

Chapter 4

Tax treatment of digital currencies

4.1 On 20 August 2014, the ATO published a suite of draft public rulings expressing its preliminary view of the tax treatment of digital currency, specifically Bitcoin. The ATO's rulings were drafted after representatives of the digital currency industry asked the ATO to publish its position on the tax treatment of Bitcoin. The ATO called for public comment on the draft rulings, which closed on 3 October 2014.¹

4.2 In this chapter, the committee considers the tax arrangements for digital currencies and whether there is a need to make changes. The digital currency industry's primary concern regarding the ATO's rulings related to the GST treatment of digital currencies.

The Australian Taxation Office's rulings

4.3 The ATO's final public rulings on digital currency were published on 17 December 2014. The ATO advised the committee that while the final rulings provided additional information and clarification, there was not any material change between the draft and final rulings.² Details of the ATO's rulings were outlined in Chapter 2.

4.4 In its submission, the ATO explained that its guidance was based on an impartial consideration of existing law and 'issues associated with potential consumer risk, tax compliance risk, administrative difficulty, and potential criminal use were not determinative in settling the ATO's view'.³ The ATO explained that it had no role in determining whether digital currencies should or should not be treated as 'money' or 'currency', rather such decisions were a matter for government.⁴ At the public hearing on 4 March 2015, Mr Michael Hardy, ATO, explained:

The tax office came to this issue with the approach that bitcoin transactions are happening and we need to provide some certainty for the community about what the tax treatment is with the tools we have available to us under the existing law. So the approach we took was to understand the technology, understand the business models, see if the existing law could or did apply and then to provide the advice. We took the approach of being as collaborative as possible. We worked with experts, industry associations—banking, finance, tax—and accounting professionals as well.⁵

1 Australian Taxation Office, *Submission 8*, pp. 3–4.

2 Mr Michael Hardy, Australian Taxation Office, *Committee Hansard*, 4 March 2015, p. 15.

3 Australian Taxation Office, *Submission 8*, p. 4.

4 Australian Taxation Office, *Submission 8*, p. 5.

5 Mr Michael Hardy, Australian Taxation Office, *Committee Hansard*, 4 March 2015, p. 15.

4.5 Mr Hardy noted that the feedback the ATO had received from the business community was not necessarily in full agreement with the ATO's advice on the operation of the existing law, however, there was an appreciation for the degree of certainty the ATO had provided.⁶ Bitcoin Group, an Australian based Bitcoin company, for example, advised the committee that while it did not agree with the ATO's ruling on GST, its 'ambitions would have been more difficult to realise without the regulatory clarity provided through the ATO's digital currency tax guidances'.⁷

4.6 One submitter noted that while the tax treatment for digital currency had been unclear prior to the ATO rulings, 'it was nonetheless obvious to most participants that normal taxation rules applied. That is, tax must be paid on any profits made, either through general income tax arrangements or as capital-gains tax on Bitcoin investments'.⁸

Goods and services tax

4.7 The Bitcoin Foundation and Bitcoin Association of Australia confirmed that the GST treatment of Bitcoin was their main concern. They noted that by treating Bitcoin transactions as barter transactions, GST can effectively be applied twice to one transaction; GST would be applied to the goods or services being provided, in addition to the 'supply' of the digital currency used as payment.⁹

4.8 The ATO acknowledged that double taxation issues were a feature of barter transactions, but they were not very common or visible until the development of digital currencies. The ATO noted that:

...this particular issue of how bitcoin might be charged twice in a barter environment became a perhaps more prominent question. So that is nothing new and nothing confined just to bitcoin. As to whether that is a good or a bad thing, that is really a policy question...¹⁰

4.9 Mr Andrew Sommer, Clayton Utz, noted that the domestic tax treatment was the critical issue for digital currency businesses, stating:

Where GST or VAT is imposed on the acquisition of bitcoins as part of a trading transaction, it makes it much more difficult and much less economically viable for me to take my Australian dollars and convert them into bitcoin if one-eleventh of that transaction is going to be lost in GST at the point that I do that. For everyday consumers, that one-eleventh cost is a real cost. That is a consequence of treating bitcoin like a commodity rather than a currency.¹¹

6 Mr Michael Hardy, Australian Taxation Office, *Committee Hansard*, 4 March 2015, p. 15.

7 Bitcoin Group Limited, *Submission 38*, p. [4].

8 Name withheld, *Submission 11*, p. [2].

9 Bitcoin Foundation and Bitcoin Association of Australia, *Submission 13*, p. 19.

10 Mr Michael Hardy, Australian Taxation Office, *Committee Hansard*, 4 March 2015, p. 16.

11 Mr Andrew Sommer, Clayton Utz, *Committee Hansard*, 26 November, 2014, p. 10.

4.10 BitAwareAustralia, a non-profit organisation that promotes the practical advantages of digital currency, emphasised that the Bitcoin community was not looking for a 'free ride', or to use the currencies as a tax haven. It noted that for the most part, the Bitcoin community accepted their obligation to pay capital gains tax on any investment profits, and it was happy to pay GST on goods or services purchased using Bitcoin. However, the community's 'only point of contention to the ATO's ruling is to our industry being rendered uncompetitive because of additional GST levied over and above our fiat-based competitors and international Bitcoin-based competitors'.¹²

4.11 The Melbourne Bitcoin Technology Center argued that 'removing the double taxation of Bitcoin is required to support start-ups develop and capture a share of the emerging economic advantage of digital currency in this country'.¹³

4.12 The committee heard of the negative effect the GST ruling had already had on some businesses. One submitter observed that:

...Australian technology firms have or are planning to shift overseas. Operations, such as my own, have either shut down or significantly curtailed their activities. This is a very disappointing personal outcome for all the Australians involved, to see their efforts invalidated through no shortcoming of their own.¹⁴

4.13 CoinJar, an Australian digital finance start-up, noted that the ATO's GST ruling had rendered it 'uncompetitive against non-Australian rivals'.¹⁵ Mr Guzowski, ABA Technology, observed that applying GST to digital currency 'puts additional friction on transactions and it completely sets it apart from other types of currency and does not make it practical to purchase locally. So...it has sent a lot of businesses offshore. It is putting a brake on the industry, for sure'.¹⁶

4.14 Mr Antonopoulos argued that the decision to apply GST to digital currency 'fundamentally misunderstands the nature of the system, ascribing it the properties of a commodity, which it is not, and as a result having significant friction. That may be a major disadvantage for Australian Bitcoin companies'.¹⁷

4.15 Professor Miranda Stewart and Mr Joel Emery from the Tax and Transfer Policy Institute, Australian National University considered that the current GST treatment 'poorly reflects digital currencies' practical purpose'.¹⁸ Professor Stewart and

12 BitAwareAustralia, *Submission 17*, p. 15; Bitcoin Group Limited was concerned that capital gains tax treatment, as well as the GST treatment of digital currency, had slowed domestic adoption of the technology, *Submission 38*, p. [3].

13 Melbourne Bitcoin Technology Center, *Submission 36*, p. [2].

14 Name withheld, *Submission 11*, p. [2].

15 CoinJar, *Submission 12*, p. 8.

16 Mr Christopher Guzowski, ABA Technology, *Committee Hansard*, 26 November 2014, p. 23.

17 Mr Andreas Antonopoulos, *Committee Hansard*, 4 March 2015, p. 4.

18 Professor Miranda Stewart and Mr Joel Emery, The Tax and Transfer Policy Institute, Australian National University, *Submission 23*, p. 12.

Mr Emery noted that the UK's VAT ruling had created a 'jurisdiction with a relatively favourable tax regime to which intermediaries may relocate if the Australian regulatory framework is considered unfavourable'.¹⁹ In the UK, digital currencies are exempt from VAT. They suggested that a similar exemption to the application of the GST in Australia 'would promote simplicity and neutrality, as it treats sales using digital currency as payment largely the same as sales using traditional cash'.²⁰

4.16 The Institute of Public Affairs shared the views expressed by Bitcoin businesses that imposing a GST on Bitcoin and other digital currencies could stifle the development of this technology. It argued that treating digital currencies in the same way as fiat currencies would 'enable the continuing development of non-state forms of currency'.²¹

GST and different currency exchange services

4.17 There has also been some uncertainty surrounding the way GST is applied to different types of digital currency exchange services within Australia.

4.18 The ATO explained the way in which different business models for exchanging digital currency such as Bitcoin may attract different tax outcomes. For example:

- A principal or direct sales model of exchange: where Bitcoin is held in its own right, the business would need to charge GST on the supply of Bitcoin, as it is being bought or sold directly by the exchange.
- An agency type model of exchange: operating like a brokerage arrangement, where the exchange does not hold Bitcoin, but charges a fee to facilitate the purchase of Bitcoin between a buyer and seller. The business would not be required to charge GST on the supply of Bitcoin as it is being supplied through an introduction service. There may be GST on the transaction fee, but not the total Bitcoin transaction volume.²²

4.19 Mr Guzowski, ABA Technology, explained that his company's business model means they do not sell Bitcoin, but facilitate the purchase of Bitcoin from overseas vendors. He charges GST on the fee for providing the service, but not on the Bitcoin itself.²³

4.20 BitAwareAustralia noted that the principal or direct sales type model proved the 'most trouble-free way to trade bitcoins'. However, the added expense of GST being charged on the total purchase had turned a lot of users away from these sites.

19 Professor Miranda Stewart and Mr Joel Emery, The Tax and Transfer Policy Institute, Australian National University, *Submission 23*, p. 13.

20 Professor Miranda Stewart and Mr Joel Emery, The Tax and Transfer Policy Institute, Australian National University, *Submission 23*, p. 13.

21 Institute of Public Affairs, *Submission 10*, p. 6.

22 Mr Michael Hardy, Australian Taxation Office, *Committee Hansard*, 4 March 2015, p. 16.

23 Mr Christopher Guzowski, ABA Technology, *Committee Hansard*, 26 November 2014, p. 23.

BitAwareAustralia noted that some direct Bitcoin sales sites have closed down in the wake of the ATO's ruling on Bitcoin.²⁴

4.21 Bit Trade Australia is an exchange which holds Bitcoin and buys and sells directly to its customers. According to Bit Trade Australia the GST ruling has:

...increased the cost of the service we are providing to customers because they not only have to pay for our service provision, which is the supply of a spot contract, but we also have to levy GST on the good itself. So compared to, say for example, purchasing bitcoin from another provider based in another jurisdiction, the cost of our service provision to the customer is 10 per cent more. A lot of Australian businesses have left the jurisdiction to set up in other markets because they found it impossible to survive with the costs levied. The net effect has been the shutdown of some businesses and reduction in volume and trade in this jurisdiction, and we have experienced drops in trade and volume.²⁵

Committee view

4.22 The committee considers that the most immediate concern for Australian digital currency businesses is the current GST treatment of digital currencies. Proposed legislative changes to address these concerns are discussed later in this chapter.

Definitions of digital currencies for tax purposes

4.23 The ATO's role in developing its guidance for digital currencies was to interpret the way in which digital currency fits within the current tax legislation.

Definition of money in the GST Act

4.24 The current definition of 'money' in the *A New Tax System (Goods and Services Tax) Act 1999* (the GST Act) includes:

- (a) currency (whether of Australia or of any other country); and
- (b) promissory notes and bills of exchange; and
- (c) any negotiable instrument used or circulated, or intended for use or circulation, as currency (whether of Australia or of any other country); and
- (d) postal notes and money orders; and
- (e) whatever is supplied as payment by way of:
 - (i) credit card or debit card; or
 - (ii) crediting or debiting an account; or
 - (iii) creation or transfer of a debt.

However, it does not include:

24 BitAwareAustralia, *Submission 17*, p. 8.

25 Mr Jonathon Miller, Bit Trade Australia, *Committee Hansard*, 7 April 2015, p. 12.

- (f) a collector's piece; or
- (g) an investment article; or
- (h) an item of numismatic interest; or
- (i) currency the market value of which exceeds its stated value as legal tender in the country of issue.²⁶

4.25 Mr Sommer, Clayton Utz, noted that he and others had made submissions to the ATO's consultation process to advise that an argument could be made that the definition of money, as it currently exists in the GST Act, could be extended to include digital currency. He stated:

One of the great things about tax law is that you can always argue both sides. In relation to this particular issue, there are two or three key definitions: there is money, currency and foreign currency. In relation to the GST law, the key definition for most of this will be the definition of money. That definition is an 'includes' definition. There is an argument to be made that the definition of money as it sits in section 1951 of the GST Act is capable, on its current terms, of extending to bitcoin.²⁷

4.26 The ATO confirmed that it had considered these arguments when making its determination.²⁸ Ms Preston noted that it was the ATO's role to interpret the law and that Treasury was satisfied with the way the ATO had dealt with digital currency.²⁹ As noted earlier, the ATO has stated that the question of whether digital currencies should be treated as 'money' or 'currency' was a matter for government.³⁰

Proposed changes to the definitions of 'money' and 'financial supplies'

4.27 The ATO advised the committee that in order to treat digital currencies as money for the purposes of GST would require changes to the definitions of 'money' and the 'financial supplies'. It advised that changing the definition of 'money' to include digital currencies would require a legislative change to the GST Act.³¹

4.28 The ATO noted the definition of 'financial supplies' is set out at regulation 40-5.09 of the *A New Tax System (Goods and Services Tax) Regulations 1999* (GST Regulations). Any change to this definition could be achieved by amendment to the GST Regulations, and would not require legislative change.³²

26 *A New Tax System (Goods and Services Tax) Act 1999* - Sect 195.1.

27 Mr Andrew Sommer, Clayton Utz, *Committee Hansard*, 26 November 2014, p. 11. See also Adroit Lawyers, *Submission 39*, p. 5.

28 Australian Taxation Office, *Submission 8*, p. 5.

29 Ms Kate Preston, Treasury, *Committee Hansard*, 4 March 2015, p. 17.

30 Australian Taxation Office, *Submission 8*, p. 5.

31 Answers to questions on notice from a public hearing held in Canberra on 4 March 2015, received from the Australian Taxation Office on 19 March 2015, p. [3].

32 Answers to questions on notice from a public hearing held in Canberra on 4 March 2015, received from the Australian Taxation Office on 19 March 2015, p. [3].

4.29 However, if the definition of 'financial supplies' were changed in the GST Regulations without also changing the definition of 'money' in the GST Act, there may be additional complexity and compliance costs for some businesses. The ATO explained:

This would make the supply of cryptocurrency input taxed. To the extent a business made acquisitions relating to the supply of Bitcoin (e.g. payments to a relevant point of sale provider) it would be blocked from claiming related input tax credits. This would not apply to businesses that are below the 'financial acquisitions threshold': see Division 189 of the Act.³³

4.30 An alternative approach would be to create specific exemptions or special rules, rather the definitions of 'money' and 'financial supplies'. However, the ATO's preliminary view is that such alternative approaches would require a change to the GST Act.³⁴

4.31 The ATO concluded that if the intention were to treat digital currency like money for GST purposes, the most straight forward approach would be to amend the definition of 'money' in the GST Act to this effect, in addition to defining digital currency as a financial supply in the GST Regulations to cater for exchange transactions.³⁵

4.32 Both the Treasury and the ATO noted that any change to the GST Act would require agreement by the states and territories.³⁶ The ATO stated:

The GST is levied by the Commonwealth, but the revenue from the GST is distributed to the states and territories. This arrangement is set out in the Intergovernmental Agreement on Federal Financial Relations...Clause A14 provides that any proposal to vary the GST base will require the unanimous support of the States and Territory Governments, the endorsement by the Commonwealth Government and the passage [of] relevant legislation by both Houses of the Commonwealth Parliament. The requirement for unanimous agreement by the states and territories is legislated in Section 11 of the *A New Tax System (Managing the GST Rate and Base) Act 1999*. The 'base' of the GST refers to the range of goods and services to which the GST applies.³⁷

33 Answers to questions on notice from a public hearing held in Canberra on 4 March 2015, received from the Australian Taxation Office on 19 March 2015, p. [3].

34 Answers to questions on notice from a public hearing held in Canberra on 4 March 2015, received from the Australian Taxation Office on 19 March 2015, p. [3].

35 Answers to questions on notice from a public hearing held in Canberra on 4 March 2015, received from the Australian Taxation Office on 19 March 2015, p. [3].

36 Ms Kate Preston, Treasury, *Committee Hansard*, 4 March 2015, pp. 17–18; Answers to questions on notice from a public hearing held in Canberra on 4 March 2015, received from the Australian Taxation Office on 19 March 2015, p. [3].

37 Answers to questions on notice from a public hearing held in Canberra on 4 March 2015, received from the Australian Taxation Office on 19 March 2015, pp. [3–4].

4.33 Ms Preston, Treasury, noted that while it was unlikely that the states and territories would treat this as an issue of major concern, they would need to be consulted on any proposed changes to the GST Act.³⁸

Committee view

4.34 The committee considers that digital currency transactions should be treated in the same manner as national or foreign currency for the purposes of the GST. The current treatment of digital currency transactions as barter transactions, creates a double taxation effect that has placed an additional burden on Australian digital currency businesses. The committee received evidence from the ATO advising that amendments to both the legislation and regulations would be necessary in order to change the current GST treatment of digital currencies.

Recommendation 1

4.35 The committee is of the view that digital currency should be treated as money for the purposes of the goods and services tax. As such, the committee recommends that the government consults with the states and territories to consider amending the definition of money in the *A New Tax System (Goods and Services Tax) Act 1999* and including digital currency in the definition of financial supply in *A New Tax System (Goods and Services Tax) Regulations 1999*.

Other taxation concerns

4.36 Although there was general agreement that digital currencies should be exempt from GST, there was some disagreement in relation to other taxation concerns. Differing views were expressed in relation to whether digital currencies should be treated in the same way as foreign currencies for the purposes of income tax, fringe benefits tax (FBT) and capital gains tax (CGT).

4.37 Some submitters disagreed with the ATO's interpretation of the existing tax law, arguing that there was scope within the legislation to define digital currencies as foreign currencies, rather than as commodities.³⁹ The Tax Institute claimed that the existing tax law defines currency and money in broad enough terms to include Bitcoin, noting that the Income Tax Act defines foreign currency to be 'currency other than Australian currency', and pointing out that if a foreign country decided to adopt Bitcoin as legal tender, a situation would arise whereby Bitcoin would fall within the meaning of 'currency of a foreign country' and 'currency other than Australian currency'. It explained:

Bitcoin would then automatically be required to be recognised as foreign currency for income tax and GST purposes, and money for FBT purposes. It is anomalous that such a situation could arise independently and outside the control of the Australian legislature or government bodies.⁴⁰

38 Ms Kate Preston, Treasury, *Committee Hansard*, 4 March 2015, pp. 17–18

39 See for example: Taxpayers Australia Limited, *Submission 9*, pp. [2]–[6]; Name withheld, *Submission 11*, pp. [2]–[3].

40 The Tax Institute, *Submission 16*, p. 3.

4.38 A number of submitters raised concerns about the ATO's ruling that digital currencies should be treated as property, rather than money, in relation to paying wages and salaries and the application of FBT. The Bitcoin Foundation and Bitcoin Association of Australia were aware of a number of international businesses that have started paying their employees in Bitcoin. Australian businesses subject to FBT would face a further barrier when competing for global talent.⁴¹ The Tax Institute proposed a legislative change to clarify that salary and wages paid in digital currency is not a fringe benefit for tax purposes. Taxpayers Australia also raised concerns about the FBT regime applying to digital currency and expressed the view that 'further consideration of the degree of integration into the PAYG withholding system, the superannuation and other employment tax obligation regimes will need to be made in respect of digital currencies'.⁴²

4.39 The Australian Digital Currency Commerce Association (ADCCA), a group representing the Australian digital currency industry, argued that the definition of currency in both the Income Tax Act and the GST Act should be expanded to include digital currency. It noted that:

...including a definition of Digital Currency, and classifying it in the same way as foreign currency in Australian tax law will ensure that the use of Digital Currency as a method of payment alongside fiat currency is not rendered obsolete before it has had a chance to enter the mainstream payment system and be tested by the market.⁴³

4.40 Similarly, Mr Sommer, Clayton Utz, stated:

I think the best solution across the board is to introduce a new concept of 'digital currency' and include that within the concepts of currency. That would then flow through into the definition of money, and you would solve the problem that way. But we could include a new concept of 'digital currency' to that end.⁴⁴

4.41 Alternatively, Professor Stewart and Mr Emery from Tax and Transfer Policy Institute disagreed with the view that digital currencies should be treated as foreign currencies for the purposes of income tax, fringe benefits tax and capital gains tax. In their view:

It is unlikely that characterising digital currencies as money under the income tax regime would be particularly beneficial for users in respect of the application of ordinary income, capital gains tax and foreign currency rules. Indeed, treating digital currencies as foreign money under the income tax regime may add unnecessary complexity, with no gain for the ATO and digital currency users. This [is] because foreign currency is generally treated as a form of capital asset leading to CGT or income tax

41 Bitcoin Foundation and Bitcoin Association of Australia, *Submission 13*, p. 19.

42 Taxpayers Australia, *Submission 9*, p. [5].

43 Australian Digital Currency Commerce Association, *Submission 15*, p. 14.

44 Mr Andrew Sommer, Clayton Utz, *Committee Hansard*, 26 November, 2014, p. 12.

consequences in any event under the income tax law. The consequences of disposing of digital currency for foreign currency, and disposing of a commodity, are broadly similar.⁴⁵

4.42 Professor Stewart and Mr Emery did not consider that there was any clear policy basis for characterising digital currencies as money for income tax purposes at this point in time. Instead, they argued that further research and analysis were necessary before making any amendments to the income tax law in this regard.⁴⁶

4.43 Ms Kate Preston advised that Treasury was monitoring digital currencies, noting that:

[Treasury] will continue to assess the environment, but I would stress that it is an industry in its infancy. So I think that it is a little bit early in the process to jump in and suggest that there should be changes to the tax law to accommodate it.⁴⁷

Committee view

4.44 In the committee's view, further research and analysis should be conducted into whether digital currency should be treated in the same manner as foreign currencies for the purposes of income tax and fringe benefits. As noted in chapter 2, the Australian government is currently examining Australia's taxation system as part of the taxation white paper process.

Recommendation 2

4.45 The committee recommends that further examination of appropriate tax treatment of digital currencies should be included in the taxation white paper process, with particular regard to income tax and fringe benefits tax.

45 Professor Miranda Stewart and Mr Joel Emery, The Tax and Transfer Policy Institute, Australian National University, *Submission 23*, p. 15.

46 Professor Miranda Stewart and Mr Joel Emery, The Tax and Transfer Policy Institute, Australian National University, *Submission 23*, p. 15.

47 Ms Kate Preston, Treasury, *Committee Hansard*, 4 March 2015, p. 17.