of Silk Road; Europol's shut-down of Bestmixer.io.
 - Some countries have banned the use of cryptocurrency entirely or its use for payment – E.g., China, Russia, Vietnam, Bolivia, Columbia, Ecuador.
 - Some countries have banned ICOs – E.g., China, Korea.



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Tax Issues Relating to Cryptocurrencies

Status of the Law

- No specific tax legislation enacted in any jurisdiction so far
- Tax authorities' guidance or published opinions on certain issues exist in many jurisdictions
- Some published court decisions on cryptocurrency taxation also exist
 - E.g. CJEU's VAT case Hedqvist (C-264/14)



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Tax Issues Relating to Cryptocurrencies

Type of Income

- Income characterization of realized value increase
 - Ordinary income?
 - Capital gain?
 - Exempted income?
- Asset type characterization for income tax purposes
 - Property?
 - Intangible asset?
 - Currency?
 - Security?
 - Commodity?
 - Financial instrument?
 - Inventory?
- Do same principles apply to both corporations and individuals?



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Tax Issues Relating to Cryptocurrencies

Amount/Timing of Income

- Timing of taxation
 - Obligation to mark to market at the end of year?
 - Taxation only when realized (sold/exchanged/used as payment etc.)?
- Amount of the income
 - Acquisition cost computation (LIFO, FIFO, or average)?
 - Value fluctuation in the same day?
 - Monetary value of a utility token?
- Loss/deduction treatment
 - Business activity
 - Private investment activity
 - Theft or fraud
 - Foreign exchange gains/losses



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Tax Issues Relating to Cryptocurrencies

Income Tax Treatment of Particular Uses

- Investment activity
 - Is cryptocurrency trading taxed as an (active) business/trading or (passive) investment/ordinary/capital income?
 - Taxation of conversion to different cryptocurrencies vs. FIAT currency?
- Taxation of acquisition of goods and services?
- Loans of cryptocurrency
 - Taxable sale or exchange of loaned cryptocurrency?
 - Treatment of interest payments?



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Tax Issues Relating to Cryptocurrencies

Special Cryptocurrency Tax Issues

- Forks
 - Is any income realized?
 - Allocation of acquisition cost?
 - Any difference on the treatment of hard or soft forks?
- Mining
 - Tax treatment of mining rewards (proof of work/stake) and transaction processing fees?
 - PE treatment of foreign mining operations?



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Tax Issues Relating to Cryptocurrencies Token Offerings/ICOs

- Tax treatment of issuers and investors?
 - Does it depend on the characterization of the tokens?
 - Asset class—property/intangible/inventory/foreign currency/security/financial instrument?
 - Functionality—equity/debt/prepaid good or service/utility (access)?
 - Taxable events—e.g., issuance/receipt of tokens, spending/receipt of tokens, conversion of tokens?
- Structuring issues
 - Domestically vs. off-shore?
 - Transfer pricing issues?
- Pre-sales of tokens – Simple Agreement for Future Tokens (SAFTs)



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Tax Issues Relating to Cryptocurrencies

Other Types of Taxes

- VAT / GST / Sales tax
 - Are cryptocurrency transactions subject to tax?
 - Conversions?
 - Sale and purchase of cryptocurrencies?
 - Using cryptocurrencies as means of payment when buying goods and services?
 - Are utility tokens:
 - Vouchers of specific goods or services or
 - Vouchers of certain value to exchanged for a number of goods and services?
- Withholding tax
 - Cryptocurrencies paid as salary, interest, dividends?
 - Tokens?



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Tax Issues Relating to Cryptocurrencies

Other Types of Taxes

- Inheritance and Gifts
 - What is possible inheritance or gift tax base if cryptocurrencies are inherited or donated?
 - Is there a taxable event?
 - Originator's acquisition cost?
 - Fair market value at death/donation moment?
 - Is value increase of the originator taxed?
- Wealth tax
 - Is cryptocurrency subject to any net wealth tax?
- Other taxes
 - Digital Services Tax?
 - Financial transaction tax?
 - Stamp duty?



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Tax Issues Relating to Cryptocurrencies

Accounting and Recordkeeping

- Is there any guidance on the accounting treatment of cryptocurrencies?
- In what way does the treatment differ from tax accounting?
- Is the taxpayer obligated to keep record of all of the transactions for tax reporting purposes?
 - Problems with access to the information?



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Future

- Where are we in 5 years?
- What is the future for cryptocurrencies and their taxation?

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