REGULATORY UPDATE ON INCOME TAX TREATMENT OF DIGITAL PAYMENT TOKENS

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Introduction

In the first article of this two-part feature, we provided an update on the latest tax guidelines published on 19 November 2019 by the Inland Revenue Authority of Singapore ("**IRAS**") in relation to Goods and Services Tax which came into effect on 1 January 2020. In this second article, we will discuss the IRAS e-tax Guide published on 17 April 2020 on the income tax treatment of digital tokens (the "**e-Tax Guide**").

Income tax treatment of digital tokens and ICOs

The e-Tax Guide provides guidance on the determination of general income tax treatment of digital token transactions based on the nature and use of the tokens rather than how they are labelled. IRAS recognizes that digital tokens are differentiable based on the nature and use of the tokens and their labels are not determinative of such. Specifically, the e-Tax Guide recognises the three main categories of digital tokens, namely, (i) Payment Tokens; (ii) Utility Tokens; and (iii) Security Tokens.

Payment tokens

The e-tax Guide provides that Payment Tokens (including cryptocurrencies) are to be treated as intangible property as opposed to legal tender. As such, the income tax treatment of transactions involving payments for goods and services in Payment Tokens will be classified as 'barter trade' and the value of goods or

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services transferred should be determined at the point of the transaction. Tax will fall on the value of the goods and services being purchased at the point of the transaction.

Security tokens

Security Tokens are regarded as being akin to capital markets products and the e-Tax Guide mentions that Security Tokens will be considered by IRAS as a form of debt or equity. Security Tokens are therefore taxed in accordance to the interest or dividend derived by the owner of the Security Token. Additionally, where the Security Token is disposed of, the tax treatment of the gain/loss on disposal will depend on the nature of the Security Token, specifically, whether it is a capital or revenue asset, and accordingly, whether the gain/loss is capital or revenue in nature.

Utility tokens

Generally, a Utility Token grants an owner of the said token a specified or implied right to use or benefit from a good or service. The proceeds from the issuance of Utility Tokens will therefore be considered revenue in the form of a prepayment for goods or services and are taxable. The point of taxation will occur when the performance obligation which the Utility Token provides is fulfilled.

ICOs

The e-Tax Guide also provides guidance on the tax treatment of income received by a token issuing company through an Initial Coin Offering ("**ICO**"). The tax treatment of the income of an issuer arising from an ICO will depend on the type of digital token offered in the ICO.

The income received by an issuer of Utility Tokens from an ICO is taxable given that Utility Tokens come with an obligation for the issuer to provide a service in the future. The income received is therefore deemed to be consideration for the payment of the future service and is taxable, being revenue in nature, specifically, deferred revenue.

Income received by way of an issuance of Payment Tokens during an ICO will also be taxable. In this instance, the ICO company is regarded as carrying on the trading of Payment Tokens, with the tokens being regarded as its trading stock.

The income received from an issuance of Security Tokens in an ICO will not be taxable. The issuance of Security Tokens confers certain rights to the owner of the Security Tokens akin to those of an equity shareholder or debt holder. In this respect, the income received by the ICO company will be akin to proceeds from the issuance of a debt or equity which is regarded as capital in nature and therefore not taxable.

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Conclusion

Overall, the e-Tax Guide has recognised the different categories of digital tokens, therefore providing much needed clarity for businesses and/or individuals who may want to deal in digital tokens. In an industry where there is still much uncertainty in relation to legal and regulatory requirements, the publishing of the e-Tax Guide is certainly welcome in establishing Singapore as a digital token friendly environment with clear legal and regulatory guidelines. You may access the e-Tax Guide via the following link:

https://www.iras.gov.sg/irashome/uploadedFiles/IRASHome/e-Tax_Guides/etaxguide_CIT_Income%20Tax%20Treatment%20of%20Digital%20Tokens.pdf

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