

Briefing document

HMRC cryptoassets business guidance

Introduction

HMRC have published guidance for businesses that undertake transactions involving exchange tokens. Exchange tokens are a subset of cryptoassets that are used as a means of exchange, so includes cryptocurrencies like bitcoin. This note sets out a high-level overview of the key points of interest in HMRC's guidance.

Taxpayers within the scope of the guidance

The guidance is intended for use by any type of entity conducting a business involving exchange tokens, including companies, partnerships and sole traders. The publication of the guidance for businesses follows the December 2018 publication of guidance for individuals. The business guidance is similar to the guidance for individuals in many respects, though goes into more detail in certain areas. Given that the position of individuals was the topic of the previous guidance, this note focuses on the position of companies.

HMRC's approach

The UK Government has not introduced legislation that applies specific tax laws to cryptocurrency. Instead, existing tax laws are applied. HMRC consider the facts and circumstances of each case and apply tax laws based on the substance of what has happened, as opposed to applying tax laws based on terminology.

This approach provides as much stability to the tax system as possible, since taxing based on substance as opposed to specific terminology in this fast-developing area means that the law does not need to be regularly changed to accommodate changes in terminology, specific types of coins and tokens, and transaction style.

Topics covered by HMRC's guidance

Much of HMRC's business guidance focuses on how the profits of a business should be calculated and taxed. This note focuses on the position of companies.

HMRC's guidance also considers the availability of tax reliefs under the venture capital schemes, the application of Value Added Tax (VAT), the tax and national insurance position when employees are paid in exchange tokens and the application of stamp taxes on the transfer of exchange tokens or when exchange tokens are used as a means of payment for the acquisition of other assets.

The Cryptoassets Taskforce comprised of the Bank of England, Financial Conduct Authority and HM Treasury previously categorised cryptoassets into three categories; i) exchange tokens; ii) security tokens and iii) utility tokens. HMRC have adopted the same definitions, and, at this stage, HMRC's published guidance only relates to exchange tokens.

Taxation of companies

Approach to taxation

Broadly, companies are subject to UK corporation tax if they are resident in the UK or have a permanent establishment in the UK. HMRC consider four ways in which returns from exchange tokens could be charged to UK corporation tax, which are; i) trading income, ii) loan relationships; iii) under the intangibles regime and iv) if none of the previous charging provisions apply, as capital gains or losses.

Despite the name, cryptocurrencies are not, currently, considered to be currency or money. This means that the corporate tax provisions that specifically apply to currencies are not relevant. It is possible that this position could evolve in the future should cryptocurrencies become more widely accepted as a means of exchange.

UK taxes are generally computed using sterling values. This means that the value of exchange tokens must be converted into their sterling value. If a transaction does not have a sterling value (for example, if one cryptocurrency is exchanged for another), a sterling equivalent must be established.

Trading income

Whether or not a trade is being carried on is determined by applying the 'badges of trade' to a company's activities. Various factors are assessed individually to determine whether or not a factor is indicative of a trade being carried on, and the overall assessment is determined by considering a balance of factors.

HMRC note that the factors which must be taken into account include i) degree and frequency of activity, ii) level of organisation and iii) intention (including risk and commerciality).

There are two means by which gains and losses related to exchange tokens could be included in taxable trading profits.

Firstly, a business could be conducted that relates directly to exchange tokens. HMRC provide an example in this area by considering mining activities. In HMRC's view, mining using a single home computer is unlikely to be regarded as trading, whereas mining using a bank of dedicated computers for an expected net profit (after taking account of equipment and electricity costs) is more indicative of a trade being undertaken.

The previously published guidance for individuals stated that "*Only in exceptional circumstances would HMRC expect individuals to buy and sell cryptoassets with such frequency, level of organisation and sophistication that the activity amounts to a financial trade in itself*". The business guidance therefore adds further details about when these exceptional circumstances may occur (e.g. a bank of mining computers).

The other means by which profits and losses associated with exchange tokens could be brought within the scope of taxation as trading profits is if the tokens are held as part of an existing trade. For example, where a company carrying on a trade accepts exchange tokens as payment from customers or uses them to make payments to suppliers, in which case tokens given and received will need to be accounted for within taxable trading profits.

Loan relationships

HMRC consider that it would be relatively unusual for the loan relationship rules to apply, since cryptocurrencies i) are not money and ii) do not represent a debtor-creditor relationship. An exception to this is where exchange tokens are used as collateral for an ordinary loan of money or other debt between two parties.

Intangible fixed assets

HMRC consider that exchange tokens may be taxable as intangible fixed assets where the exchange tokens represent both an intangible asset for accounting purposes and where the asset is an 'intangible fixed asset' for corporation tax purposes. This requires that the exchange token is either acquired or created for use as a long-term asset on a continuing basis. Exchange tokens which are simply held by a company will not meet this definition. There are further specific rules that apply in some circumstances.

Capital gains

If none of the income charging provisions apply, the guidance states that returns from exchange tokens are typically within the scope of the chargeable gains rules. The rules that apply to calculate and tax gains on disposals of shares and securities also apply to cryptocurrency. This means that gains and losses on disposal are calculated in a prescribed order by matching the disposal of a given type of cryptocurrency to cryptocurrency of the same type acquired:

1. On the same day.
2. Within the previous 10 days (for companies – individuals are instead subject to a rule that matches disposals to acquisitions within the following 30 days).
3. From the 'pool'. If cryptocurrency is acquired and not matched to a disposal on the same day or the previous 10 days, it enters the 'pool' for that type of cryptocurrency. Gains or losses on disposal are then, effectively, calculated using the average cost of the cryptocurrency.

Gains and losses on each type of cryptocurrency are calculated independently. For example, if a company disposes of 100 bitcoin and then buys a further 100 bitcoin on the same day, it would be treated as disposing of the bitcoin purchased on the same day. If instead the company disposed of litecoin, the disposal would not be matched to the same day acquisition of bitcoin, but instead to any acquisitions of litecoin on the same day or in the previous 10 days or, if none, from the litecoin cryptocurrency pool.

While cryptocurrency may have been subject to tax as a form of income on receipt (for example, as a profit from mining activities), exchange tokens which are retained as an investment may be within the scope of the capital gains rules on a future disposal (broadly, on the uplift in value compared to the amount that was taxable as income when the exchange tokens were first received).

HMRC also comment on the position of exchange tokens acquired due a 'hard fork' occurring, or due to an airdrop. These points are considered by HMRC in the context of their guidance on capital gains.

Broadly, a 'hard fork' occurs when new tokens come into existence as a spin-off from an existing cryptocurrency. HMRC's guidance states that the cost of the original exchange tokens (e.g. the purchase price) would need to be split between the old and new tokens on a 'just and reasonable' basis. HMRC state that they will consider any areas of difficulty as and when they arise.

Airdrops occur when a person is given new tokens, for example, as part of a marketing or advertising campaign. HMRC's guidance comments that *"...the tokens of the airdropped cryptoasset will need to go into their own pool unless the recipient already holds tokens of that cryptoasset (in which case the airdropped tokens will go into the existing pool)."*

HMRC state that the provisions that split base cost between old and new cryptocurrencies do not apply to airdropped tokens that are of a cryptocurrency not already held and so, presumably, HMRC's expectation is that such tokens will not have a base cost for capital gains purposes. Accordingly, any proceeds on disposal of airdropped tokens will be treated as a capital gain, assuming that the tokens are not of a type which has been separately acquired for consideration (e.g. such that there is no cryptocurrency pool containing acquisition costs on purchase of the same type of cryptocurrency).

In general, costs incurred in the process of acquiring or disposing of an asset can be deducted when calculating the gain on disposal; the same principle should apply to airdropped tokens.

Venture capital schemes

The venture capital schemes provide various tax reliefs for investors, and include the Enterprise Investment Scheme and Venture Capital Trusts.

HMRC note that, in order for the venture capital schemes to be available, the company must be trading. This is determined as set out in the "Taxation of companies" section above. HMRC provide various examples of activities that are related to a core business that would not, in themselves cause the venture capital schemes to be unavailable. These are:

- Providing goods and services to customers that operate in the exchange tokens sector;
- Accepting exchange tokens as payment, and;
- Using distributed ledger technology as a means of recording or publishing information.

The position is less clear for companies that deal in exchange tokens on their own account; enter into exchange token transactions or broker these for others, and that mine cryptocurrency.

Companies can apply to HMRC under the non-statutory advance assurance service to request HMRC's opinion on whether or not the venture capital scheme(s) would be available in respect of proposed investments into the company.

Value Added Tax (VAT)

HMRC state that VAT is payable in the normal way on any goods or services sold in exchange for cryptoasset exchange tokens; i.e. the VAT position does not change depending on whether cash or cryptocurrencies are used to pay for goods or services.

In terms of supplying or arranging the supply of exchange tokens, HMRC consider various circumstances and, in all of the cases considered in their guidance, conclude that the matter under consideration is either outside the scope of or exempt from VAT. This includes situations in which "traditional currencies" (i.e. legal tender such as sterling) are exchanged for non-legal tender such as bitcoin. These are classed as financial transactions and accordingly are eligible for an exemption from VAT.

HMRC do however note that the VAT position is provisional pending further developments, including any regulatory changes or European Union VAT developments that apply in the UK.

Paying employees in cryptoassets

Employees must pay income tax if they are paid in exchange tokens. The amount to be taxed will be the value of the tokens because HMRC consider that cryptocurrencies are "money's worth".

How tax is collected and the application of National Insurance Contributions (NICs) depends on whether or not the exchange tokens are "Readily Convertible Assets" (RCAs). Broadly, exchange tokens are RCAs if trading arrangements exist or are likely to come into existence, so that tokens can be converted into cash. HMRC considers that exchange tokens generally will be RCAs.

If a token is an RCA, Employer's and Employee's NICs will be payable and both the NIC and income tax the employee is due to pay must be collected from the employee's salary by the employer and paid to HMRC through Pay As Your Earn (PAYE). If there is no cash salary, the employer still has to account for the tax and NIC and pay it to HMRC. The employee must "make good" the tax the employer has paid on their behalf within 90 days of the end of the tax year in which the asset was received, otherwise additional income tax and NICs will apply.

Stamp taxes

Stamp duty and stamp duty reserve tax

Stamp duty applies to instruments that transfer stocks and marketable securities, and interests in partnerships if partnership assets include stocks or marketable securities. Stamp duty reserve tax is a related tax and is charged on agreements to transfer chargeable securities.

HMRC state that each case would need to be considered based on its specific facts and circumstances but, at the time of publication of the business guidance, HMRC does not consider that exchange tokens meet the definitions they would need to meet in order for these taxes to apply on a transfer of exchange tokens.

Stamp duty reserve tax would apply if exchange tokens are used as payment for assets within the scope of the tax, as the tax applies if payment is made in "money's worth". Tax would be due based on the sterling value of the exchange tokens.

The same is not true of stamp duty, which applies where the consideration paid for a chargeable asset is money, stock or marketable securities or debt. HMRC consider that exchange tokens are not money or debt and are generally not stock or marketable securities.

Stamp Duty Land Tax (SDLT)

SDLT is payable on purchase of land in England and Northern Ireland. Different taxes apply in Scotland and Wales.

HMRC does not consider transfers of exchange tokens to be land transactions and so SDLT does not apply to such exchanges. SDLT would apply if exchange tokens are used to settle the purchase price of the land, since SDLT applies when a purchase is made for "money or money's worth".

Find out more...

This note reflects the law in force as at 15 April 2020. It focuses on HMRC's cryptoassets guidance for businesses first published in November 2019 and also refers to HMRC's guidance for individuals published in December 2018. The guidance for businesses can be accessed at <https://deloi.tt/2NgBHxy> and for individuals at <https://deloi.tt/2WQfoC2>

Please be aware that it does not cover all aspects of this subject. To find out more about any aspect of the above, please discuss with your usual Deloitte contact. If you do not have a usual contact, please contact Michelle Robinson (michellerobinson@deloitte.co.uk).

For further information visit our website at www.deloitte.co.uk.

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