

# THE POWER OF BEING UNDERSTOOD

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## VAT AND BITCOINS



## VAT INSIGHTS

### VAT and bitcoins

The sense of history leads cash money to be replaced by e-money in the near future. Therefore, markets and laws will have to incorporate this new data into their regulations and frameworks. Since VAT is a tax on economic flows, the regulations must apply to e-money transactions like any other flows.

In any case, before applying VAT rules the flows must be described and qualified.

The first issue is to know what e-money is. There are wide variety of e-money currencies such as : ether, litecoin , dogecoin , monero , ripple , augur, iconomi, zcash, and stellar to name a few. Each kind of e-money has its own specificities. We are focusing here on one of them: the bitcoins.

In addition to the bitcoin definition, the life cycle of e-money and the way to use it have to be analyzed to find out where the taxable events occur, if any, and the way to tax them.

There are several definitions of e-money. They are quite similar. For example, for the European Central Bank it is an electronic store of monetary value on a technical device that may be widely used for making payments to entities other than the e-money issuer.

The article 2 clause 2 of the European Directive 2009/110/EC states gives the following definition "electronically, including magnetically, stored monetary value as represented by a claim on the issuer which is issued on receipt of funds for the purpose of making payment transactions [...], and which is accepted by a natural or legal person other than the electronic money issuer"

Bitcoins (BTC) comply with those definitions. Bitcoins were created in 2009 from the "Blockchain".

This is a computer technology for storage and transmission of data that is secure and operates in the frame of a peer-to-peer network. The bitcoins transactions are made by digitally exchanging anonymous, heavily encrypted data.

Each user has an electronic wallet to store bitcoins and to pay goods or services.

The Bitcoins algorithm is designed to generate only 21 millions of bitcoins. At the end of 2017, 16.7millions have been generated already.

The smallest subdivision of a bitcoin is 0.00000001BTC.



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Suppliers called “miners” who validate all transactions and add them to global the register (the Blockchain) generate the bitcoins. Those suppliers are remunerated by new bitcoins generated by the system and a mining fee generally paid and defined by the spender of BTC.

In the aforementioned process, we can see at least four different main types of transaction:

- Issuance of new bitcoins
- A mining fee
- Buying and selling bitcoins
- Selling goods and services paid with Bitcoins.

It can be easily stated that all the above stated transactions are in the scope of VAT. Effectively, they all comply with definition given by the GCC VAT agreement: operations carried out for consideration in the frame of an economic activity operated independently.

Concerning the new bitcoins and the mining fee received by the Miner, they are two considerations paid for the same service of validation and posting in the Blockchain. A Miner in UAE or KSA would be a taxable Person if he exceeds the registration threshold of SAR 375,000 (USD 100,000), otherwise the operations are not taxable.

If the Miner is a taxable Person, the last question is to find out if the transactions are exempt, zero-rated or taxable at the 5% rate.

The definition of financial services are quite similar in both countries.

In KSA financial services concern the provision or dealing with money, short-term finance or long term finance including issue, transfer, receipt, payment of money or any dealing with money or security for money or any note or order for payment of money.

In UAE, financial services are generally directly related to money, dealings in money or its equivalent, or the provision of credit.

Keeping in mind these definitions, we can ascertain that the supply of mining services qualifies as financial service.

In UAE and KSA, financial services are exempt except when they are compensated with explicit fee, commission or commercial discount are taxable.

It seems that new bitcoins received and the mining fee can qualify as explicit fee. The number of new bitcoins received is a public fixed amount given by the system. For example during the third quarter of 2018, the amount was 12.5 BTC per validated block. The mining fee is also a fixed amount decided and offered by the Spender of Bitcoins for the validation of the transaction. The higher the proposed fee is the quicker the transaction is validated.

Therefore, the new bitcoins received by the Miner and the mining fee should be taxable at the rate of 5%.

It should be the same thing for operations, carried out by special market places, consisting to buy and sale bitcoins. In fact, it is a currency exchange service compensated by an explicit exchange rate or exchange commission. Therefore, the currency exchange fee of bitcoins should be also taxable at the rate of 5%. However the differential of rates (buying value vs selling value) is an implicit margin obtain by the miner. This implicit margin is exempt.

Concerning all the supplies of goods or services paid with bitcoins they are obviously taxable in connection with the rate to be legally applied to the good or service

concerned. For those transactions, the prices could be displayed in SAR or UED and BTC. However, in KSA the VAT must be showed in Riyals and in EAD in UAE.

Therefore, the VAT calculated in the local currency is to be paid whatever could be the exchange rate of the bitcoins received for payment.

There are plenty other ways to utilize bitcoins such loans, loyalty program, discount etc. Each of them have to go through the analysis grid of the VAT regulations.

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