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German Tax and Legal News

MOF issues guidance on VAT treatment of virtual currency

The guidance confirms that Germany will not impose VAT on cryptocurrency used as a form of payment.

Germany's Federal Ministry of Finance (MOF) issued guidance on 27 February 2018 that clarifies the VAT treatment of virtual currency, such as bitcoins, in response to a 2015 decision of the Court of Justice of the European Union (CJEU) (C-264/14). The guidance confirms that Germany will not impose VAT on such currency where the virtual currency operates as a substitute for "traditional" currency and is used only as a form of payment.

Background

Article 135(1)(e) of the EU VAT directive provides a VAT exemption for certain transactions involving currency, bank notes and coins used as legal tender; this exemption has been implemented into German domestic law in section 4(8)(b) of the VAT Act.

In its decision dated 22 October 2015, the CJEU held that no VAT is due on the exchange of a "traditional" currency into "bitcoin" (and vice versa), which means that bitcoin receives the same VAT treatment as real currency, i.e. a VAT exemption. Services providing for the exchange of traditional currency in units of bitcoin constitute a supply of services for consideration, but these services are exempt from VAT under article 135(1)(e) of the EU VAT directive.

According to the CJEU, transactions involving virtual currencies should be considered VAT-exempt financial transactions to the extent the currencies have been accepted by the parties to a transaction as an alternative to legal tender and have no purpose other than to serve as a means of payment. To interpret article 135(1) (e) of the VAT directive as covering only transactions involving traditional currencies would deprive it of part of its effect. On this basis, the CJEU concluded that the VAT exemption under the directive covers the supply of services consisting of the exchange of traditional currencies for units of bitcoin, and vice versa.

MOF guidance

In compliance with the principles of judgement and the general explanations on the VAT treatment of virtual currencies which, like bitcoin, are accepted as contractual means of payment between economic operators and which serve no purpose other than their use as means of payment, the tax authorities take position on the exchange of bitcoin, bitcoin "mining," virtual bitcoin wallets, trading platforms and sales relating to other virtual currencies.

According to the guidance, the conversion of traditional currencies into bitcoin (and vice versa) is a taxable service which, within the framework of the VAT directive, is VAT-exempt. The use of bitcoin is equated with the use of a traditional means of payment, provided its only purpose is to function as a means of payment. Bitcoin's dedication to the mere payment of fees is therefore not taxable. Where a payment is made with bitcoin, the fees paid by the service provider generally are determined by the equivalent value in the currency of the EU member state in which the service is provided, and at the time the service is provided. The conversion must take place at the last published selling rate (e.g. on corresponding conversion portals on the internet), which must be documented by the performing contractor.

The MOF guidance clarifies the concept of bitcoin mining. Bitcoin is "mined" (i.e. created) when "miners" use complex algorithms to verify and record transactions in a "block" and then transfer the transactions to a "block chain" (a computer file that operates as a publicly available ledger that contains information on all transactions carried out with the virtual currency). In this way, miners that make their computing power available to the mining pool perform a critical function for transacting in bitcoin. The transaction fees miners can receive from other users of the system are paid voluntarily and are not directly related to the services provided by the

miner. Additionally, remuneration in the form of the receipt of new bitcoin by the system itself is not considered remuneration for the mining services, since those services are not provided within the scope of an exchange of services relationship.

A virtual wallet is software a person can install on a computer, tablet or smartphone to engage in transactions using a virtual currency. According to the MOF guidance, if a provider requires a fee to use a digital wallet, the service is subject to VAT.

In the case of trading platforms, a distinction must be made between a situation where the platform operator merely makes the platform available and where it carries out the purchase/sale of bitcoin as an intermediary in its own name. Where an operator makes a website available to market participants, the acquisition or trading of bitcoin simply enables technical settlement so the VAT exemption clearly is not applicable. However, if the operator of the platform buys and sells bitcoin as an intermediary in its own name, the transaction is VAT-exempt.

The guidance also provides that other virtual currencies will be treated as legal tender if they have been accepted by the parties to a transaction as an alternative contractual and direct means of payment and serve no other purpose than to function as means of payment. Accordingly, the conversion of such virtual currencies into legal tender and vice versa will be VAT-exempt. Virtual gaming money (especially in online games), however, will not be exempt from VAT because it is not a means of payment within the meaning of the VAT law.

Comments
 The VAT treatment of crypto currencies and especially the underlying blockchain technology is still in its early phase, but this technology is expected to revolutionize business and tax practice. The technology also can be used in the form of "smart contracts" that digitize and automate the creation and execution of contracts. This could enable financial administration to make data exchange and payments between companies and authorities more transparent and efficient. Invoicing, in particular, could be improved, as the entire history of the supply chain always can be automatically assigned to an invoice, for example. Fraud could be limited by smart audits, which also would provide more legal certainty with regard to cross-border deliveries.

Legal Norms
 Art. 135 (1) (e) VAT Directive

Reference
Letter of the FMoF dated on 27 February 2018

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