# Submission to the Senate Economics References Committee's Digital Currency Inquiry

This submission primarily addresses the definition of digital currencies under Australian tax law.

## Completeness of the ATO's current interpretation

The Australian Taxation Office's (ATO) draft ruling (GSTR 2014/D3) articulates its view that digital currencies such as bitcoin are subject to GST, hinging mainly on its view that they cannot be considered to be a form of money. While the reasoning in the draft ruling generally convincing, arguably this is less so for those sections relating to whether bitcoin meets the definition of a payment, and by extension, whether it is money.

The draft ruling notes in section 30 that for the purposes of the GST Act, **money can be defined as 'whatever is supplied as payment by way of: i) credit card or debit card; ii) crediting or debiting an account; iii) creation or transfer of a debt'**. Sections 57-60 interpret the word 'payment' as excluding bitcoin because bitcoin is not denominated in fiat currency. Perhaps there is a subtlety to the language here that is not readily apparent, but on face value the ATO's assertion appears to be incorrect when consideration is given to the large number of websites, ATMs and private persons who offer to buy or sell bitcoin at a price denominated in fiat currency.

A cursory internet search will identify websites that substantiate our point, including those in Australia that target Australian clients. These websites will generally show the user the current value of bitcoins in a fiat currency, such as Australian dollars, and allow the user to submit a transaction based on a total value of fiat currency that they wish to spend (e.g. A$200 of bitcoins) and/or the number of units of the product (e.g. 1.5 bitcoins) that they wish to trade. In this sense it is little different than any other transaction, for instance the child who goes to a corner store to make a purchase of lollies denominated either in fiat currency ("20 cents of mixed lollies please") or straight numerical units ("4 of those please").

While our view is that bitcoins pass this definitional test, the draft ruling goes on to state that this is irrelevant because it fails the subsequent tests of:

- 'by way of: i) credit card or debit card'. It is our view that this test may in fact be passed as Australian and international merchants provide debit cards that can be charged with bitcoins and used in the same manner as any other credit/debit card. It is not clear with the ATO has considered any implications of this.
- 'by way of: ii) crediting or debiting an account'.
    - The ATO interprets 'account' to require that there is an account provider that has a relationship with an account holder. It is not clear why this need be the case, but it should be considered that bitcoins are essentially held in accounts not dissimilar to those more familiar from the banking sector. Bitcoins are held in wallets identified by an alphanumeric string. A banking customer will make a payment by sending some of their account's balance to another account that is identified by a BSB and account number. The same process applies for bitcoins, with the alphanumeric string taking the place of the BSB and account number. In their record system, the bank(s) will change the balance of the accounts to show that the transfer has occurred. The same happens with bitcoins, except the record system is not a

centralised register but a decentralised one for which the identical copies are held on thousands of computers.

- Further, many commercial enterprises dealing with bitcoins provide bitcoin-denominated accounts to their clients. The clients of these firms are account holders, and they are able to enforce that the account provider takes certain actions in relation to their holdings, such as processing a transfer to move their account balance elsewhere. This appears directly contrary to the ATO's statements in section 64, including that 'a holding of bitcoin creates no right of action against anyone'.

It is the view of this submission that the above points reflect weaknesses in the ATO's interpretation of existing regulations, possibly due to an incomplete awareness of the nature of the bitcoin sector. As such, arguably it should be recognised that bitcoins meet the GST Act's definition of money and therefore would not be subject to GST.

## Taxation should only occur when it provides a net gain to Australian society

Australia cannot have a bitcoin industry if it is subject to GST as the ATO is currently proposing, or at least not in any meaningful way. Bitcoins can be transferred around the world within an hour, and are identical regardless of where they were purchased. An Australian or foreign person could buy bitcoins from an Australian seller and pay GST, or simply click on a different website and purchase the exact same thing for around 10% less. There is little or no rational reason why any Australian entity would receive an individual's business.

Already it can be observed that Australian technology firms have or are planning to shift overseas. Operations, such as my own, have either shut down or significantly curtailed their activities. This is a very disappointing personal outcome for all the Australians involved, to see their efforts invalidated through no shortcoming of their own.

More importantly, it also reflects a net loss for the Australian taxation system. While the tax treatment of bitcoins has always been unclear, it was nonetheless obvious to most participants that normal taxation rules applied. That is, tax must be paid on any profits made, either through general income tax arrangements or as capital-gains tax on bitcoin investments. For entities that operate bitcoin exchanges, even the application of GST to their value-add (i.e. 10% tax paid on the margin they make between buy and sell prices) would probably have been sustainable. Instead, applying GST to the entire sale price means the businesses must shut or move offshore. In either case, not only does this mean no increase in taxation receipts from GST, but it also means the loss of all possible taxation revenue that would otherwise be received.

As such, the proposed GST interpretation is likely to actually decrease tax receipts. The negative consequences build from there – increased administrative burden for any remaining firms, lost income tax receipts from employees moved offshore or made redundant, and the multiplier effects that any decrease in economic activity has more broadly. All the negative effects of a tax are present here with none of the offsetting positives that must be present to justify it.

## Lessening business impacts from anticipated changes in the future

In general, entrepreneurs and innovators are not restricted to single industries or products. Many of those who have had their initiatives significantly harmed by the proposed taxation arrangements will remember this as a cautionary lesson when considering the merits and risks of innovation in other areas. This likely means less innovation and economic development, or its movement offshore.

This Senate Inquiry is a positive step. It hearteningly shows the potential responsiveness of legislators even to matters which, in the context of broader Australian society, are admittedly relatively niche. We would like to see arrangements put in place for the greater and earlier use of proactive measures such as this.

Unfortunately in this instance, the Inquiry may have come too late to meaningfully mitigate the damage to the digital currency industry in Australia. Unless some moratorium or other arrangement can be made to immediately ameliorate the impacts of the taxation treatment then it is likely that most entities will have moved offshore or shut down by the time the Inquiry reports, and then the recommended measures are considered and implemented. Further, little new business development can be expected in that period of uncertainty. A few years of industry hiatus is never good, but rarely more damaging than in new fields of the information technology sector.

That the ATO was considering this topic was no surprise, nor were the potential negative implications unforeseen. It would have been better for the Inquiry, or some similar process, to have either preceded or been conducted concurrently with the ATO’s review. Had this happened it may have been possible for solutions to have been developed and so allow for business development and operations to continue with little interruption. Although perhaps beyond the scope of this Inquiry, we encourage recognition that it is more desirable to prevent the injury rather than waiting for it to occur and only then beginning to look at how (or whether) the injury can be patched.