Cryptocurrency checklist 2023

Including explanatory guidance

# Cryptocurrency Checklist 2023

This guide and checklist is designed to assist public practice members in discharging their obligations in preparing the 2023 taxation returns in relation to for crypto assets.

This information is based on legislation current as at 19 May 2023.

The following version control information has been included to assist you monitor changes to the checklist to ensure you are using the latest version.

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**About the author**

This checklist was updated by Hall Chadwick (NSW) Pty Ltd on behalf of CPA Australia.

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# Introduction

Cryptocurrencies, and crypto assets, are a series of digital assets that use cryptography to ensure digital security, while using distributed ledger technology to permanently record transactions. Cryptocurrencies and crypto assets can exist on a blockchain, which is a digital ledger which stores records of every single crypto transaction. There are countless blockchains in existence, with more being developed every day. The most popular include the Ethereum blockchain, Bitcoin blockchain, Cardano blockchain and Polkadot blockchain. However, there are many others.

The tax implications of cryptocurrencies and assets are numerous and tax agents will need to take these issues into account when working on clients’ tax affairs. With new cryptocurrencies and processes constantly being developed, it is important to understand the different income characterisations and taxing points as well as how the fast-evolving crypto ecosystem affects the tax treatment of specific currencies or assets.

This document provides:

* Explanations of common terms
* Information on tax issues for practitioners
* Pre-meeting questionnaire for clients
* Client checklist for meetings.

The Australian Taxation Office (ATO) also provides further guidance on [crypto asset investments](https://www.ato.gov.au/Individuals/Investments-and-assets/Crypto-asset-investments/).

# Common terms and explanations

## Cryptocurrencies and crypto assets

Two phrases you may come across quite often are **cryptocurrency** and **crypto assets**. While inherently similar as they both exist on the blockchain, there are some differences. It is important to note that currently, from an accounting perspective, both have the same implications. A cryptocurrency tends to be a form of digital currency, whereas a crypto asset includes things such as non-fungible token (NFTs), utility tokens, security tokens and more.

Table : Examples of cryptocurrencies and crypto assets

|  |  |
| --- | --- |
| Cryptocurrency | Crypto assets |
| ETH (Ethereum) | NFTs |
| BTC (Bitcoin) | Utility tokens |
| USDC (USD Coin) | Security tokens |
| SOL (Solana) | Governance tokens |

## Smart contracts

The cornerstone of blockchains such as Ethereum are smart contracts. **Smart contracts** are agreements in the form of computer code that is programmatically designed to execute when certain requirements are met. Blockchains are made up of smart contracts, which is how they remove the need for a financial intermediary. It also means they are indelible and cannot be changed.

## Wallets

Typically, cryptocurrencies and crypto assets are stored on either a **hot wallet** or **cold storage**. Both have benefits, but people choose to alternate between the two depending on the level of security they require.

A hot wallet is a crypto wallet that is connected to the internet, for example, a MetaMask wallet.

Cold storage however, is stored in an offline environment. This may be in the form of a USB device or similar.

Regardless of how your client chooses to store their cryptocurrencies and crypto assets, they are still relevant for tax purposes.

## Security

Security is key in the crypto world. In an industry that’s built on complex coding, there is always the opportunity for bad actors. There are several measures you can advise your clients to take to help protect their assets:

* Using two-factor authentication for accounts.
* Back up your seed phrase (the group of random words generated by your crypto wallet when you first set it up) correctly.
* Use a strong password.
* If dealing with large amounts of value, consider using cold storage.
* Check the URL of the website you’re interacting with.
* Never share your private key (a string of random characters that will grant you access to your funds) with anyone.

The ATO has released its [Crypto glossary](https://www.ato.gov.au/individuals/Investments-and-assets/crypto-asset-investments/crypto-assets-glossary/) which provides further information on current terminology.

# Tax issues for practitioners

## Common crypto CGT events

As cryptocurrency and assets are considered property, capital gains tax events occur when a disposal is actioned. A disposal is considered to occur when the beneficial owner of an asset changes.

Disposal events include:

* Selling crypto for fiat currency
* Swapping one crypto asset for another crypto asset
* Using cryptocurrency for goods and services
* Gifting crypto.

The 50 per cent discount for assets held longer than 12 months also applies to crypto assets. The ATO has also provided [guidance](https://www.ato.gov.au/Individuals/Investments-and-assets/Crypto-asset-investments/Crypto-as-a-personal-use-asset/) on what constitutes a personal use asset in relation to cryptocurrency.

## Common crypto income tax events

Whilst cryptocurrency transactions will generally incur CGT, there is also the potential to incur income tax liabilities depending on the nature of the activity. Some examples of crypto activity where rewards and/or profits are taxed as ordinary income include:

* Getting paid all, or part of, your salary in crypto
* Selling NFTs as a creator
* Earning interest via yield farming
* Earning rewards via liquidity pools
* Earning rewards from a play to earn game
* Using crypto lending platforms to earn interest
* Receiving airdrops
* Earning staking rewards.

Decentralised finance ([DeFi](https://cryptotaxcalculator.io/blog/the-ultimate-defi-tax-guide/)) in particular, has opened a whole new realm of potential tax implications. DeFi takes the intermediary out of the financial process, lowering costs and increasing returns to consumers. Essentially, the consumer has control over their assets on the blockchain, and they can lend them out, borrow against them or trade them without ever using a financial institution. This means that anyone can lend out crypto assets, and correspondingly, anyone can borrow these assets. Users also have the opportunity to participate in activities like staking protocols, earning annual percentage yield (APY) at a very different rate to traditional avenues. No formal advice has been published by the ATO other than via the [ATO Community Board](https://community.ato.gov.au/s/question/a0J9s0000003TJI/p00173526).

Another example of a relatively new process is wrapped tokens. In Australia, there is a general consensus that the process of wrapping a token constitutes a disposal event via a crypto-to-crypto swap. However, there is currently no formal ATO guidance on wrapped tokens other than via the [ATO Community Board](https://community.ato.gov.au/s/question/a0J9s0000001IHj/p00046589) which is consistent with the general consensus that there is a disposal.

## Tax treatment of crypto

In Australia, a key distinction between crypto and fiat money (like the Australian dollar) is that cryptocurrency and/or crypto assets are viewed as [property](https://www.ato.gov.au/Individuals/Investments-and-assets/Crypto-asset-investments/What-are-crypto-assets-/) rather than a currency by the ATO. This means that the taxation rules for crypto are those which apply to assets more generally and will depend on the nature of the interaction with the crypto asset in question.

To determine whether a taxable event has happened, you will need to consider the client’s purpose for holding the asset. That is, is the client:

* [carrying on](https://www.ato.gov.au/Business/Income-and-deductions-for-business/Crypto-assets-and-business/Crypto-assets-used-in-business/) a crypto asset [business](https://www.ato.gov.au/business/starting-your-own-business/are-you-in-business-/?=banner_home_sec_are_you_in_business)
* investing in crypto assets, or
* holding the crypto purely for personal use?

This consideration will have ramifications on how their activity is treated from a tax perspective.

Depending on the type of transaction, it will give rise to a [taxable](https://www.ato.gov.au/Individuals/Investments-and-assets/Crypto-asset-investments/Transactions---acquiring-and-disposing-of-crypto-assets/) event. Note that the size of your client’s transactions, activity, or level of trading sophistication doesn’t necessarily mean that they are considered a business. The ATO provides a [full list](https://www.ato.gov.au/Business/Income-and-deductions-for-business/Crypto-assets-and-business/Crypto-assets-used-in-business/) of the tax implications of a business using crypto.

The tax treatment of cryptocurrency and/or crypto assets for [personal use](https://www.ato.gov.au/individuals/investments-and-assets/crypto-asset-investments/crypto-as-a-personal-use-asset/) or consumption may be disregarded if it is clear that it was **not** utilised as an investment, to make a profit and/or in the course of carrying on a business.

The ATO has released this [video](https://publish.viostream.com/play/bi9or7odtapk57) which covers the tax treatment of cryptocurrencies and assets.

## Loss, theft of crypto assets and administration of crypto exchanges and platforms

Evidence is required to prove where a crypto asset is lost or stolen to claim a loss. The [ATO guidelines](https://www.ato.gov.au/Individuals/Investments-and-assets/Crypto-asset-investments/Transactions---acquiring-and-disposing-of-crypto-assets/Loss-or-theft-of-crypto-assets/) sets out that proof of ownership is required, as well as proof of the loss or theft. Where a crypto exchange or platform is in administration, no loss is available until the administration is complete. Loss or theft of a crypto asset in this way could give rise to a capital loss but this is quarantined to be offset against capital gains.

## Record keeping

It is important that your clients have retained all records with regard to their cryptocurrency transactions. You may only see your client once a year, accordingly, the record-keeping of your client needs to be clear on the buying, owning and disposing of any assets.

Monitoring the transactions of crypto assets can be difficult. It is important that your client keep evidence of every transaction. The ATO has guidance on [keeping crypto records](https://www.ato.gov.au/Individuals/Investments-and-assets/Crypto-asset-investments/Keeping-crypto-records/).

Clients will need to keep records for each transaction such that each income and/or CGT event can be calculated. This record keeping can be undertaken in a variety of ways, including specialist crypto asset software which will assist in the tracking of:

* Transaction dates
* The [value of the cryptocurrency and/or crypto asset in Australian dollars](https://www.ato.gov.au/individuals/investments-and-assets/crypto-asset-investments/transactions---acquiring-and-disposing-of-crypto-assets/crypto-asset-transactions/?anchor=ValuingcryptoassetsinAustraliandollars#ValuingcryptoassetsinAustraliandollars) at the time of the transaction
* Details of the transaction and the identity of who your client traded with
* Receipts when you buy or transfer cryptocurrency and/or crypto assets
* Exchange records (which can be downloaded directly from the exchange in question)
* Records of agent, accountant, and legal costs
* Digital wallet records and keys
* Software costs that relate to managing your tax affairs.

An important note is that the ATO recommends where possible to keep tangible items that prove your clients’ assertions in case of an audit. For example, clients should hold copies of their transaction history (e.g. a downloaded comma separated values (CSV) file from an exchange such as Binance and bank statements that show the transfer of funds). The more tangible records, the better.

Some exchanges provide their users with CSV formatted documents that aggregate the details of their trading activity. While this is convenient, you and your client will still need to collect details across all platforms they’ve interacted with and confirm that all the necessary data is present. If you do not want to use a crypto tax software provider, you can work with your clients to maintain a manually updated list of their transactions. This would exist in a spreadsheet and would need to have all the aforementioned details on what the ATO considers necessary for record-keeping purposes.

# Pre-meeting client questionnaire

This questionnaire can be sent to clients to gather information and records in preparation for your meeting.

Client questionnaire

|  |  |
| --- | --- |
| Client questionnaire | Notes |
| Please list all the accounts you have used to transact and/or store crypto currency and/or assets.  This includes wallets (cold and hot), exchanges, accounts and any other transaction activity. |  |
| Did you dispose of cryptocurrency or crypto assets?  This includes:   * Selling crypto for fiat currency * Swapping one crypto asset for another crypto asset * Using cryptocurrency for goods and services * Gifting crypto. |  |
| Did you receive income from cryptocurrency or crypto assets?  This includes:   * Getting paid all, or part of, your salary in crypto * Selling NFTs as a creator * Earning interest via yield farming * Earning rewards via liquidity pools * Earning rewards from a play to earn game * Using crypto lending platforms to earn interest * Earning staking rewards * Receiving air drops |  |
| For each transaction, please provide:   * Transaction dates * Value of the cryptocurrency and/or crypto asset in Australian dollars at the time of the transaction * Details of the transaction including the counterparty.   This information is usually available from receipts, exchange records and specialist crypto asset software. |  |
| If you have disposed of cryptocurrency or crypto assets, you may be liable for capital gains tax.  To determine how much you paid for the currency or asset, please provide details and records about your initial purchase. This includes:   * Transaction dates * Value of the cryptocurrency and/or crypto asset in Australian dollars at the time of the transaction * Details of the transaction including the counterparty * Any associated capital expenses such as exchange fees. |  |
| Did you hold crypto assets in an exchange/platform that has been in administration? Have you otherwise suffered a loss or theft of your crypto such as loss/stolen private keys? Please provide details including:   * Proof of ownership and cost of asset * Timing of loss * Timing of administration and if it is completed at year end |  |
| Please provide details and records for your associated expenses. These include:   * Records of agent, accountant, and legal costs * Software costs that relate to managing your tax affairs. |  |
| Have you properly declared your crypto activities in your prior year returns?  If not, would you like advice on how to amend your tax returns. |  |

# Checklist for client meetings

This checklist can be used by tax agents to guide conversation when meeting with your clients:

Step 1: Check whether your client has declared prior-year crypto activities

|  |  |  |
| --- | --- | --- |
| Prior year crypto activities | Y | N |
| Has the client purchased, held, traded or disposed of crypto in prior income years?  If so, inform them of their tax and record-keeping obligations. |  |  |
| Has the client declared all crypto activity as required in the previously lodged tax returns?  If not, inform them of the consequences of incorrect tax returns and advise on their options to amend prior year returns. |  |  |
| Was the disclosure of ordinary income accurate?  Consider checking methods of calculation and review expense claims. |  |  |
| Was the disclosure of capital gains accurate?  Consider checking methods of calculation, including cost base. |  |  |

**Note:** If your clients have traded in previous income years but have not yet declared their trading activity in the respective tax returns, they will need to go back and amend these previous tax returns.

Step 2: Assess the breadth of your client’s crypto activities

|  |  |  |
| --- | --- | --- |
| Current crypto activity | Y | N |
| Has the client disclosed all accounts that have crypto transactions?  Ask for details of accounts including:   * Wallets * Exchanges * Accounts * Other transaction activity.   Inform your client of the consequences of not declaring all accounts and the serious implications on the accuracy of their tax return. |  |  |
| Identify the legal name/s the exchanges and/or wallets are registered under.  This is required for record keeping purposes and to determine tax obligations including transfers of beneficial ownership. |  |  |
| Confirm that the client holds sufficient records of transactions including history.  Advise client about record keeping requirements including time periods and cost base documentation. |  |  |

**Note:** You will need to obtain *all* of your client’s trading history records for an accurate crypto tax return.

**Step 3: Confirm exactly what way your client interacted with crypto**

|  |  |  |
| --- | --- | --- |
| Current crypto activity | Y | N |
| Has your client utilised cryptocurrency and/or crypto assets as:   * An investment * A business * Personal use?   Depending on which category they fall into will affect the tax implications of their trading activity. Read the ATO’s information on [crypto assets](https://www.ato.gov.au/individuals/Investments-and-assets/crypto-asset-investments/what-are-crypto-assets-/).. |  |  |
| Has your client purchased/sold cryptocurrency and/or assets in the financial year?  Determine:   * cost base * revenue - ordinary income and/or capital proceeds * expenses * value in Australian dollars at the transaction date/s. |  |  |
| Has the client transferred cryptocurrency and/or crypto assets between their own wallets? How has this been recorded?  If so, they will need to have the ability to prove ownership over the various wallets. |  |  |
| Has the client received cryptocurrency and/or crypto assets as income/wages?  If so, they will need to declare the value at the time of receipt as ordinary income. |  |  |
| Has your client sent cryptocurrency and/or crypto assets as a gift?  If so, this is considered by the ATO to be a CGT event. |  |  |
| Has the client purchased or sold any non-fungible tokens (NFTs)?  If so, they will need to establish the cost base for future CGT events and/or calculate any CGT on disposals. |  |  |
| Has the client been involved with any NFT creation or minting activities?  If so, they may need to attribute any value gained from NFT creation and sales as ordinary income. |  |  |
| Has your client received any cryptocurrency and/or crypto assets from:   * Airdrops * Chain splits * Forks?   If so, they may need to declare assets earned from these activities as ordinary income. |  |  |
| Has your client participated in any Decentralised Finance (DeFi) activities such as:   * Staking * Yield farming * Mining * Margin trading * Derivatives   If so, they may need to declare assets earned from these activities as ordinary income. |  |  |
| Has the client participated in any Initial Coin Offerings (ICOs)?  If so, they will need to establish the cost base and keep records for future CGT events. |  |  |
| Did your client lose their private key/s?  If so, they may be able to claim any inaccessible funds as capital losses. |  |  |
| Did your client have their private key/s stolen?  If so, they may be able to claim any inaccessible funds as capital losses. |  |  |
| Did your client have their cryptocurrency exchange or trading platform enter an external administration?  If so, they may be able to claim any lost funds as capital losses. |  |  |
| Has your client participated in any metaverse games and earn tokens or other rewards from these activities?  If so, they may have to declare rewards earned from these activities as ordinary income. |  |  |
| Has your client been involved with any crypto gambling activities?  If so, they will need to take cost bases and values into account for future CGT events. |  |  |