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Crypto tax guide for the United Kingdom

The United Kingdom was one of the earliest countries that imposed taxes on cryptoassets.

HMRC is among the most active tax authorities in tracking down people who avoid declaring and paying for their cryptocurrency taxes.

This guide lets you know how to file and pay for your crypto taxes in the UK. We'll break down what cryptoassets are, which taxes apply to them, and how these taxes are calculated and paid.

What cryptoassets are

Cryptoassets are another term for cryptocurrencies. These are coins or tokens available electronically and function as digital cash. There are numerous kinds of cryptoassets, but popular ones that have taken the world by storm include Bitcoin, Ethereum, Litecoin, Dash, and Ripple.

Cryptoassets work through a peer-to-peer system with no central authorities used to facilitate transactions. They can be traded, stored, or transferred to others electronically without mediators such as banks.

Digital Ledger Technology (DLT) is a system used by cryptoassets to record transactions and their details. DLT also enables multiple crypto transactions to be recorded from different places all at the same time. However, note that all cryptos may be using some form of DLT, but cryptoassets may not be involved in all applications of DLT.

Now, many people consider cryptos as a form of money. It could function as one, but it's generally not money-like as of now, and this is the reason why central finance authorities refer to cryptos as cryptoassets rather than cryptocurrencies.

The UK's HMRC doesn't see cryptos as a currency form, either. They instead classify cryptoassets into three – utility, exchange, and security tokens. We'll quickly explain each of them here.

The rules around taxation and the regulation of cryptoassets are continually changing. The information provided in this guide was correct at the time of publication, however, may be subject to amendment at any time without notice. That is why it is important for you to seek expert, professional advice. If you have any questions regarding this guide, please contact us.

Utility tokens

Utility tokens are cryptos developed and used in exchange for goods or services. The tokens, therefore, act as payment for goods and services.

Businesses or organisations carrying out transactions using utility tokens typically issue their tokens and commit to using them inside a particular business platform.

Many utility tokens started up through an organisation developing and issuing them first. Later, the new utility token is used to purchase goods and services offered by the crypto developer or issuer.

Transactions made through utility tokens are usually meant to raise funds for the organisation to expand further and introduce new developments to their new cryptos and platforms.

Exchange tokens

Exchange tokens are meant to be used as a payment method. DLT is used to facilitate transactions using these tokens. Unlike utility tokens, exchange tokens aren't backed by an individual business entity and do not provide access or rights to any kind of goods and services.

In essence, exchange tokens are valued simply through their use as an investment or exchange vehicle. Most popular cryptocurrencies fall under the exchange tokens category.

Security tokens

Security tokens are cryptoassets that function as investment contracts. A security token holder may anticipate a future profit from any revenue share, dividend, or market appreciation derived from the tokens.

> “There are stringent guidelines attached to security tokens regarding who can purchase the coins and how they are transferred to others.”

For instance, you need to complete a Know Your Customer (KYC) protocol before being allowed to hold a security token for crowdfunding events. KYC ensures that each token investor has their real identity revealed, unlike the anonymity that dominated utility and exchange tokens.

Cryptoasset characteristics

Now, utility, exchange, and security tokens are all highly unpredictable in terms of value. Several cryptos started with high values only to drop to considerably low numbers. Others remain relatively stable, making them continuously lucrative to investors amidst the possible losses and risks.

Volatility is a crucial characteristic of cryptoassets. But other factors include the following:

- Decentralized nature
- Runs on a trustless ecosystem
- Immutable – transactions cannot be undone
- Fungible – individual tokens can be interchanged with other cryptoasset types
- Generally anonymous; some cryptos like Bitcoin can be pseudonymous as owners are only identified through addresses or keys
- Offers an exclusive cryptographic proof of ownership for the crypto holder

All these characteristics play important roles in the formulation of cryptoasset taxation policies in the United Kingdom and elsewhere in the world.

Which taxes apply

Most cryptoasset holders are individuals who use cryptos as a personal investment. They typically use the tokens to make certain purchases or gain capital appreciation, which increases the value or price of the cryptoassets.

As such, the HMRC mandates that crypto holders are liable to pay Capital Gains Tax when they “dispose” or use their cryptos in the following ways:

- Utilising cryptos for payment of goods and services
- Exchanging crypto assets for another crypto type
- Selling cryptos to gain fiat money
- Giving away crypto assets to other people

Computation for such taxes will be determined by the capital gains an individual gets from the crypto transaction.

Meanwhile, Income Tax and National Insurance contributions shall be collected from individuals who receive crypto assets from:

- Mining
- Airdrops
- Lending / Staking
- Hard forks (not subject to Income Tax)
- Income

“This is because these crypto assets provide an individual with transactions comparable to those earned from wages or business incomes/profits. They can also be classified as miscellaneous income, on which Income Taxes will be imposed.”

Now, employers may pay their employees using crypto assets, and it’ll be classified as a non-cash payment. In this case, the employee recipient becomes liable to pay Income Tax and National Insurance contributions.

Exchange tokens location and taxation

HMRC introduced an update to its guidance concerning exchange tokens taxation in December 2019. This concerns the crypto assets' situs, or location, being an essential factor in determining the tax liability on the tokens. Note that this only applies to exchange tokens and not to utility or security tokens.

To date, HMRC doesn't have a clear position regarding the location of both utility and security tokens.

In the United Kingdom, a non-domiciled person is either a British national/passport holder or a foreigner who lives in the UK but considers another country as their domicile or permanent home. Non-domiciles play a significant role in the UK's income taxation.

As such, non-domiciles income taxation is based on remittance, which means only gains and income remitted to the United Kingdom are taxed.

For crypto assets, HMRC mandates that exchange tokens held by a non-domiciled individual will be in the United Kingdom when the person is a UK resident. Therefore, the person becomes liable to pay taxes to the UK.

Now, crypto assets are generally intangible assets, as seen by the UK courts. Considering the exchange tokens' location, using the beneficial owner's residency is the best way to determine its liability to pay taxes.

Typically, the Taxation of Chargeable Gains Act 1992 sections 275 and 275A provide guidance on which assets are deemed located in the UK. However, these stipulations cannot be applied to exchange tokens in most circumstances. This is because:

- Exchange tokens are seen as a new form of intangible asset. As such, determining its location is entirely different from the rules that apply to other intangible assets like debentures or shares.

- Exchange tokens can be "turned to account," which means that they can carry absolute economic values when used in transactions such as payment for goods and services, exchanging for another kind of token, or exchanging them for fiat money, a legal tender.

- The exchange token's beneficial owner is the token's only identifiable party who will become liable for taxes.

Now, what happens if a particular crypto asset is co-owned by two or more beneficial owners? How will the Capital Gains Tax be paid for the exchange token?

For this, section 275C of the Taxation of Chargeable Gains Act 1992 applies.

> “Under this legislation, the beneficial owners’ interest in the co-owned tokens is determined by where that beneficial owner is a resident.”

For instance, you’re a UK resident who co-owns an asset with a non-UK resident. You’ll be liable for Capital Gains Tax on the premise that your share of the co-owned asset’s interests is in the UK. However, this will not affect your co-owner’s location since he is not a UK resident.

Meanwhile, the Inheritance Tax is another story. HMRC’s position regarding crypto assets and Inheritance Tax is rooted in section 158 of the Inheritance Tax Act 1984.

Crypto assets are viewed as “property” for purposes of Inheritance Tax. As such, the assets’ location is not determined through Double Taxation Agreements.

Capital Gains Tax

Most people who hold crypto assets use them for personal investment instead of participating in business-level severe crypto assets trading. Hence, HMRC mandates individuals participating in personal investment activities to pay Capital Gains Tax on their profits.

Cryptocurrencies are intangible since they are considered digital assets. If the crypto assets have a realisable value, as well as a capability to be owned by anyone, it counts as a “chargeable asset”. As such, that’s the primary basis for imposing Capital Gains Tax on crypto assets.

In this section, we’ll dive deeper into how Capital Gains Tax works in different crypto asset situations.

Crypto asset disposal

Disposal is a term often encountered and tied to Capital Gains Tax. Disposal refers to using the crypto assets in a variety of ways, including the following:

- Crypto assets used as payment for different goods and services
- Crypto assets being exchanged for a different token type
- Crypto assets given away to other people
- Crypto assets sold for fiat money
- Crypto assets sold for stable coins

All these activities constitute a crypto asset disposal. As such, you can then determine your need to pay Capital Gains Tax by calculating any gains or losses you get because of crypto disposal.

Now, notice that donation to charity isn’t listed among the crypto asset disposal activities that merit a Capital Gains Tax liability. That’s because you don’t need to pay any Capital Gains Tax on charity donation activities.

However, two circumstances may require you to pay Capital Gains Tax on donations:

- Tainted charity donations, that is, the person donates crypto assets with a pre-arranged purpose of directly or indirectly obtaining financial advantages from the charity which received the crypto donation.
- When a donor provides donated crypto assets at an amount more than the acquisition cost, hence realising again.

Allowable costs

In calculating gains or losses for Capital Gains Tax, you can declare costs as a deduction to reduce your tax burden. These allowable costs include the following:

- Any transaction fees paid before the transaction is added to the blockchains
- Original pound sterling valuation that was paid for to acquire the asset
- Costs of advertising for a vendor or purchaser
- Costs covering professional services for contracts regarding disposal or acquisition of cryptos
- Costs incurred in making an apportionment or valuation for calculating gains or losses
- Meanwhile, the following are not included in allowable costs:
- Costs deducted against profits used for Income Tax filing
- Mining activities costs, including electricity and equipment

Some crypto holders may argue that mining costs should be included in allowable costs. However, HMRC’s position is that mining is an activity that isn’t exclusively and wholly used to acquire crypto assets. Apart from mining, there are other ways to earn crypto assets. And as such, this characteristic of mining activity does not satisfy requirements for allowable costs stipulated under Section 38(1)(a) of Taxation of Capital Gains Act 1992.

Pooling

Pooling is a method used to simplify the calculations for Capital Gains Tax. It is used in shares and securities, as well as cryptoassets. HMRC believes that cryptoassets must be pooled per Section 104 Taxation of Capital Gains Act 1992.

How does pooling work in taxation? Essentially, you assign each crypto asset type that you have in its own "pool". Then, every consideration (in pound sterling) paid originally for the tokens goes into every pool, thereby creating a "pooled allowable cost".

Now, to illustrate pooling, let's say you have three kinds of cryptos: Ether, Ripple, and Bitcoin. Each of these crypto token types creates one pool. Hence, you now have three pools – one for Ether, one for Ripple, and one for Bitcoin. Each pool of your cryptos will have its own pooled allowable cost associated with it.

If you frequently move, transact with, acquire, or dispose of your coins, then the pooled allowable cost for each of your crypto pools will then change often, too. Anytime you sell tokens from your pools, it shall constitute a " part-disposal". Hence, your pooled allowable costs shall be deducted with the corresponding amount of sale when computing for your losses and gains.

Rules for cryptoassets acquired within 30 days of selling

There are also special pooling rules that apply when these conditions are met:

- If you acquired your crypto asset tokens on the same day, you disposed of tokens of the same cryptoasset type. It applies even if the disposal happened before your acquisition.

- If you acquired a cryptoasset within 30 days after disposing of tokens of the same type of cryptoasset.

> **"As such, the new cryptos you acquire, and their related acquisition costs shall be recorded separately from the pool. Computations for gains and losses will be based on the new tokens' costs that are recorded separately from your pools."**

HMRC's pooling method can be quite tricky to accomplish, especially if you have lots of cryptoasset types on hand. While pooling's primary purpose is to simplify calculations, that may not always be the case in practical life. So, it's a good practice to continue tracking every amount spent on each of your cryptoassets.

Capital Gains Tax losses

A loss happens when a person disposes of his cryptoassets for less than the allowable costs. Losses should be reported to the HMRC, most especially if you want to use “allowable losses” to reduce your overall gain.

Assets that lose their value

You can use negligible value claim to crystallise any losses on cryptos that have been reduced to a worthless state. Under this claim, you must declare the following information:

- The cryptoasset that is the claim’s subject
- The date your cryptoassets are treated as disposed of
- The amount your cryptoassets should be treated as disposed of

You can file a negligible value claim and report it as a loss at the same time to HMRC. Note that using this claim to dispose of your cryptos will constitute a loss, so you should report it to HMRC.

Lost private keys

Misplacing your private key means you cannot access your cryptoassets anymore. However, you still owned the cryptoassets and can be found still existing in the distributed ledger. It’s just that you lost the private key that gives you access and control over the cryptoassets.

> “With these things in mind, HMRC does not constitute lost private keys as a disposal for Capital Gains Tax purposes.”

But if there is no way to find the private keys anymore, you can file for a negligible value claim. Once HMRC accepts your request, you can crystallise your loss.

Fraud victims

Hacked or stolen cryptoassets are not treated as a disposal by the HMRC. Technically speaking, you still own the assets and have the right to recover them from the ones who victimised you. As such, theft and hacking victims cannot claim losses from a Capital Gains Tax perspective.

Capital loss may only be claimed if:

- Cryptoassets with a current market value are paid for but are not received by the purchasing person

- Worthless cryptoassets are paid for and received by the buyer

Income Tax

Some activities are taxed as income, and we will investigate the specific situations in the following section. Income Taxes possibly apply to:

- Financial trading
- Mining
- Airdrops

Income Tax losses

HMRC mandates that trading losses be reported in your Self-Assessment tax return. You can understand how these losses are reported through the HMRC's help sheets: HS227 Self-Assessment help sheet and HS325: Other Taxable Income.

Traders can reduce Income Tax liability through an offset of their losses against other incomes or future profits. Meanwhile, losses can also be carried forward to later years if your trading activities have profits declared as miscellaneous income.

Crypto tax scenarios

Buying and Selling Cryptoassets (Including Stable coins)

There are no taxes on buying crypto in the UK if you just buy it and hold it forever. You should always keep records of the transactions if you need to prove where you got the funds from or if you want to sell them in the future.

When you decide to sell crypto to fiat, you will have to pay capital taxes on the gains you create with the asset's sale. Every cryptocurrency is seen as a separate Capital Gains Tax Asset.

When you trade crypto to crypto you also must pay Capital Gains Tax on the Gains created in the trade. It is seen as if you would sell it to GBP and convert it to the new cryptocurrency asset. The same rules apply to trades between your crypto assets and stable coins.

Financial trading in cryptoassets (trading as a business)

Are you using your cryptoassets to trade? Then, the HMRC will require you to pay Income Tax on your trading profits. However, this will depend on the frequency and intensity of trading activities you're doing. You can either be liable for an Income Tax or a Capital Gains Tax from crypto financial trading.

Individuals who use cryptoassets to trade frequently with a high level of intensity, sophistication, and organisation are deemed to be doing an activity that already amounts to a financial trade. Thus, the financial trading activity would be considered a business; hence, the need to pay Income Tax on profits gained from it.

Meanwhile, individuals who practise trading activities in a lesser frequency and intensity through simpler means will become liable for Capital Gains Tax instead. HMRC deems that these people trade their cryptoassets almost recreationally. Hence, the activity doesn't constitute a trading business by nature and is therefore not liable for Income Tax but for Capital Gains Tax (see more in section Capital Gains Tax).

Now, how would you know if your trading activity is already comparable to a business, making you liable for an Income Tax on cryptoasset trading profits? It all boils down to a question of fact. HMRC acknowledges that individuals who trade as frequently and intensely as a business do happen only in exceptional circumstances. You'd see if you're often trading cryptoassets similarly as you would trade in securities, shares, and similar other assets.

If you need further guidance, HMRC's Business Income Manual (BIM56800) can help determine if your trading activities are hinging to a business-like level.

Mining

Mining is the process of verifying blockchain ledger additions by solving complex mathematical problems using your computers. Cryptoassets are generated and given to miners as a reward for their mining work.

Now, mining activities can either be a hobby or a full-fledged business. Mining can amount to a taxable trade depending on the following factors as declared by HMRC:

- Mining risk
- Organisation of activity
- Degree of mining activity
- Commerciality

Taxing mining as a hobby

Cryptoassets awarded because of mining as a hobby will have their values evaluated in pound sterling at the time of receipt. The value shall then be taxed under miscellaneous income. The amount chargeable can be reduced depending on the expenses from the miscellaneous income if any.

> “Also, remember that your cryptos gained from mining as a hobby will be subjected to Capital Gains Tax once you dispose of them.”

Taxing mining as a business

If the HMRC determines that your mining activities constitute a business, your mining income shall be added to trading profits and filed under Income Tax. Fees or rewards collected from mining shall likewise be added to your taxable income. Note that all these are again dependent on mining risk, organisation, degree, and commerciality of mining activities.

Should you dispose of the cryptoassets taken from mining as a business, you should add to your trading profits any gains in crypto market value from the time you acquired the tokens. You also need to pay for the National Insurance Contribution.

Airdrops

Airdrops are free tokens or coins given to numerous wallet addresses. These free cryptoassets are often a part of a marketing campaign from specific organisations. Some airdrops are also automatically given to individuals due to registering for an airdrop campaign or for holding kinds of cryptoassets in their wallet.

Income Tax is often applied to airdrops. However, airdrops may be exempted from Income Tax on two conditions:

- The airdropped cryptos are received without doing anything in return (not related to any conditions or any other services)
- The cryptoassets are not a part of businesses or trade that involves cryptos and mining

Income Tax shall be collected on airdrops received in return for a service. For individuals, it will be classified under miscellaneous income. It shall also be subjected to Capital Gains Tax upon disposal of the airdrop cryptoassets. Meanwhile, businesses that received airdrops in return for services shall pay Income Tax and may declare them under trading profits as well. Crypto businesses are also required to pay for National Insurance Contributions too.

Pooling can also be applied to airdrops. Airdropped tokens of which the receiver already has existing tokens shall be pooled together with the existing cryptoasset pool. Meanwhile, airdropped tokens will go into its pool if the holder doesn't have any current cryptos of the same type.

Tax on hard- and soft-forks

Blockchain forks are splits in the blockchain network. It may be due to situations wherein two or more blocks have similar block heights, misalignment in blockchain software from different miners, or an outright modification of existing blockchain code to create changes and new cryptos.

The two types of forking are known as hard forks and soft forks. Hard forks are meant to create new cryptoassets from changes in the main blockchain code. On the other hand, soft forks are meant only to update the protocol for everyone to adopt. New tokens or blockchain networks are not created in soft forks.

Now, HMRC imposes Section 43 Taxation of Capital Gains Act 1992 on taxing blockchain forks, most especially for hard forks with newly minted cryptoassets. This means that your new cryptoassets' value shall be taken from the cryptoassets you already hold before the fork.

If you hold new cryptos due to forking, your cryptoassets should now be divided into two: an original cryptoassets pool and a new cryptos pool. Allowable costs for pooling of your original cryptos will be split between these two pools. Crypto received from a Hard fork is not subject to Income Tax.

Now, if your cryptos are held through an exchange, it is the exchange's responsibility to choose if it will recognise the new cryptos emerging from the fork. Note that you cannot dispose of your new cryptos if your exchange does not recognise them. If this happens, HMRC will deem that you own units of the cryptoasset arising from the fork.

As for apportionment, HMRC does not particularly prescribe any method for cryptos arising from forks. HMRC can enquire into apportionment methods used if it is seen as unreasonable. Also, HMRC can investigate cases depending on their difficulty, as forking can be quite complex in taxation.

Tax on cryptocurrency margin trading

The tax classification for Futures, CFDs (Contract for Difference), and margin trading as far as cryptocurrency is concerned has no clear guidelines from HRMC.

As a financial trader - gains are added to his/her trading profits and is subject to Income Tax. When the individual is not a financial trader, HMRC has not defined if the gains and losses should be considered as CGT or added to miscellaneous income and should be added to the individual's Income Tax.

Tax on gifts

When you gift cryptocurrency to anyone (except your spouse or civil partner), you will have to find out what the market value of the crypto is on the date that you gifted it in sterling pound (fiat). This gift will be considered as sales proceeds in the Capital Gains Tax field.

If the gifted tokens' value has already been charged with Income Tax, the sales proceeds will be reduced according to section 37: Taxation of the Capital Gains Tax Act 1992, which means that the sale of the token will be subjected to the Capital Gains Tax with a reduced Income Tax.

Tax on crypto donations

An individual is entitled to Income Tax relief if they donate crypto to a charity.

They might also be exempt from Capital Gains Tax except for the following cases:

- If the individual sells the crypto asset to the charity at a cost (and is higher than the acquisition cost), he/she will have to pay Capital Gains Tax on the difference between the selling price and the acquisition cost.

- If the individual arranges with a charity to get a financial advantage or kickback. This donation is also called a "tainted donation."

Cryptoassets received as earnings

Cryptoassets may be used to provide income for employees instead of the traditional fiat money. As such, all cryptos received as employment income are subject to Income Tax. The receiver is also required to pay National Insurance Contributions in proportion to the assets' price value.

Now, there are three situations under cryptos received as earnings:

1 Readily Convertible Assets (RCAs)

Readily Convertible Assets (RCA) is a term used to define cryptoassets that are given under existing trading arrangements. RCAs exist per section 702 of the Income Tax (Earnings and Pensions) Act 2003 (ITEPA 2003).

Trading arrangements often already exist or are likely to live during the time cryptos as received as income. This is because cryptocurrency exchanges often facilitate easy exchange from one crypto token to fiat money.

Employers with a UK tax presence should deduct the due amounts for Income Tax and Class 1 National Insurance contributions through PAYE's operations. They should remit these deductions to HMRC in the best possible estimate value from crypto to pound sterling.

Meanwhile, employers who, for some reason, cannot deduct the Income Tax amount from the income are still accountable to HMRC for the due amount. The expected amount should be reimbursed to HMRC within 90 days after the tax year ends. Failure to comply will mean additional charges for Income Tax and National Insurance contributions, as stipulated under section 222 ITEPA 2003.

2 Cryptos that aren't RCAs

Income Tax and National Insurance contributions will still be collected from crypto payments that aren't part of the RCAs. The individual should declare this income on his Self-Assessment tax return. Meanwhile, the employer needs to pay any Class 1A National Insurance contributions since non-RCA cryptos issued to an employee are classified as payments in kind under the National Insurance contributions perspective.

3 Third-party providers of cryptos in connection to employment

Third parties are allowed to provide cryptos as a form of payment in connection to employment. Hence, Income Tax should be collected on these cryptoassets as stipulated in Part 7A ITEPA 2003. Meanwhile, National Insurance contributions will also be collected under Social Security (contributions) Regulations 2001. It is the third-party provider's responsibility to remit all dues to the HMRC through PAYE's operation.

Record keeping

Record keeping primarily lies in the hands of the individual holding cryptoassets. While crypto exchanges provide some form of transaction records, these records last only a limited time and could no longer be existing come the time for tax return filing.

Hence, you, as the prudent crypto holder, should keep a record of the following, encompassing all cryptoassets you have:

- Cryptoasset type
- Transaction dates
- Number of units
- Transaction values in pound sterling
- State of the tokens (bought or sold)
- The cumulative total of all crypto investment units held
- Wallet address/es
- Bank statements

Other considerations

Here are some final considerations regarding cryptoasset taxes in the UK:

- There's an annual tax-free capital gains allowance of £12,000 for crypto traders. Anything after that will generate a Capital Gains Tax according to their tax bracket (10% for basic rate taxpayers and 20% for high-rate taxpayers).

- Pound sterling must be used in completing your Self-Assessment tax return. Gain and loss values should always be converted to pound sterling, first using an appropriate and consistent valuation methodology.

- Some crypto-to-crypto transactions may inherently not have a pound sterling value (for instance, a bitcoin to Litecoin transaction). As such, you should use an appropriate exchange rate for the crypto and pound sterling values during the time the transaction was made.

- Keep all records of your valuation methodology so you can present it to HMRC in case of further inquiries.

- For pensions, HMRC doesn't allow cryptos to be used for creating a relievable tax contribution to a pension scheme.

- Cryptoassets are treated as property for Inheritance Tax perspectives and purposes.

Which tax forms do you report your crypto on?

You must report your capital gains on the capital gains summary form (SA100 Tax Return) when your profits are higher than the annual CGT allowance (12,000 pounds in 2019).

You will have to enter the number of disposals, profits, and losses from your crypto trades and any other capital gains you had during the year.

You can find the capital gains summary forms **here**.

And with that, we conclude our crypto tax guide for the UK. We hope to have shed some light on HMRC's positions on crypto taxation for different situations.

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