

## OECD releases report on taxing virtual currencies

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### Executive summary

The Organisation for Economic Co-operation and Development (OECD)/G20 [Inclusive Framework on Base Erosion and Profit Shifting](#) (BEPS), on 12 October 2020, released a report ([the Report](#)) on taxing virtual currencies that provides a cross-jurisdictional overview of the tax treatment and emerging tax policy issues in relation to virtual currencies. The jurisdictional overview is based on a questionnaire to identify domestic variations in taxation of crypto-assets, focusing in particular on the treatment of virtual currencies for purposes of income tax, property tax and Value Added Tax (VAT).

The Report was presented to the meeting of G20 Finance Ministers and Central Bank Governors<sup>1</sup> and covers three main areas:

1. Key concepts and definitions of blockchain and crypto-assets, looking at the characterization, legality and valuation of virtual currencies and analyzing the tax consequences across the different stages of their lifecycle, from creation to disposal.
2. Tax policy implications of several emerging issues related to the taxation of virtual currencies, including the rise of stablecoins (e.g., Libra, Tether) and "Central Bank Digital Currencies" (CBDC), as well as the evolution of the consensus mechanisms used to maintain blockchain networks (e.g., the increasing use of Proof-of-Stake rather than Proof-of-Work) and the rise of decentralized finance (DeFi).

3. Identification of key tax policy considerations based on a comparative overview across more than 50 countries<sup>2</sup> of the tax treatment of virtual currencies from the perspective of income, consumption and property taxation. These policy considerations are not intended as recommendations or best practices, but rather are observations that domestic legislators and policymakers may take into consideration when strengthening their regulatory framework for taxing virtual currencies.

The Report was discussed during the Tax Talks [webcast](#) that the OECD held on the same date to update stakeholders on the latest developments in the OECD's tax work.

## Detailed discussion

On 12 October 2020, the OECD released the Report on taxing virtual currencies, which was prepared with the participation of over 50 jurisdictions. According to the Report, this is the first comprehensive analysis of the approaches and policy gaps across the main tax types (income, consumption and property taxes) for such a large group of countries. It also considers the tax implications of a number of emerging issues, including the growing interest in stablecoins and CBDC's, as well the evolution of the consensus mechanisms used to maintain blockchain networks and the dawn of decentralized finance.

The Report is divided into four sections:

- Section 1: Introduction and key concepts
- Section 2: Key tax policy considerations and overview of country treatments
- Section 3: Common tax policy challenges and emerging issues
- Section 4: Conclusions and considerations for policymakers

### Key concepts and definitions

As the Report states, there is no uniform definition of the various features of crypto-assets. The common features, however, are related to financial assets based on distributed ledger technology (e.g., blockchain) and cryptography as an inherent part of the perceived value of the assets. The Financial Action Task Force (FATF) defines a "virtual asset" as "a digital representation of value that can be digitally traded or transferred and can be used for payment or investment purposes." (Financial Action Task Force, 2019).

Regardless of a common definition, a three-part subdivision of crypto-assets has broadly been identified: (i) payment tokens, (ii) utility tokens, and (iii) security tokens (Global Digital Finance, 2019; European Banking Authority, 2019). They are defined as follows:

- (i) Payment tokens represent an asset that can be used for exchange of goods and services. Payment tokens are commonly referred to as virtual currencies.
- (ii) Utility tokens are primarily used for access to certain services or infrastructure, where the tokens can represent pre-payments, vouchers or licensing of specific rights.
- (iii) Security tokens are tradable in nature and are often held for investment purposes.

There are varieties within these three categories, in addition to the fact that some tokens may have "hybrid" features covering more than one category. Tokens also may change over time due to their multi-layered nature, similar to multi-layered derivatives contracts. However, virtual currencies or payment tokens are the tokens that are mainly addressed in the jurisdictions covered by the Report. By contrast, less guidance is currently provided by policymakers on utility and security tokens. Typically, it is expected that these types of tokens follow the same treatment as payment tokens, although specific difference and nuances may arise based on the nature and features of these tokens.

### Overview of tax treatment of virtual currencies

The comparative overview in the Report focuses on the extent to which virtual currencies are subject to income tax, property tax and/or VAT for consumption purposes. The differences in regulatory approaches highlight the need for policymakers to balance competing goals and perspectives in order to safeguard a coherent and robust regulatory regime for virtual currencies. For the time being, domestic differences create a tension where regulatory arbitrage may take place without sufficient disclosure mechanisms in place.

The following is a summary of key take-aways from the Report on the domestic tax treatment of virtual currencies related to (i) income tax, (ii) property tax and (iii) VAT.

#### Income tax

Almost all countries that provided input to the questionnaire confirmed that virtual currencies are to be considered as a form of property, and most often as intangible assets other

than goodwill. Income tax is common upon disposal or exchange of a virtual currency, although some jurisdictions allow individuals to exchange virtual currencies for fiat currency without the transaction representing a taxable event. Further, exchange of virtual currencies for services, goods or wages typically qualifies as a taxable event.

There can be differences in the tax treatment of transactions in virtual currencies depending on the status of the parties involved. For instance, occasional traders may be subject to capital gains tax, which can be reduced by losses. Companies that are trading virtual currencies as part of their business generate business or capital income or losses, which will be subject to business tax or potentially give rise to deductions.

### Property tax

Virtual currencies qualify as property for tax purposes in most jurisdictions covered in the Report, subjecting the value of virtual currencies to inheritance, gift, wealth taxes in countries where these taxes exist. There can be different property taxation for resident and nonresident companies, which affects the tax rate or method of calculation. In some countries, such as Switzerland, there is a regime under which virtual currencies must be converted to Swiss francs for tax assessments, provided by the Federal Tax Administration (FTA).

Transfers of virtual currencies typically are not subject to transfer taxes due to the definition of the assets that trigger such taxation. However, this is likely to change over time.

### VAT

The trading and handling of virtual currencies, including the creation process of mining, may all have VAT consequences. Generally, the VAT treatment of virtual currencies is more consistent than the income tax treatment. The main reason for this seems to be a European Court of Justice case from 22 October 2015, *Skatteverket v Hedqvist* (C-264-14), which ruled that transactions, including the exchange of fiat currency for virtual currencies and vice versa, are exempt from VAT. Hence, most European Union (EU) countries have a joint consensus that the exchange to or from virtual currencies is not subject to VAT. The same applies for using virtual currencies to buy goods or services. Thus, no VAT should be charged on the use of virtual currencies itself. However, on the opposite side of the same transaction, the supply of taxable goods and services that is paid for with virtual currencies is considered subject to VAT.

Most countries, with exceptions for countries like France and Italy, consider the act of receiving new virtual currencies that have been mined, as a VAT-liable event. Further, not all types of virtual currency services are treated consistently among EU Member States or other countries. Online wallet services and virtual currency exchanges are two examples of services that are treated differently in different countries.

### Overview of policy considerations

While the Report does not make recommendations, it does provide a number of general insights that policymakers may consider in the taxation of virtual currencies:

1. **Policymakers may ensure that their country has clear guidance and a clear legislative framework, for example by:**
  - Providing guidance on how virtual currencies fit within the existing framework and determining if and to what extent existing laws are unclear or not adapted to virtual currencies given their special characteristics (e.g., price volatility, hybrid nature, type and number of transactions, creation protocols). Similarly, providing a definition of virtual currencies for tax purposes may be helpful.
  - Addressing comprehensive guidance on major taxable events and forms of income associated with virtual currencies (e.g., income taxes, VAT, property or transfer taxes). Major taxable events may include the creation of virtual currencies (via mining/forging, initial token offerings (ITOs) and airdrops), exchange with other virtual currencies, with fiat currency, and for goods and services (including valuation), disposal via gift or inheritance, loss or theft, emerging developments (hard forks,<sup>3</sup> stablecoins, CBDC, interest-bearing tokens) and related services (e.g., exchange services and wallets).
  - Providing guidance that indicates how other forms of crypto-assets (including security and utility tokens) are to be treated for tax purposes. Official guidance on the boundaries between different types of crypto-assets, and on how other forms of these assets are treated for tax purposes, could be useful.
  - Frequently reviewing and adapting guidance to ensure that it remains relevant in the face of technological and market developments related to virtual currencies and other emerging asset-types. It may also be helpful to take stock of approaches adopted in other countries and any emerging international trends.

2. **Policymakers may consider communicating the rationale behind the adopted tax treatment.** Given the fast-changing nature of these assets, stating the rationale behind the classification adopted for tax purposes could enable the tax treatment to be more transparent and more flexible should a new form of virtual currency emerge.
3. **Policymakers may consider the consistency between the taxation of virtual currencies and the taxation of other assets in order to ensure tax system neutrality.**
4. **Policymakers may facilitate a coherent regulatory framework for virtual currencies including the tax treatment.** It is of importance for policymakers that policy aspects such as tax transparency and legal, financial and consumer protection work together and not stand as competing interests.
5. **Policymakers may consider how to support improved compliance in terms of disclosure and taxation of virtual currencies.** This is particularly challenging due to volatility, various exchange rates for the same virtual currency, lack of a one-to-one relation between value of virtual currencies and fiat currency and keeping records of transactions. All these challenges make it difficult for tax administrations to obtain reliable and timely information on the value of virtual currency transactions. Hence, policymakers may consider whether intermediaries such as crypto exchanges and custodians of private keys could be included in a broader disclosure regime for tax purposes.
6. **Policymakers may consider the extent to which occasional or non-professional small traders can be subject to a relaxed or simplified taxation regime.** In this context, policymakers may consider whether a simplified tax regime can exempt capital gains tax for completed transactions and rather impose tax on a basis similar to foreign currency or alternatively provide a "de minimis exception" for small traders.
7. **Policymakers may consider how the tax treatment of virtual currencies aligns with or undermines other policy objectives.** For example, a decline in cash use has led some governments to look at how to support electronic payments, including development of CBDCs.

Environmental challenges towards energy aspects with regards to the costly computing power required to generate and mine virtual currencies may also be taken into consideration to determine the tax treatment of virtual currencies.

### Overview of future regulatory challenges, e.g., Stablecoins, CBDC and DeFi

The Report also reviews some trends and emerging developments within the field of virtual currencies where policymakers may want to pay particular attention to the tax treatment. Areas where separate or updated guidance may be needed are:

1. **The tax treatment of new assets received when a hard fork occurs has only been addressed by a handful of countries.** One of the main challenges is when the taxpayer is deemed to have received the assets for tax purposes. Exercise of dominion and time of first disposal can be considered against a basis of zero. In addition, the receipt of new tokens can raise liquidity issues for the taxpayer based on the timing of when the tokens can be accessed. In addition, volatility issues such as how losses are to be treated if the value of the token falls after it is received and taxed may be considered.
2. **Stablecoins and CBDCs represent new forms of virtual currencies. These new asset types have unique characteristics that tax policymakers may consider further and more specifically.** Stablecoins and CBDCs are often backed by other assets or fiat currencies. Their specific characteristics can be key for tax purposes, and policy makers may want to consider whether existing rules are appropriate.
3. **Other new token types and characteristics are also emerging.** However, almost no countries have issued tax treatment guidance for new token types such as proof of stake generated tokens or use of virtual currencies as an interest-bearing asset. There are similarities with traditional capital or financial assets that may be relevant. Hence, consideration could be given to whether tax treatment akin to capital income is more appropriate than capital gains income. Tax guidance on such issues could provide certainty for taxpayers and prevent tax planning opportunities.

## Implications

The Report is the first formal report of the OECD and its Inclusive Framework on BEPS that is specific to taxing virtual currencies and the related emerging tax policy issues. Although the Report does not explicitly contain recommendations, it is expected that the OECD will do more work on this topic. As such, the Report should be viewed as a first important step towards more clarity and guidance on several areas in relation to virtual currencies where policymakers currently face challenges. It is expected that policymakers in several Inclusive Framework member countries will follow the Report's suggestions on providing more guidance on these issues, which will benefit all stakeholders with respect to virtual currencies.

Also, the Report states that the OECD is currently developing technical proposals in order to ensure an adequate and effective level of reporting and exchange of information with respect to crypto-assets. It is not yet clear what these technical proposals will entail. Similar to the increasing

regulatory requirements that are being proposed and implemented by the OECD for Virtual Asset Service Providers (VASPs), it may be that additional measures will be proposed to improve tax transparency. This may include what information tax administrations need to know about transactions for purposes of compliance and enforcement. Such measures may also include applying the Common Reporting Standard (CRS) to VASPs so that information about holders of virtual currencies can be automatically exchanged with tax authorities to combat tax evasion.

Additional guidance and rules and regulations are necessary in the rapidly changing world of virtual currencies, in particular now that national central banks and the European Central Bank are considering the development of their own virtual currencies. The Report has taken a first step in laying the groundwork for policy developments and greater convergence on a regional or global level. While these developments are particularly important for financial institutions and fintech businesses, there may be implications for taxpayers in all sectors.

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## Endnotes

1. See EY Global Tax Alert, [G20 Finance Ministers and Central Bank Governors' meeting communiqué extends mandate of Inclusive Framework to continue negotiations on BEPS 2.0 project until mid-2021](#), dated 14 October 2020.
2. Responses were received from Andorra, Argentina, Australia, Austria, Belgium, Brazil, Bulgaria, Canada, Chile, Colombia, Costa Rica, Cote d'Ivoire, Croatia, Czech Republic, Denmark, Estonia, Finland, France, Georgia, Germany, Greece, Grenada, Hong Kong (China), India, Indonesia, Ireland, Israel, Italy, Japan, Korea, Latvia, Lithuania, Luxembourg, Malaysia, Malta, Mexico, the Netherlands, New Zealand, Norway, Peru, Poland, Portugal, Saint Lucia, Singapore, Slovak Republic, Slovenia, South Africa, Spain, Sweden, Switzerland, Turkey, the United Kingdom, and the United States. These countries are collectively referred to in the report as the "respondent Countries."
3. A "hard fork" is a backward-incompatible update to a blockchain network. A hard fork can occur when the nodes in the blockchain add new rules in a way that conflicts with old rules. The new nodes will then only communicate with the other nodes that operate the new version. Hence, the blockchain splits and creates two separate networks of old and new rules.

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