Removal of the double taxation of digital currencies

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In brief

Transactions in digital currency will no longer give rise to double taxation in the hands of consumers from 1 July 2017, as a result of legislative amendments that were recently enacted.

The amendments align the Goods and Services Tax (GST) treatment of digital currency with money. This means that supplies and acquisitions of digital currency will only fall within the scope of GST if they are supplied in exchange for 'money' or other 'digital currency'. Where this is the case, the supply of digital currency will be treated as a financial supply which is input taxed.

Whilst the necessary amendments have been made to the *A New Tax System (Goods and Services Tax) Act 1999* (GST Act), corresponding amendments to the GST Regulations are yet to be made. As a result, the Commissioner of Taxation has provided administrative relief to apply the new law from 1 July 2017 until the amendments to the GST Regulations are registered.

No changes to the income tax treatment of digital currency are proposed.

In detail

Prior to the changes, digital currency has been treated as neither 'money' nor a 'financial service' for GST purposes. As a result, both the purchase of digital currency as well as its subsequent use in exchange for goods and services could give rise to GST liabilities, thus creating 'double taxation' for consumers.

Under the new law, it is intended that digital currency will be treated in a similar way to money; albeit it will have its own stand-alone definition as opposed to being a subset of money (see below). Broadly, this means that supplies and acquisitions of digital currency will only fall within the scope of GST if they are supplied in exchange for 'money' or other 'digital currency'. Where this is the case the supply of digital currency will be treated as a financial supply which is input taxed.

GST-registered suppliers of input taxed digital currency may not be entitled to full input tax credits on things acquired to make those supplies – the usual GST apportionment rules will apply. Suppliers may be entitled to claim 75 per cent reduced input tax credits (RITCs) for specified acquisitions and the GST regulations will be amended to include arranging the supply of digital currency and transaction processing, account maintenance and report generation services provided to suppliers of digital currency as reduced credit acquisitions.

Defining digital currency

One of the more complex issues surrounds the definition of digital currency and whether it will stand the test of time, particularly given that the features of digital currency could rapidly change as a result of emerging technology and protocols.

The definition introduced by the legislative amendments is principles-based and has been modelled on the fundamental features of fiat currencies. Specifically, the definition of digital currency has been formulated to cover currencies that:

- are fungible;
- are available as consideration for a supply and available to the public for largely unrestricted use;
- are not denominated in any particular local or foreign currency;
- do not have a value based on anything else; and
- do not have a value solely or mainly because they give an entitlement to receive, or direct the supply of a particular thing or things.

This principles-based approach to the definition will be effective in capturing the current state of digital currency in Australia. However, periodic review will be crucial to ensure that this definition continues to cover the rapidly changing state of digital currencies.

Effective date and administrative treatment

The legislative amendments have a retrospective date of effect to supplies and payments made on or after 1 July 2017. Importantly, this date aligns with the effective date of the B2C changes which have the effect of imposing GST on cross-border supplies of intangibles to Australian consumers.

Whilst the amendments to the GST Act were enacted on receiving Royal Assent on 30 October 2017, the corresponding amendments to the GST Regulations are yet to be made. As a result, from 1 July 2017 until the date that the amendments to the GST Regulations are registered, the Commissioner of Taxation has confirmed that taxpayers have the option to lodge Business Activity Statements (BAS) in accordance with the current or new legislation.

Once the GST Regulations are registered, those taxpayers who continued to act in accordance with current legislation will be required to lodge requests for an amended assessment. If an amendment results in a reduction in liability, taxpayers may be entitled to receive a refund for any overpaid GST.

Where an amendment results in an increase in a liability, the Commissioner has advised that:

- Tax shortfall penalties will not apply; and
- General interest charges attributable to the shortfall will be remitted to nil for a period up until 28 days after the amending GST Regulations are registered. Taxpayers should be aware that following this period penalties and interest charges may apply.

Overall, it is expected that the administrative and compliance burden of treating digital currency in the same manner as money is expected to require few changes to existing business systems and processes.

The takeaway

The changes represent a fundamental shift for users of digital currency, and of course the platforms which facilitate that use.

The dynamic nature of digital currency will require the Government to continue to monitor these amendments to ensure that they continue to capture the current state of digital currency. However, the principles-based definition provides a strong base for the legislation to work effectively.

Taxpayers will need to observe the administrative approach adopted by the Commissioner to ensure that they are compliant when the GST Regulations are finally registered in the imminent future. Given that the administrative impact will be low, it is expected that businesses will be compliant with these new rules.

Overall, the removal of double taxation on digital currency is a positive change for Australian consumers and is likely to spark further growth of the Australian FinTech industry.

Let's talk

For a deeper discussion of how these issues might affect your business, please contact:

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