Division Head
Individuals and Indirect Tax Division
The Treasury
Langton Crescent
PARKES ACT 2600

RE: GST Treatment of Digital Currency - Discussion Paper

FinTech Australia thanks Treasury for the opportunity to submit comments on this important issue for the Australian digital currency and blockchain industry.

As we outlined in our "*Priorities for Reform of the Australian Financial Services Industry*" paper, the Goods and Services Taxation (**GST**) treatment of digital currencies has been a concern to the growing Australian digital currency sector for some time. In this regard, we are very pleased that Treasury has sought to address this issue through a consultative process.

More broadly, we believe that if a balanced regulatory backdrop can be created for the digital currency and blockchain industry it'll assist in further fuelling the 'ideas boom'. Specifically, by removing impediments to innovation in this sector, Australia is sending a clear signal to the startup ecosystem that it supports an industry with extraordinary potential to impact how consumers and business interact.

About FinTech Australia

FinTech Australia is a national not-for-profit organisation with a vision to make Australia the number one market for FinTech in the Asia-Pacific region. Founded in November 2015, the founding membership base comprises over 50 startups, venture capital funds, hubs and accelerators from across Australia that specialise in FinTech. We have seven committee members based in Sydney, Melbourne, Perth and Brisbane.

The Association's key objectives are:

- to support the Australian FinTech community;
- build awareness and trust in FinTech startups; and
- to advocate for better policy on behalf of our members.

Responses To Discussion Questions

Please find below our responses to the questions raised for discussion in the '*GST Treatment of Digital Currency - Discussion Paper*'.

Identifying Digital Currencies

1. **Should digital currencies be identified for GST purposes by defining them or listing them? If a combination or alternate approach should be used, please describe how it would work.**

Digital currencies should be identified by definition, not by list.

A list would hinder the growth of blockchain technology because of the potential time delay in updating the list. In addition, it would create a significant administrative burden, regardless of whether the list is in legislation, regulations or ATO publications.

The nature of blockchain-based digital currencies is such that 'forking' a currency's blockchain can change the characteristics of the currency, and can also create a new currency. It will be impractical to monitor the status of all digital currency blockchains in order to update a list.

Although the use of a definition will inevitably require interpretation, this will certainly not be unique in the tax law – it is the role of tax professionals and ATO guidance to provide clarity to taxpayers in these situations.

2. **Assuming digital currencies are to be defined for GST purposes, what criteria should be included? Should specific types of other currencies be explicitly excluded in the definition? Would all criteria be given equal weight?**

The criteria should include the following:

- Relies on a blockchain or distributed ledger
- Functions as a store of value
- Does not represent an ownership interest or right to any other property
- Does not rely on a contractual relationship with the issuer

Relies on a blockchain or distributed ledger

This will capture all currently understood concepts of digital currencies. The inclusion of the term 'distributed ledger' is broad enough to capture all presently foreseeable technologies which could be used to create digital currencies.

Functions as a store of value

This is a lower threshold than 'medium of exchange' and is more appropriate given that in the early stages of a digital currency, there may not be sufficiently widespread adoption to constitute a 'medium of exchange'

Does not represent an ownership interest or right to any other property

This will exclude blockchains which record a right to some other asset, rather than exist as a store of value in themselves. For example, blockchains can be used to record ownership of real property, shares or other assets. In those cases, the digital tokens do not function as digital currency but as a representation of rights to those other assets. Accordingly, the GST law should apply to those rights or assets as it otherwise would - i.e. taxable real property or input taxed shares.

Does not rely on a contractual relationship with the issuer

This criterion will exclude ‘closed-loop’ currencies such as in-game currencies and loyalty points schemes.

The criteria should <u>not</u> include any of the following:

- The legality of purposes for which the currency is used (see further below)
- Any examination of the developers or maintainers of the currency (the focus should be on the characteristics of the digital currency itself)
- The extent of use, number of users or transaction volumes (adds uncertainty, and a ‘minimum size’ or ‘minimum adoption’ criteria should not be a policy objective of this change)

3. **Regardless of how digital currencies are identified for GST purposes, should a decision- maker have the capacity to exclude one or more of them under certain circumstances, such as if a currency was being used predominantly for illegal purposes?**

No. This would undermine the purpose of having a definition of digital currencies, and could result in a de-facto list-based approach.

It would be difficult to set an objective standard about the use of a particular currency ‘predominantly for illegal purposes’. It would also place unnecessary burden on the decision-maker.

In any event, this should not be a policy objective of the GST Act. Many other aspects of the tax law do not differentiate between legal and illegal activities. Other areas of law (such as anti-money laundering and financial crime) can be used to discourage and penalise illegal activities involving digital currency.

4. **Regardless of how digital currencies are identified for GST purposes, what can be done to ensure the provisions remain relevant as technology advances?**

The use of broad and technology-neutral definitions (e.g. ‘distributed ledger’) will assist.

Consideration should also be given to the policy objectives of the GST Act. The amendments should err on the side of being broader rather than narrower. The current application of the GST Act - that supplies of digital currencies are taxable supplies - has been acknowledged as an anomaly rather than a policy objective. Therefore, revenue impact should not be a significant criteria in deciding the scope of the amendments.

Addressing Double Taxation

5. **Should digital currencies be given input-taxed treatment or be treated equivalently to 'money' for GST purposes, noting the limited differences in outcome and the likely compliance burdens and timeframes for implementation?**

The simplest option appears to be input taxed treatment. However, this may result in input tax credit leakage for digital currency exchange businesses, as detailed in sections 6 and 7 below.

The digital currency industry is at an important inflection point. The need to support the industry as it matures is of vital importance to the Australian fintech innovation agenda. Accordingly, in determining the preferable option, speed of implementation should be a major consideration. Given that a change to input tax treatment would only require modifications to the Regulations which accompany the GST Act, there is a strong preference for this option.

Further, as noted by Treasury in the discussion paper, treating digital currencies as input taxed or 'money' for GST purposes is unlikely to result in a materially different outcome for the majority of cases. Further, the move to input tax treatment aligns with the indirect tax treatment most other jurisdictions have adopted with respect to digital currencies. Also, from an Australian GST perspective, the alignment of digital currencies with other synthetic financial instruments reduces the possibility of tax distortions as a result of the change. In this regard, we consider input taxed treatment as the preferred option.

However, we do note that industry participants have commented that treating digital currencies as 'money' for GST purposes would result in an outcome that aligns more closely with how most perceive them - as currency. Further, the optics in relation to treating digital currencies as 'money' may aid in further advancing the industry in Australia.

It should also be noted that a change to input taxed treatment will require modifications to the table in 70-5.02B of the GST Regulations. Specifically, there will be a need for newly specified RITCs to be included which reflect the supplies commonly made by digital currency companies.

6. **Are there specific examples of different outcomes between the options that would result in one option being favoured? How frequently would these circumstances arise for relevant businesses?**

Under input taxed treatment there are some concerns regarding the potential for 'GST leakage' on acquisitions that can not access full input tax credit - for example, due to breaching the financial acquisitions threshold (**FAT**). To the extent that they are able to access reduced input tax credits (**RITCs**) this issue may be somewhat mitigated.

This issue is most likely to arise for businesses whose sole or main business is the supply of digital currency - known as digital currency exchanges. Digital currency exchanges play a key role in the digital currency sector, by enabling other businesses to convert between local currencies (e.g. AUD) and digital currencies (e.g. bitcoin). For these businesses, input taxed treatment would result in them making input taxed supplies of digital currency. This could result in input tax credit leakage because they are unable to claim input tax credits on their acquisitions of taxable supplies.

One potential solution is to make RITCs available to these businesses - for example by ensuring table in 70-5.02B of the GST Regulations is adequately amended to incorporate supplies commonly made by digital currency exchange businesses.

7. **What effect does each of the options have on the regulatory burdens and compliance costs of different market participants (for example, consumers, merchants and digital currency traders/intermediaries)?**

It is likely that the compliance burden in relation to the change to either input taxed or 'money' treatment for most industry participants should be minimal.

In most instances, consumers will not be required to make any changes to the way they currently account for GST transactions related to digital currencies. For businesses wishing to accept payment in digital currency and/or pay their suppliers in digital currency, the changes will result in a minor compliance cost associated with modifying how they account for digital currency transactions.

Under all proposed options, the initial compliance cost will likely be felt most by digital currency exchange operators. Depending on the business model used by the business (e.g. broker or intermediary/agent), the compliance burden of shifting to accounting for a differing GST treatment might be non-trivial.

More specifically, one of the major concerns relating to input taxed treatment is that digital currency exchange businesses may not be entitled to full input tax credits for GST incurred on expenses that relate to their supply of digital currency. For example, in the instance where the FAT has been exceeded, a digital currency exchange business may not be able access full input tax credits on a variety of expenses incurred in connection with their digital currency exchange business in Australia (e.g. rent, power, server costs etc).

This situation may result in additional regulatory complexity and further compliance costs for digital currency businesses as they will need to determine the appropriate GST treatment of their acquisitions. This along with 'GST leakage' associated with the acquisition of supplies that do not qualify for a full input tax credit may lead to some startups still electing to relocate or continue to conduct their operations from outside of Australia.

8. **Are additional reduced credit acquisitions required to be specified in the GST Regulations to allow access to RITCs for the digital currency industry? If so, what types of acquisitions would they include?**

It is likely that further items will need to be added to the table in 70-5.02B of the GST Regulations to reflect specific acquisitions industry participants make in procuring bitcoin.

For example, these may include:

- fees associated with acquiring digital currencies from other exchanges;
- power costs directly incurred in mining digital currencies;
- rent;
- server costs;
- marketing;
- computer equipment;
- consulting fees; and
- other general vendor costs.

9. **Under input taxed treatment or treatment as ‘money’ for digital currencies, would Australia regain sufficient international competitiveness, compared to other jurisdictions?**

Treating digital currencies as input taxed financial supplies would put Australia at parity with the UK and EU, following the decision in the ECJ case of *Hedqvist*.

However, businesses operating in jurisdictions without a VAT-style consumption tax (e.g. the US) would still have an advantage over companies operating in Australia, because they do not face input tax credit leakage (not being able to claim input tax credits).

To further Australia’s fintech agenda, a treatment that does not result in input tax credit leakage should be preferred.

10. **Does GST-free treatment have any significant advantages that haven’t been considered?**

By all measures, digital currencies have seen immense growth since the inception of bitcoin. This has created a thriving global industry which Australia has the opportunity to be a leader in.

As we note in our response to question 9, businesses operating in jurisdictions which do not have a comparable indirect tax systems may have an advantage over Australian companies because they do not face the same input tax credit leakage.

GST-free status would avoid the added complexity of amending RITC entitlements or requiring digital currency businesses to rely on the FAT.

In this regard, granting GST-free treatment to digital currencies may stimulate the growth of Australia's digital currency industry and further advance the fintech innovation agenda.

11. **Are there other options to address the current GST treatment of digital currencies that have not been considered and which would provide significant advantages?**

All the options available under the GST Act have been addressed in the Treasury discussion paper.

Please let us know if you require any further information on the points discussed in this submission.

Regards

Alan Tsen
Board Member
Bitcoin Association of Australia

Reuben Bramanathan
Associate Counsel
Coinbase