Sars should give crypto investors more carrot and less stick

It has been more than three years since the South African Revenue Service's (Sars') media statement on cryptocurrencies, in which it said that it would apply "normal income tax rules" to cryptocurrencies when assessing whether a gain is revenue or capital in nature, and that crypto assets are not seen as currency for income tax purposes.

Tertius Troost, tax manager, Mazars

Any further guidance from the revenue service has been scarce. “Crypto traders, especially those that have no financial or tax background, often turn to fellow traders on social media platforms for advice (not an advisable option). Based on my interaction with cryptocurrency HODLers (a term referring to buy-and-hold strategies in the context of cryptocurrencies), uncertainty remains with many being surprised when I explain the so-called “normal rules”, which become pretty complicated as the crypto market continues to develop," says Tertius Troost, tax manager at Mazars.

Scarce information

He adds that media outlets, along with Sars commissioner, Edward Kieswetter, have been quick to state that Sars will crack down on non-compliant taxpayers who do not declare their crypto asset profits. “However, many of these taxpayers do not even know that they are non-compliant. So why not provide more guidance to assist taxpayers in declaring their crypto asset profits? The only guidance to date is the previously mentioned media statement along with 15 FAQs on cryptocurrencies hidden away on the Sars website.”

Anecdotally, it seems that Sars still views crypto assets as highly speculative intangible assets “However, it should be noted that exponential change is taking place in this industry since their initial media statement on 6 April 2018. Cryptocurrencies have provided us with various initiatives and businesses that are shaping this alternative financial system. These initiatives include cryptocurrency arbitrage, investments into predefined cryptocurrency bundles, lending and borrowing through the use of decentralised finance (DeFi), staking and mining rewards for solo or pooled staking and mining.”

At a minimum Troost suggests that Sars - together with National Treasury - states that gains (and losses) on crypto assets are deemed to be capital in nature if held for a period of more than one year (similar to section 9C, which provides equity shares to be deemed to be capital in nature after three years). “In this way, Sars can at least assist taxpayers in having certainty in their disclosures. It also assists in bringing taxpayers to Sars, instead of Sars needing to try and find non-compliant taxpayers in a space they are ill-equipped to conquer.”

Transparency

With all tax collection methods, the cost of the collection must be weighed up against the actual amount that can be collected. Providing this form of incentive will encourage taxpayers to disclose their positions and save Sars the cost of finding extremely expensive methods of obtaining this information from markets. Not to mention, the number of devices that Troost has noted that shield this information from authorities.

“For true transparency, Sars should attempt to detail as much of the current crypto transactions they are aware of in an interpretation note. Touching on aspects like the interaction between crypto assets and section 24J (interest), whether crypto to crypto conversions qualify as disposals (in my opinion it does), the rebalancing of crypto bundle investment and whether these should fall within the ambit of a collective scheme of investments, staking rewards that could be argued as being interest and the tax implication of collateralized lending through DeFi.”

Voluntary disclosure

In the meantime, Troost says that if taxpayers have not declared crypto asset profits, it remains advisable to follow the voluntary disclosure programme provided for by Sars. Failing to disclose any relevant amounts could result in substantial penalties and/or harsh criminal sanctions.

“As highlighted by my colleague Wiehann Olivier, digital asset lead at Mazars in South Africa, crypto assets were originally designed to facilitate peer-to-peer transactions across the Internet. This meant that there was no need for any intermediary or monetary regulations, which led people to believe that crypto assets should operate independently from any form of regulation. However, they fail to realise that certain regulations are, in fact, imposed to protect consumers and economic stability,” Troost says.