

# Briefing document

## HMRC manual on cryptoassets

### Introduction

HMRC have published their manual on cryptoassets. HMRC manuals are written for HMRC staff and set out HMRC's view of how UK taxation should apply. HMRC publish their manuals as doing so can assist taxpayers and their advisors in understanding HMRC's interpretation of the law. This note provides a high-level overview of HMRC's cryptoassets manual.

### Scope of the cryptoassets manual

The cryptoassets manual contains HMRC's explanation of what cryptoassets are and guidance for the tax position of individuals and businesses. The majority of HMRC's comments on how cryptoassets should be taxed focus on 'exchange tokens', which includes cryptocurrency.

The HMRC manual is largely drawn from the guidance for individuals that was first published in December 2018 and the guidance for businesses that was first published in November 2019.

### HMRC's approach

There are no tax laws that apply specifically to cryptoassets. Instead, existing tax laws are applied. HMRC comment that "*...the facts of each case need to be established before applying the relevant tax provisions according to what has actually taken place (rather than by reference to 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 or transaction style. HMRC comment that their views may evolve as the sector develops and they may amend their guidance or publish additional guidance as the need arises.

### Definition of cryptoassets

Cryptoassets, sometimes called "tokens", are defined by HMRC as "*cryptographically secured digital representations of value or contractual rights that can be transferred, stored and traded electronically*". HMRC state that all cryptoassets use some form of distributed ledger technology, but not all applications of distributed ledger technology involve cryptoassets.

HMRC provide a list of the main types of cryptoassets which are:

- Exchange tokens, which include cryptocurrency such as bitcoin.
- Utility tokens, which provide the holder with access to particular goods or services on a platform.
- Security tokens, which provide holders with rights or interests in a business, such as ownership, repayment of a specific sum of money or entitlement to share in future business profits.
- Stablecoins, which HMRC summarise as having a premise of minimising volatility as they may be pegged to something with a fixed value such as fiat currency (i.e. money such as pounds sterling or US dollars) or precious metals such as gold.

HMRC's manual, and the remainder of this note, focus on cryptoassets owned directly, as opposed to, say, financial instruments such as derivatives which have a value linked to the movement in price of an asset such as cryptocurrency.

Despite the name, HMRC do not consider cryptocurrency to be currency or money, and so the tax provisions that apply to currency and money do not apply to cryptocurrency. HMRC also do not consider the buying and selling of cryptoassets to be the same as gambling, which means that the tax exemptions that can apply to gambling winnings do not apply to gains or losses on disposal of cryptoassets.

## Taxation of individuals

### Approach

HMRC state that in the vast majority of cases individuals hold cryptoassets as investments, usually in the hopes of capital growth. Accordingly, UK resident individuals are generally subject to Capital Gains Tax (CGT) at a rate of up to 20% on disposal of cryptocurrency. Income tax may apply at a rate of 45% in some circumstances.

### Income tax

Income tax, and potentially national insurance contributions, may apply instead of CGT in some circumstances, including:

- When employees receive cryptoassets from their employers, in which case employment tax provisions apply.
- When cryptoassets are received from mining activities, transaction confirmations and sometimes from airdrops (see below). HMRC's view is that it would be unusual for individuals to carry on a trade in cryptoassets and so profits would be taxed as miscellaneous income. HMRC do however caveat that the analysis depends on the particular facts and so, for example, using a bank of dedicated computers to mine tokens for an expected net profit may be indicative of a trade.

If individuals retain cryptoassets that were subject to income tax on acquisition, CGT may apply on a future disposal.

In terms of buying and selling cryptocurrency, HMRC consider that only in exceptional cases would individuals buy and sell cryptocurrency with sufficient frequency, level of organisation and sophistication for this activity to amount to a financial trade. HMRC expand on their view in the business section of their guidance, and note that the factors which must be taken into account include i) degree and frequency of activity, ii) level of organisation, iii) risk and iv) commerciality.

If an individual is trading, income tax and national insurance will apply.

### Capital gains tax

HMRC consider that buying and selling cryptocurrency is normally an investment activity and so, in the absence of CGT being overridden by income tax in the aforementioned circumstances, any gains or losses on disposal are within the scope of CGT.

'Disposal' is a broad concept and, in addition to selling cryptocurrency in exchange for cash, includes exchanging one type of cryptocurrency for another, using tokens to pay for goods or services and making gifts of tokens to other people.

The same rules that apply to determine gains or losses on disposals of shares apply on disposal of cryptocurrency. The gain is equal to the disposal proceeds less the cost of the cryptocurrency. The proceeds are usually the sterling cash received, or the sterling value of the asset received in exchange for the cryptocurrency (e.g. where bitcoin is exchanged for ethereum, the sterling value of the new ethereum tokens received is treated as the proceeds for the bitcoin that has been disposed of).

The base cost is determined by applying specific ordering rules on a cryptocurrency by cryptocurrency basis to acquisitions:

1. On the same day.
2. Within the following 30 days.
3. From the 'pool', which effectively means that gains on disposal are calculated using the average cost of the cryptocurrency.

For example, if an individual buys and sells 100 bitcoin on the same day, he or she would be regarded as disposing of the bitcoin purchased on the same day. If instead litecoin was sold, the litecoin disposal would not be matched to the same day bitcoin acquisition, but instead to any acquisitions of litecoin made on the same day, in the following 30 days or, if none, from the litecoin cryptocurrency pool.

HMRC refer to some cryptoassets as 'non-fungible tokens', which means cryptoassets where only a specific identifiable token can be disposed of. Instead of the above rules applying, the capital gain or loss on disposal is calculated by comparing the proceeds on disposal to the cost of acquiring the particular asset. An example of a non-fungible token is digital artwork.

### Forks

Broadly, a 'hard fork' occurs when new tokens come into existence as a spin-off from an existing cryptocurrency. HMRC essentially treat the tokens created by the hard fork as a new cryptocurrency holding, with the result that the new tokens go into a separate pool for CGT purposes. The cost of the original cryptocurrency (e.g. the purchase price) would need to be split between the old and new tokens on a 'just and reasonable' basis in order to calculate gains and losses on future disposals.

### Airdrops

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)."

## Location of cryptoassets

HMRC comment that the location, or situs, or cryptoassets is relevant to:

- Non-UK domiciled individuals, who may be eligible to use the remittance basis while UK resident, such that foreign income and gains are only taxable if 'remitted' (brought into) the UK, and may only be subject to inheritance tax on UK situs assets.
- Taxpayers who need to disclose previously undeclared income and capital gains under the 'Requirement to Correct' legislation, in which case the offshore penalty regime can apply higher penalties to foreign income and gains.

For CGT purposes, where there is an underlying asset (e.g. where a token's value is linked to the value of a particular gold bar), the token is situated where the underlying asset is located for CGT purposes (in this example, where the gold bar is kept). Where there is no underlying asset, HMRC state that the asset's location should be determined based on the tax residence of the individual who owns the asset. This point is relevant to cryptocurrency.

No specific tax laws apply for inheritance tax purposes. Instead the location of assets for inheritance tax purposes is determined by applying the laws that generally apply to private property. The application of Double Taxation Treaties may need to be considered in some circumstances.

HMRC do not comment on the source of income arising from cryptoassets. Source is relevant to both income arising to remittance basis users, and to non-UK residents who are only subject to income tax on UK source income.

## Taxation of companies

### Guidance on taxation of businesses

HMRC's manual contains a section on businesses, which is relevant to any type of entity conducting a business involving exchange tokens, including companies, partnerships and sole traders. In terms of profits and losses, the analysis for businesses carried out in a personal capacity is as set out in the above section on individuals. This section of this note therefore focuses on the taxation of companies.

### Approach to corporate 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 as; i) trading income, ii) loan relationships; iii) under the intangibles regime, and; iv) as chargeable gains or losses.

### Trading income

HMRC's view of the likelihood of companies trading in buying and selling cryptocurrency is aligned with that for individuals, and as such HMRC consider that companies would only buy and sell exchange tokens with such frequency, level of organisation and sophistication for such sales and purchases to amount to a trade "*in exceptional circumstances*". As with individuals, the facts and circumstances of each case would need to be considered. Particular attention should be paid to mining activities.

Profits and losses from exchange tokens will need to be taken into account as trading income if tokens are held as part of an existing trade. For example, where a trading company 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 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 state 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, which means an asset which 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.

### Chargeable gains

HMRC say that the chargeable gains rules should apply where exchange tokens are held as an investment. The chargeable gains position for companies is very similar to that of individuals, including the application of share-matching rules. These are broadly the same as the rules for individuals except the "following 30 days" rule is replaced by a "previous 10 days" rule.

### Paying employees in cryptoassets

As noted above, employees must pay income tax if they are paid in exchange tokens. The amount to be taxed is the value of the tokens because HMRC consider that cryptocurrencies are "money's worth". HMRC considers that exchange tokens will generally be "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.

Accordingly, employer and employee NICs will be payable when employees are paid in exchange tokens. The employer must collect the income tax and NICs due and pay it to HMRC through Pay As Your Earn (PAYE). This applies even if an employee does not have a cash salary, in which case 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.

### **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 cryptocurrency is 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.

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.

### **Venture capital schemes**

The venture capital schemes, including the Enterprise Investment Scheme, provide tax reliefs for investors into companies. These schemes usually require that a company is trading. HMRC provides examples of some activities that are related to a core business that would not, in themselves, cause the venture capital schemes to be unavailable. These are i) providing goods and services to customers that operate in the exchange tokens sector; ii) accepting exchange tokens as payment, and; iii) 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/or that mine cryptocurrency.

HMRC caution that, if companies accept cryptocurrency as payment, relief may be unavailable due to “substantial non-trading activities” being undertaken if a high value of cryptocurrency is retained by the company as an investment.

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

### **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. In HMRC’s view, while each transfer will need to be considered individually, it is unlikely that exchange tokens would meet these definitions and so these duties are unlikely to apply to transfers 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”. The tax due would be based on the sterling value of the exchange tokens.

Stamp duty applies where the consideration for assets within its scope is paid using money, stock or marketable securities or debt. The only one of these categories that HMRC consider could encompass exchange tokens is debt, if there is a debt in the form of exchange tokens which is released or assumed on a transfer.

#### **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 on 9 April 2021 and HMRC’s cryptoassets manual as first published on 30 March 2021, which is published at <https://www.gov.uk/hmrc-internal-manuals/cryptoassets-manual>. Please be aware that this note 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](mailto:michellerobinson@deloitte.co.uk)). For further information visit our website at [www.deloitte.co.uk](http://www.deloitte.co.uk).

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