CRYPTOCURRENCIES
THE UK TAXMAN COMETH

ANDERSEN

Introduction

Although the birth of cryptocurrencies was over a decade ago, their decentralised and esoteric nature and the seeming total secrecy with which people bought and sold them or spent them has meant that, to a large degree, many people in the “crypto community” have regarded them as being unregulated and sitting outside normal boundaries – including taxation. For their part, tax authorities around the world (including HMRC in the UK) have been slow to react to the explosive popularity of cryptoassets and adopt effective means of policing the taxation of them.

With the news that HMRC has collected customer data directly from crypto exchanges and received such data from their foreign counterparts, the “normal” rules are set to come to bear on the crypto world with a vengeance.

Why is selling or using cryptocurrency taxable?

In the UK, cryptocurrencies have no special tax status and are treated as normal intangible assets for tax purposes. Every time cryptocurrency units are either sold and exchanged for normal currency (like pound sterling), are exchanged for other crypto or other assets or used to pay for services there is a disposal for tax purposes. Such disposals normally give rise either to a capital gain or capital loss but in some limited circumstances could instead be treated as trading gains or trading losses. Either way, any net gains or profits fall within the scope of UK taxation.

For Higher Rate and Additional Rate taxpayers subject to UK Capital Gains Tax, the applicable rate of tax on any capital gains net of any allowable capital losses and reliefs is 20% (although it is widely speculated that this rate will be aligned with Income Tax rates in 2022). The small minority of people who have traded rather than invested in cryptoassets face potential Income Tax rates far higher still (up to 45%).

What if no tax was paid in earlier years?

Depending upon the circumstances and the “behavioural” reasons for any under-declared income or gains, HMRC can still assess and collect any unpaid tax for up to 20 years. Even in the most benign circumstances – where there was no overseas element and an “innocent error” was made in a tax return, or there was a reasonable excuse for not filing a tax return at all - HMRC can go back at least four years to assess and collect any unpaid tax.

In addition to collecting any unpaid tax, depending upon the circumstances, HMRC can also levy substantial “tax geared” penalties and will charge late payment interest for the time any tax still assessable was unpaid.

Why have I received a “nudge letter” about cryptocurrencies?

If you receive a “nudge letter” from HMRC it is because data HMRC has obtained from a cryptocurrency exchange or from some other source – either by its own efforts or from an overseas tax authority – has identified you as selling or otherwise disposing of cryptocurrency assets. HMRC’s sophisticated computer system, known as CONNECT, has cross compared the information obtained against your tax records and has identified a risk that you have omitted to declare those disposals in full and may have underpaid UK tax.

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What do I do if I receive a “nudge letter” or have something I know I need to tell HMRC about?

You should seek urgent expert advice. Your nudge letter will set out a list of options either for telling HMRC about any omissions or for signing and returning a declaration that you have no omissions to tell them about. You must first confirm with appropriate professional advisers whether or not your tax filings are complete and accurate and how best to respond to HMRC – either to initiate a disclosure or to state that there are no omissions to disclose.

If tax omissions have occurred, a disclosure should be made to HMRC setting out the full background – including the behavioural factors (that determine for which years tax is still collectable and the level of any penalties) and computing the amounts of tax, late payment interest and penalties payable.

What happens if I do nothing?

Not all nudge letters are sent to people who have unpaid tax liabilities because the computerised checks are not detailed and tend to lack all relevant information. However, anyone who ignores a nudge letter, or who otherwise wilfully chooses not to come forward to rectify any known omissions, risks HMRC opening a formal investigation into their tax affairs. Such enquiries can be time consuming, professionally expensive and can extend into all other aspects of a person’s tax affairs and those of their businesses.

In these circumstances, HMRC often adopt a less open-minded stance than when people come forward to make a voluntary disclosure and may argue much harder that the relevant behaviours mean that more years are still assessable and that higher penalty levels should apply on the tax payable.

It must be emphasised that HMRC also takes a dim view and can harshly penalise those who seek to rely on “Nelsonian blindness” - “holding a telescope to the wrong eye” for fear of what they might see if they look properly. HMRC tend to regard failing to review one’s tax affairs properly out of a suspicion that there might be further tax to pay as deliberate conduct and the tax courts have supported that position.

Contacts

We have specialist expertise both in the taxation of cryptoassets and in making voluntary disclosures to HMRC to maximally mitigate and regularise any outstanding UK tax liabilities.

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