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THE EFFICACY OF THE EXISTING ANTI-AVOIDANCE PROVISIONS AND CONTROL MECHANISMS IN THE TAX ADMINISTRATION ACT AND INCOME TAX ACT IN RELATION TO THE NATURE AND UTILISATION OF CRYPTOCURRENCIES IN THE CURRENT ECONOMIC CULTURE

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SUMMARY

THE EFFICACY OF THE EXISTING ANTI-AVOIDANCE PROVISIONS AND CONTROL MECHANISMS IN THE TAX ADMINISTRATION ACT AND INCOME TAX ACT IN RELATION TO THE NATURE AND UTILISATION OF CRYPTOCURRENCIES IN THE CURRENT ECONOMIC CULTURE

By

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DEPARTMENT: MERCANTILE LAW

DEGREE: LEGUM MAGISTER (TAX LAW)

This study aims to evaluate the existing anti-avoidance provisions contained in the Tax Administration Act No 28 of 2011 and Income Tax Act 58 of 1962 in relation to cryptocurrencies. The purpose is to evaluate whether the existing anti-avoidance provisions provide adequate means to identify and regulate the use of cryptocurrencies to prevent tax evasion.

Virtual currency is an anonymous and intangible fund which consists of various forms such as centralised and decentralised virtual currency. The technology used to trade cryptocurrencies is called blockchain. This technology requires the users of the cryptocurrencies to verify the transactions which result in an authenticated and trusted transaction.[1]

[1] See Chapter 2 paragraph 2.1.

In this study, the tax regulatory frameworks of cryptocurrencies in the United States of America and Canada are discussed. These countries incorporate two very different approaches in respect of the reporting duties in their respective tax legislation frameworks in an effort to prevent tax evasion. The United States of America incorporated their Currency and Foreign Transactions Reporting Act to regulate cryptocurrencies, whilst Canada introduced the reporting duty in their Income Tax Act.[2]

The existing anti-avoidance provisions in the South African Tax Administration Act and Income Tax Act are examined against the backdrop provided in the study of the regulatory frameworks of the United States of America and Canada. The aim is to determine whether the anti-avoidance provisions in South Africa are sufficient to prevent tax evasion and avoidance.[3]

The premise is that the existing anti-avoidance provisions in the South African legislative framework are insufficient and that a need to incorporate reporting duties, similar to those that can be found in the Financial Intelligence Centre Act 38 of 2001, exist.[4] The new proposed tax amendment bill will also be considered to determine whether it adequately addresses the shortfalls in the current tax legislative framework in relation to cryptocurrencies.[5]

It was concluded that the existing anti-avoidance provisions are insufficient to adequately prevent tax evasion in respect of cryptocurrencies. It is suggested that the South African authorities incorporate a general reporting duty in respect of cryptocurrencies in one of two ways.[6] The first manner to facilitate this reporting duty is to incorporate it in tax regulatory framework. In the alternative, a multi-legislative approach must be considered by amending the Financial Intelligence Centre Act, by broadening its scope of application, to include transactions related to cryptocurrency to prevent tax evasion and tax avoidance.[7]

[2] See Chapter 3 paragraph 3.2 -3.5.
[3] See Chapter 4.
[4] See Chapter 5 paragraph 5.1 and 5.2.
[5] See Chapter 5 paragraph 5.3.
[6] See Chapter 6 paragraph 6.6.
[7] See Chapter 6 paragraph 6.6.

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CHAPTER 1: INTRODUCTION

1.1 BACKGROUND AND RATIONALE FOR THE STUDY

In the modern, borderless world, governments are faced with the challenge to enhance investments and to stimulate economic growth. Cryptocurrency is currently unregulated by most governments around the world which is why it is one of the most prominent investment instruments used by investors. The question that arises, is why control is necessary but more importantly if control is deemed to be necessary how such control will be implemented to optimise the effect thereof without limiting trade and placing a compliance burden on taxpayers.

As at the date of writing this chapter the Bitcoin index was at USD6300.00 which is about R87,164.91. The total value of cryptocurrency traded in approximately 24 hours in USD 13,279,379,539 which equates to R1,8 trillion in South Africa.[1] Considering the value attached to cryptocurrency it is easy to see why the growing interest in the regulation thereof exists.

In March 2018, the managing director of the International Monetary Fund ("IMF") expressed her concern regarding the increasing use of cryptocurrencies as a means to shift value.[2] The IMF indicated that cryptocurrencies pose threats to the international financial market as a vehicle for money laundering and financial crimes, such as tax evasion.[3] The increased use of cryptocurrencies demands regulation by governments.[4] The IMF proposed to combat the threats of cryptocurrencies through the effective use of technology to both regulate and supervise the growing industry of cryptocurrencies.[5] This is to ensure financial stability and integrity in international markets to protect consumers.[6]

1 https://cryptoindex.co/ (accessed on 13 November 2018)
2 Lagarde C (2018) Addressing the dark side of the Crypto World Finance and Development Publications by the IMF available at https://bit.ly/2DpATi1 (accessed on 13 November 2018).
3 Lagarde (2018).
4 Lagarde (2018).
5 Lagarde (2018).
6 Lagarde (2018).

In line with the proposition of the IMF, the then Minister of Finance, Malusi Gigaba, expressed the need for a growing tax regulatory system in the South African 2018 National Treasury Budget Speech presented on 21 February 2018.[7] The minister indicated that the South African National Treasury Department and the South African Reserve Bank are working towards reforming the legislative framework of the financial markets and the payment system.[8] Furthermore, governments will be partnering with entities such as FinTech to design and structure a regulatory framework for new developments such as cryptocurrencies.[9] The rise of cryptocurrencies demands a response from the government in respect of the existing tax framework. The South African legislature responded to the call for draft legislation on 16 July 2018 when the Draft Taxation Legislation Amendment Bill by National Treasury was tabled.[10]

It is clear that a so-called ‘wait and see” approach by governments to regulate cryptocurrencies will not suffice to curb the risks associated therewith. The failure of governments to regulate cryptocurrencies might lead to instability and unreliability of international and domestic markets.[11]

The reason can be found in that value is shifted across international and domestic borders without any means to track and trace these shifts. The uncertainties and risks associated with the regulation of cryptocurrencies should not deter governments from embracing cryptocurrencies as an effective mechanism to increase investment.[12]

1.2 RESEARCH PROBLEM STATEMENT

In the light of the risks posed by cryptocurrencies for financial markets and the increase in tax evasion there exists a need to investigate the existing anti-avoidance provisions to determine whether there is a reporting duty similar to the duties in the Financial

---

[7] 2018 Budget Speech delivered by Minister M Gigaba on 21 February 2018 available at https://bit.ly/2ELuMd2 pg. 21 (accessed on 13 November 2018).
[8] 2018 Budget Speech at 21.
[9] 2018 Budget Speech at 21.
[10] National Treasury Draft Taxation Legislation Amendment Bill https://bit.ly/2zTgWkL (accessed on 12 November 2018).
[11] Lagarde (2018).
[12] Lagarde (2018).

Intelligence Centre Act 38 of 2001 and the Prevention of Organised Crime Act 21 of 1998. Foreign jurisdictions have generally aligned their tax legislation and Acts aimed at money laundering to establish a legal framework for the identification, regulation and taxing of cryptocurrencies.

The research question that arises is whether the existing anti-avoidance provisions in the Income Tax Act 58 of 1962 are sufficient to prevent tax evasion and to limit avoidance structures by means of cryptocurrencies.

1.3 RESEARCH OBJECTIVES

To address the problem statement the following objectives are formulated to answer the research questions.

1.3.1 PRIMARY OBJECTIVE

The primary research objective is to comparatively investigate whether the existing anti-avoidance provisions in the Income Tax Act 58 of 1962 and the Tax Administration Act 28 of 2011 are sufficient in respect of cryptocurrencies.

1.3.2 SECONDARY OBJECTIVES

The following secondary objectives will support the primary research objective:

- A study of the nature of cryptocurrencies and the functionality of the technology;
- Investigating a global view of the legal tender status of cryptocurrencies and the question of whether illegal tender can attract tax consequences. In this regard, the status of cryptocurrency in South Africa will be compared to the position in Canada, Netherlands, United States of America and Russia. The reasons for the

comparison of the aforementioned countries is their interest in the development of regulations pertaining to cryptocurrencies and are summarised as follows:

Canada: The Canadian revenue service completely legalised cryptocurrencies and makes use of so-called “virtual wallets” and “Bitcoin Automated Teller Machines (“ATMs”) in which the user stores the cryptocurrencies. This “virtual wallet’ is regulated and monitored by the Canadian Revenue Service.

Netherlands: A reported judgment in the Supreme Court of Appeal in 2016 pronounced on the legal tender status of cryptocurrencies within the Netherlands. It was held that cryptocurrencies are not legal tender and no merchant is obliged to accept it.

United States of America (with reference to specific case law referenced in the State of Florida): The court held that in circumstances where the legislature has not provided clarity on the method in which cryptocurrencies are dealt with, the defendant cannot be prejudiced; and

Russia: The Russian government is set to release a new bill on the status of cryptocurrencies in and aims to release their own CryptoRuble;

- An investigation into the guidance provided by the United States of America and Canada in their approach to identify and regulate cryptocurrencies to enable their revenue services to tax cryptocurrencies;

- Proposing recommendations on the most suitable approach by the South African Revenue Service to prevent tax evasion and to limit tax avoidance in relation to cryptocurrencies.

1.5 RESEARCH METHODOLOGY

The research will be conducted using a combination of a comparative and doctrinal study.

The regulatory tax framework of cryptocurrency in the United States of America and Canada will be investigated to determine different approaches to the taxation of cryptocurrencies with the aim of identifying the most suitable proposal.

The existing anti-avoidance provisions of South Africa will be investigated using a doctrinal approach considering the language, grammar and context of the provisions and to determine their application to cryptocurrency.

1.6 CHAPTER EXPOSITION

1.6.1 CHAPTER 1: INTRODUCTION

The aim of this chapter is to provide the reader with the context within which the study is conducted. This is aim is achieved by providing a short introduction and rationale for the study. The research methodology applied in the study and objectives is stated. A summary of the research problem is provided to assist the reader to easily conceptualise the existing problem. Finally, the chapter concludes with a brief outline of what is to be expected in each chapter of the study.

1.6.2 CHAPTER 2: THE NATURE OF CRYPTOCURRENCIES

This chapter revolves around the nature of cryptocurrencies. The definition and functionality of the technology are explained. The legal status of cryptocurrencies in South Africa is examined and compared to the position of cryptocurrencies in the

Netherlands, United States of America, Canada, and Russia to provide a global view on the status of cryptocurrencies. The secondary focus of the chapter is if the cryptocurrencies do not enjoy legal tender status, whether as an illegal receipt it may still attract tax consequences.

1.6.3 CHAPTER 3: TAX TREATMENT OF CRYPTOCURRENCIES IN THE UNITED STATES OF AMERICA AND CANADA

In this chapter, the tax regulatory position of cryptocurrencies in the United States of America and Canada is discussed. These countries incorporate reporting duties in their respective tax legislation in two very different approaches. The United States incorporated their Currency and Foreign Transactions Reporting Act,[13] to regulate cryptocurrencies, whilst Canada introduced the reporting duty in their Canadian Income Tax Act.[14]

1.6.4 CHAPTER 4: EXISTING ANTI-AVOIDANCE PROVISIONS IN THE INCOME TAX ACT

The focus in this chapter is on the existing anti-avoidance provisions of South Africa to provide an understanding of how it currently operates to prevent tax evasion. The main principles related to tax evasion and avoidance are discussed. The new proposed tax amendment bill will also be considered to determine whether it adequately addresses the shortfalls in the current tax legislative framework in relation to cryptocurrencies.

[13] Currency and Foreign Transactions Reporting Act of 1970 31 of USC 5311.
[14] Canadian Income Tax Act R.S.C. 1985, c. 1 5th Supp.

1.6.5 CHAPTER 5: REPORTING DUTIES IN OTHER LEGISLATION DEALING WITH ONLINE TRANSACTIONS

This chapter focusses on the South African position in relation to cryptocurrencies and the tax legislative framework. The premise is that the existing anti-avoidance provisions in the South African legislative framework are insufficient and require a need to incorporate reporting duties similar to those that can be found in the Financial Intelligence Centre Act 38 of 2001.

1.6.6 CHAPTER 6: CONCLUSION

This chapter concludes the study by indicating the findings of the study, the conclusions drawn, and the recommendations proposed.

CHAPTER 2: THE NATURE AND FUNCTIONALITY OF CRYPTOCURRENCIES

In his opening address to the Senate Homeland Security Committee in the United States of America on 18 November 2013, Senator Thomas Carper accurately describes the position relating to cryptocurrencies when he stated that "[v]irtual currencies, perhaps most notably Bitcoin, have captured the imagination of some, struck fear among others, and confused the heck out of the rest of us".[1]

The focus in this chapter is to describe the nature and function of cryptocurrencies and to determine its status among other tenders. It is imperative that the reader first understands what cryptocurrency is and how the technology function, before the possible regulation thereof can be investigated.

2.1 THE DEFINITION AND FUNCTION OF CRYPTOCURRENCIES

The investigation into the nature and operation of cryptocurrencies starts with the consideration of its definition.

The Financial Action Task Force ("FATF") in its paper on Key Definitions and Potential AML/CTF in 2014 defined virtual currencies as a digital representation of value that can be traded on an electronic platform but does not have legal tender status in any jurisdiction.[2]

The FATF categorised virtual currencies into two groups namely convertible and non-convertible virtual currency. The difference between the two groups relates to the virtual currency's ability to convert into real currency.[3] On the one hand, convertible virtual currency has an equivalent in real money. Bitcoin is the most renowned convertible virtual currency. On the other hand, non-convertible virtual currency is intended for a specific community and the governing rules of this community does not

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[1] Viswanatha A (2013) U.S. Officials: virtual currencies vulnerable to money laundering at https://reut.rs/2ruSb9X (accessed on 5 December 2018).
[2] Financial Action Task Force (FATF) Paper on Key Definitions and potential AML/CTF 2014 pg. 4.
[3] FATF (2014) pg. 4.

allow the exchange of the virtual currency into real money.[4] An example of a non-convertible virtual currency is World of Warcraft gold coins that players can use for in-game purchases.

Once a virtual currency is categorised into one of the above groups, it is further classified as centralised or decentralised virtual currency. The difference between a centralised virtual currency and a decentralised virtual currency is whether an administrative body governs the virtual currency. Centralised virtual currency has a single administrative body which governs the use of the virtual currency. An example of centralised virtual currency is PayPal, which is a mechanism to transfer accepted currencies. Centralised convertible currency is accepted as currency since it is exchangeable for cash and is regulated by the financial institutions.[5]

Decentralised virtual currency does not have a centralised administrative framework. It is math based, peer-to-peer and functions on blockchain encryptions.[6] Decentralised virtual currencies are not redeemable as cash but may be traded for cash. This means that the user may trade it for consideration, but the decentralised virtual currency cannot be redeemed at a bank for cash. This is an important distinction because it relates to the determination of the value of the virtual currency.[7]

Decentralised virtual currencies are referred to as “cryptocurrencies” since it is protected by cryptography and blockchain encryptions. It relies on public and private keys to transfer value from one person to another. Each transaction must be cryptographically signed.

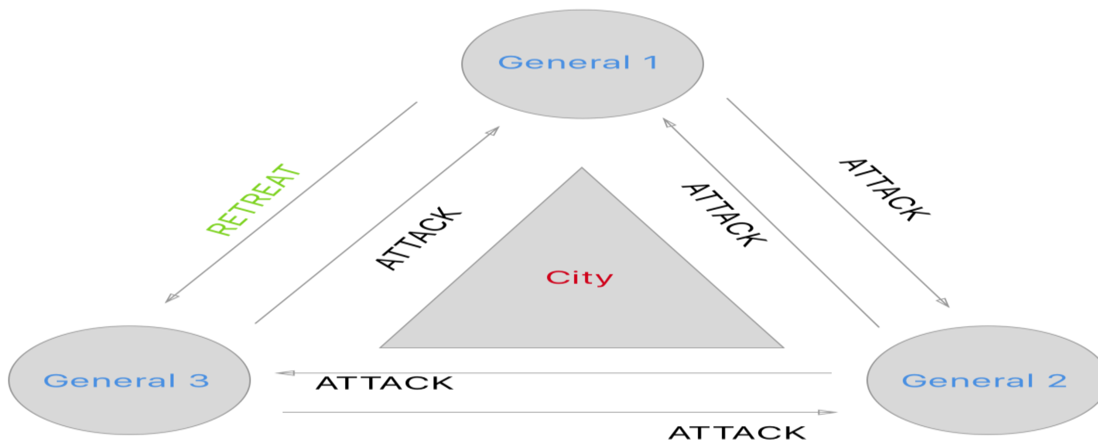
In a Position Paper published in 2014, the South African Reserve Bank (“SARB”) accepted the definition of virtual currency as defined by the FATF. The SARB indicated that it does not regulate or supervise the virtual currency platform and that the use of virtual currency is at the individual’s own expense and risk.[8] The South African National Treasury issued a User Alert dated 18 September 2018 titled “Monitoring of virtual currencies” in terms whereof virtual currency is defined as “…a unit of account

[4] FATF (2014) pg. 4-5.
[5] A Niemand (2015) PER 18 No 5: A few South African cents; worth on Bitcoin pg. 1984.
[6] FATF pg. 5.
[7] Niemand (2015) pg 1984. FATF 1 at pg. 5.
[8] South African Reserve Bank (SARB) 2014 Position paper pg. 12.

that is digitally or electronically created or stored. Members of the virtual community agree to accept the units as a representation of value in the same way that currency is accepted."[9] The aforementioned definition is important since it hints at the so-called Byzantine Fault Tolerance System which is discussed below. To identify the risks involved in virtual currencies and especially cryptocurrencies, one must understand the working of the blockchain encryptions cryptocurrencies.

To understand the need for cryptocurrency one must consider the olden Diner's Club credit cards. The need for a cash-free society started with the 1960's Diner's Club Credit Card which was the first international credit card that was used. Society demanded a sort of internet cash which was instant and untraceable like normal cash. It is for this need of "internet cash" that is both instant and untraceable that Cryptocurrencies was designed.[10]

The problem is what the computer sciences call the "Byzantine Fault Tolerance" also known as the "Byzantine Generals Problem". The Byzantine Generals Problem refers to a situation where multiple parties must execute the same act to avoid the failure of the system.[11] As illustration hereof imagine a city surrounded by a group of generals and their troops. The generals must decide whether to attack or retreat.



9 South African National Treasury User Alert 18 September 2014 "Monitoring of virtual currencies" pg. 1-2.

10 Your World Explained Episode 5 "Cryptocurrency" Netflix Studios aired 6 June 2018 produced by Frank Matt and Edited by Nora Tenessen.

11 Konstantopoulos G (2017) *A Medium Corporation* "Understanding Blockchain Fundamentals, Part 1: Byzantine Fault Tolerance" at https://bit.ly/2FFLfAl (accessed on 17 September 2018). See also *Coin Central* "What is the Byzantine Generals Problem" at https://bit.ly/2PmK0pp (accessed on 17 September 2018).

Source: www.medium.com

There must be consensus on the battleplan or else they are all bound to fail. The difficulty is that the generals cannot trust each other to follow the same plan, similar to internet users who cannot trust one another.[12] To ensure that everyone follows the same battleplan, the plans are routed to a central authority. Likewise, if you purchase an item on Takealot, Takealot verifies with your bank that you are good for the money.[13]

The blockchain technology solves this problem of trust over the internet. This is done through the verification process that each transaction undergoes. “Blockchain” is a public ledger of all transactions ever processed, like ledgers that banks have.[14] The ledger is distributed between computers all around the world that automatically dates and verifies the ledger. Therefore, if the Byzantine Generals recorded their battleplans on a blockchain every general would have a copy of the others’ battleplans which is up to date and verified.[15]

The blockchain is maintained by “miners” of the cryptocurrencies who voluntarily verify the ledger and the system issues the cryptocurrencies as a reward.[16] The verification is the cryptography which protects the authenticity of the transactions. Thus, each user has control over the sending and the receiving of cryptocurrencies.[17] The simplest manner to explain how the transactions are verified is by way of the following schematic depiction:

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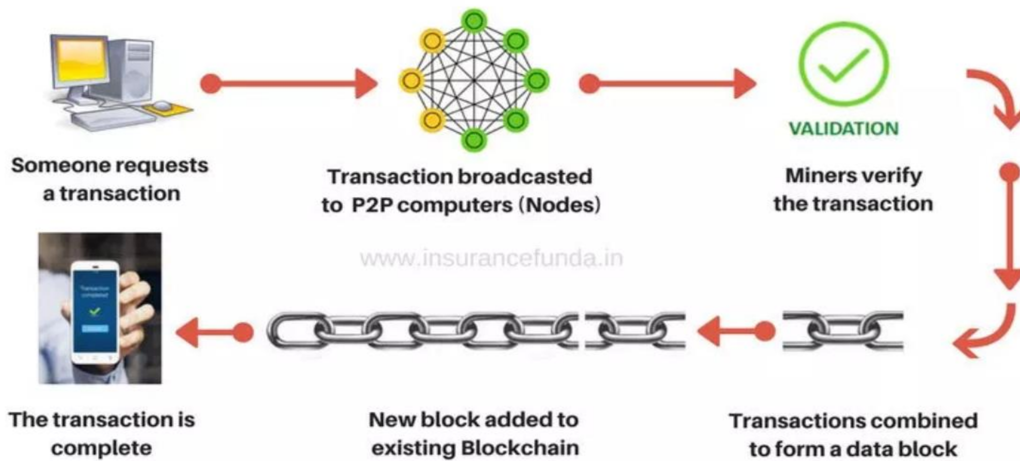
[12] Konstantopoulos (2017).
[13] Konstantopoulos (2017).
[14] Konstantopoulos (2017) and Niemand (2013) at 1986-1988.
[15] Konstantopoulos (2017).
[16] Konstantopoulos (2017).
[17] Niemand (2013) at 1986-1988.



Source: https://insurancefunda.in/bitcoin-cryptocurrency/

Therefore, every request sent has a specific identifying algorithm which is unalterable. The miners verify the algorithm and add a new data block to the transaction link. Every time the transaction is verified a new "block" is added which is required for the authenticity of the transaction. Every request for a transaction and every receipt is verified by the miners who in turn receive a cryptocurrency.

2.2 DOES CRYPTOCURRENCY ENJOY LEGAL TENDER STATUS?

The obligation to accept cryptocurrencies means that it will enjoy the same status as real money. Consequently, courts will be competent to award payment in cryptocurrency for claims such specific performance, damages as a result of delict or breach of contract or insurance pay-outs. This poses many difficulties, for example, how will the value be determined for payment in terms of a court order, will the receipt of the cryptocurrency be included or excluded in the taxpayer's gross income?

In what follows the status of cryptocurrency as legal tender in various countries are considered. The aim is to provide a global perspective on the legal tender status of cryptocurrencies.

2.2.1 NETHERLANDS

The question of whether payment of damages in cryptocurrency and more specifically Bitcoin may be ordered was considered in the Dutch courts in 2014 and 2016. In the Dutch Court Case 2014 in Court of Overijssel,[18] the Plaintiff and the Defendant signed an agreement for the sale and purchase of 2750 Bitcoins for €22,137.50. The Defendant only delivered 990 Bitcoins. The Plaintiff claimed €14,168.00 for the cancellation of the agreement and €132,792.00 worth Bitcoins as damages.[19] The court held that the Plaintiff was entitled to claim for the breach of contract, however, the court held that Bitcoin does not qualify as legal tender in the Netherlands and as such the court cannot award payment in Bitcoin.[20]

The Plaintiff in the Dutch Court Case of 2014 appealed the decision by the Court of Overijssel to the Court of Appeal Arnhem-Leeuwarden in 2016. In the Dutch Court Case on Appeal,[21] the Appellant claimed that the Respondent should be ordered to pay damages by delivering 1,760 Bitcoins. The Court of Appeal held that the general rule is that compensation for damages is payable in cash. The Court of Appeal held that Bitcoin is not accepted as legal tender and that special circumstances which allow the payment of compensation in something other than cash had to be present.[22] The court expressly stated that there exists no obligation to pay in Bitcoin.[23] The appeal was dismissed, and the appellant was ordered to pay the costs.[24] The key principle is that the Netherlands do not accept virtual currencies as legal tender and there exists no obligation to pay or to accept payment in the form of virtual currency.

The question is what is regarded as “accepted currency”. The current global perspective is that only coins and notes issued from the bank of a specific country or

[18] Court of Overijssel with case number C / 08/140456 / HA ZA 13-255 dated 14 May 2014 at https://bit.ly/2rn5Xer (accessed on 12 February 2018). The details of this court case have been anonymised in terms of the Anonymisation Guidelines published in accordance with Article 1 of the Personal Data Protection Act. For ease of reference I will refer to the case as the “Dutch court case of 2014” and the “Dutch court case on appeal 2016”.
[19] The Dutch court case 2014 pg. 1-4.
[20] The Dutch court case 2014 pg. 5-7.
[21] Court of Appeal Arnhem-Leeuwarden with case number 200.155.040 dated 31 May 2016 at https://bit.ly/2EdRSIJ (accessed on 26 April 2018).
[22] The Dutch court case on appeal 2016 par 4.4.
[23] The Dutch court case on appeal 2016 par 4.6.
[24] The Dutch court case on appeal 201622 par 5.

from a country whose jurisdiction is recognised are regarded as legal tender. This is evident from the legislative framework in the United States of America, Canada, Russia and South Africa.

2.2.2 UNITED STATES OF AMERICA

The United States Department of Treasury Financial Crimes Enforcement Network in its paper titled "Application of FinCEN's Regulations to Persons Administrating, Exchanging, or Using Virtual Currencies" dated 18 March 2013 defines currency as "coin and paper money of the United States or any other country that is designated as legal tender and that circulates and is customarily used and accepted as a medium of exchange in the country of issuance."[25]

In the matter of *The State of Florida v Michell Abner Espinoza* the Defendant used Bitcoin in a money laundering swindle.[26] The Circuit Court of Florida held that although Bitcoin shares attribute with real currency, it should be distinguished from real currency. The court warned that although Bitcoin may be exchanged for items of value it is not often used as a means of exchange. The court held that there is no obligation on merchants to accept it. The court cautioned that the volatility of Bitcoin creates uncertainty and limits its ability to act as a store of value. The court held that Bitcoin still has a long way to go before it can be the equivalent of money.[27]

2.2.3 CANADA

The Canadian Currency Act,[28] defines the concept of legal tender in section 8. There are two types of legal tender namely the Canadian coins and the notes issued by the

[25] US Department of Treasury Financial Crimes Enforcement Network: "Application of FINCEN's Regulations to Persons Administrating, Exchanging, or Using Virtual Currencies" 18 March 2013 pg. 1.
[26] The *State of Florida v Michell Abner Espinoza* (2016) case number F14-2923 Criminal Division in the Circuit Court of the Eleventh Judicial Circuit in and for Miami-Dade County, Florida at pg. 6.
[27] *Espinoza* pg. 5-6.
[28] Canadian Currency Act C52 of 1985.

Bank of Canada. Virtual currency is not issued in terms of the Canadian Currency Act and is not recognised as legal tender. This, however, does not exclude the tax liability that the use of virtual currency may attract.[29]

2.2.4 RUSSIA

Article 27 of the Russian Federal Law on the Central Bank of the Russian Federation states that the Russian Rouble is the official monetary unit. The issuance of any other monetary units or quasi-money is prohibited. Article 29 states that the Russian banknotes and coins shall be the only legal tender in the Russian Federation.

2.2.5 REPUBLIC OF SOUTH AFRICA

Section 14 of the SARB Act 90 of 1989 states that the SARB has the sole right to issue banknotes and coins. The current legal tenders issued by the SARB are set out in section 17 of the Act. Legal tender in South Africa are –

a) banknotes issued by the SARB or another bank for which the SARB has assumed liability;[30] and

b) coins issued by the SARB or gold coins (such as Krugerrands) for which the bank is prepared to buy the gold coin.[31]

Therefore, virtual currencies are not statutorily regarded as legal tender in South Africa and the SARB has warned users thereof not to use it as payment for the discharge of an obligation in a manner that suggests that they are suitable of legal tender status.[32]

[29] This aspect is more fully discussed in Chapter 3.
[30] Section 17(1) of the SARB Act 90 of 1989.
[31] Section 17(2) of the SARB Act 90 of 1989.
[32] South African National Treasury User Alert pg1-2.

2.3 CAN AN ILLEGAL RECEIPT ATTRACT A TAX LIABILITY?

The fact that cryptocurrencies are not accepted as legal tender and there exists no obligation to accept it as value prompts the question of whether it can be regarded as an illegal receipt. An illegal receipt commonly occurs in two circumstances. The first is where the benefit is illegal in nature, such as uncut diamonds. Secondly, the manner in which the benefit was obtained is illegal, such as money laundering schemes. Considering that cryptocurrencies in itself are not illegal, and the trading thereof is not prohibited, it will not be regarded as an illegal receipt.

Since cryptocurrencies are not regarded as legal tender but cannot be considered an illegal receipt, the question arises, what will trigger the tax liability? Before considering the question of what constitutes the trigger of the tax liability two important aspects need to be highlighted. Firstly, even though cryptocurrencies are not legal tender it does not mean that a common law agreement where cryptocurrencies are the subject of performance is unlawful and invalid. Cryptocurrencies can, therefore, be the subject of a lawful and enforceable agreement. Secondly, the converse is also true being that where the performance of an agreement is fulfilled, and cryptocurrencies were the subject of performance, the receipt thereof is not unlawful. To determine the trigger of the tax liability in respect of cryptocurrencies it is submitted that the principles related to illegal receipts can be *mutatis mutandis* applied.

In what follows it will be shown why using the tax principles related to illegal receipt, can be utilised as an appropriate trigger for the tax liability caused by a lawful agreement of which cryptocurrencies are the subject of performance. The issue of the taxability of illegal receipts was historically thoroughly canvassed in the South African jurisprudence.

In the case of *MP Finance Group CC (in liquidation) v CSARS*[33] the taxpayer conducted an illegal pyramid scheme by creating successive entities and promised the investors returns of ostensible amounts. Some of the investors did receive some returns before the scheme collapsed.[34] The question was whether the illegal receipt

[33] *MP Finance Group CC (in liquidation) v CSARS* 2007 5 SA 521 (SCA).
[34] *MP Finance Group CC* at 522.

of monies in terms of the pyramid scheme was taxable in terms of section 1 of the Income Tax Act as 'gross income'. The court held that from the facts an intention to enter a legally binding contractual relationship existed and to receive the money for its own benefit. Thus, an illegal contract is not without legal and fiscal consequences. The receipts of the taxpayer did, in fact, fall within the ambit of section 1 and that the assessments were correct.[35]

The important principle that should be extracted, for purposes of this dissertation, from the *MP Finance Group CC*-case is that the intention to enter into a contract is decisive.[36] Therefore, even if there exists no obligation to pay in virtual currency, the contract may still be enforceable. The issue that might arise is whether a court will be competent to order payment in terms of cryptocurrencies. There should however not be any doubt that the courts are competent to enforce a contract in which cryptocurrency is the subject matter. This interpretation is in line with the principles applied in the Dutch Court Case on Appeal 2016.

It is further not necessary for the trading of virtual currency to be ruled as legal for the receipt thereof to be taxable. In *CIR v Delagoa Bay Cigarette Co Ltd,*[37] the taxpayer operated an illegal lottery and sold cigarettes at an amount much higher than the normal selling price.[38] The court held that the question whether the taxpayer's business is legal or illegal is not material in determining whether the receipts are subject to tax.[39] Muller,[40] opines that the correct approach is that a taxpayer who is not entitled to a receipt or accrual but who intends to benefit therefrom should be taxed.[41]

The principle in the *Delagoa Bay Cigarette Co Ltd*-case was also applied in the case *ITC* 1545,[42] where the taxpayer was buying and selling uncut stolen diamonds. The

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[35] *MP Finance Group CC* at 523.
[36] Olivier L "The Taxability of Illegal Income" 2008 4 *TSAR* 814-819 at 819.
[37] *CIR v Delagoa Bay Cigarette Co Ltd* 1918 TPD 391.
[38] *Delagoa Bay Cigarette Co Ltd* pg. 394.
[39] *Delagoa Bay Cigarette Co Ltd* pg. 398. See also Classen LG "Legality and Income Tax - Is SARS 'Entitled to' Levy Income Tax on Illegal Amounts 'Received by' a Taxpayer?" 2007 *SA Merc LJ* 534-553 at 546. See also Olivier (2008) at 816.
[40] Muller E "The Taxation of Illegal Receipts: A Pyramid of Problems! A discussion on ITC 1789 (Income Tax Court – Natal)" 2007 *Obiter* 166-181.
[41] Muller (2007) at 177.
[42] *ITC 1545* 54 SATC 464.

taxpayer knew the diamonds were stolen.[43] The court held that proceeds from an illegal activity can have tax consequences and the taxpayer received the illegal proceeds for his own benefit.[44]

SARS published an interpretation note regarding the issue of whether illegal receipts can have tax consequences.[45] According to this interpretation note, the issue is not whether the victim of a scheme intended to part with the money or property. The issue is whether the thief intended to benefit from the money or property.[46] The same analogy can be drawn with cryptocurrencies. The issue is whether the cryptocurrency user intended to benefit from the virtual currency in a manner that is subject to tax. Once the cryptocurrency user benefitted or had the intention to benefit from the cryptocurrency, it will be subject to tax and subject to legislative framework regarding the anti-avoidance rules.

The Canadian Financial Consumer Agency ("CFCA") issued a notice in which it states that cryptocurrencies are not regarded as legal tender but that the normal rules of taxation are applicable to cryptocurrency transactions.[47] The CFCA indicated that the normal tax rules are applicable to digital currency transactions including cryptocurrencies. This means that digital currencies are subject to the Canadian Income Tax Act and the receipt of cryptocurrency or goods purchased must be included in the seller's income for tax purposes.[48]

Like the Canadian position, SARS indicated on 6 April 2018 that the normal tax rules apply to cryptocurrencies despite cryptocurrencies not being regarded as legal tender as it possesses a value and it is subject to tax.[49] Therefore, the cryptocurrency user benefits from the cryptocurrency since it has a value, and coupled with the intention to benefit as laid down in case law, the cryptocurrencies will be subject to the provisions

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[43] *ITC 1545* pg. 468.
[44] *ITC 1545* pg. 468.
[45] CSARS' Interpretation note 80 dated 5 November 2014.
[46] CSARS' Interpretation note 80 dated 5 November 2014 pg. 14-15.
[47] Financial Consumer Agency of Canada: Digital currency 12 February 2018 pg. 2.
[48] Financial Consumer Agency of Canada: Digital currency 12 February 2018 pg. 2-3.
[49] CSARS' Stance On The Tax Treatment Of Cryptocurrencies- 6 April 2018 http://www.sars.gov.za/Media/MediaReleases/Pg.s/6-April-2018---SARS-stance-on-the-tax-treatment-of-cryptocurrencies-.aspx (accessed on 28 April 2018).

of the South African Income Tax Act 58 of 1962 and the Tax Administration Act 28 of 2011.

The statement of SARS on 6 April 2018 prompts the question of whether the current legislative framework relating to tax evasion is sufficient to deal with cryptocurrencies. It is trite that legislation should always be clear and unambiguous to be effective.[50]

In the *Espinoza*-case the Circuit Court of Florida in the United States the court stated that it is "unwilling to punish the man for selling his property to another when his actions fall under a statute that is so vaguely written that even legal professionals have difficulty finding a singular meaning."[51] Thus, when considering the legislative framework for virtual currency care must be taken to ensure that the legislation is clear and unambiguous.

2.4 CONCLUSION

Considering the above the following conclusions is drawn which is relevant for the investigation into to the regulation of cryptocurrencies:

a) Cryptocurrency is based on a trusted and verified blockchain encryption which means that the regulation thereof can be based on the information sourced from the encryption. A possibility to be investigated is whether a second blockchain can be used by SARS to determine whether a transaction has taken place.

b) Cryptocurrency is anonymous which may pose several difficulties in determining the identity of the ultimate taxpayer. In this regard a similar approach as in the FICA legislation should be considered to create a reporting duty or to extend the current reporting duty in the tax legislative framework, coupled with excessive penalties as an incentive to report the transactions.

c) Cryptocurrencies are not regarded as legal tender which means that there is no obligation on merchants to accept it as payment. SARS has indicated that despite

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50 *Natal Joint Municipal Pension Fund v Endumeni Municipality* 2012 (4) S 593 (SCA) par 18.

51 *Espinoza* pg. 7-8

cryptocurrencies not having legal tender status it will be subject to a tax liability. This means that the anti-avoidance principles will have to be applied to the cryptocurrencies. The extent of the liability to pay tax on the cryptocurrency is outside the scope of this dissertation

CHAPTER 3: REGULATION AND IDENTIFICATION OF CRYPTOCURRENCIES

As shown in the preceding paragraphs, there are concerns and fears from both the public and private spheres with regard to the nature and the consequences of Cryptocurrencies. The countermeasure to the fears and dangers alluded to above is proper regulation of cryptocurrencies by governments. This chapter deals with the way the United States of America and Canada apply regulation to temper the fears raised by the public and private spheres. As a point of departure, one must first consider the dangers of cryptocurrencies to fairly assess the efficiency of the regulatory framework used by the aforementioned countries.

This chapter firstly deals with the dangers associated with cryptocurrencies. Secondly, the tax regulatory position of the United States of America in respect of cryptocurrencies is considered. Finally, the tax treatment of cryptocurrencies in Canada is considered.

3.1 THE DANGERS ASSOCIATED WITH CRYPTOCURRENCIES

The first danger of virtual currency is the uncertainty linked to it. There is not a general acceptance of cryptocurrency among global government which leads to uncertainties among investors.[1] The growth of virtual currencies is also uncertain since it does not have an inherent value such as gold and it is also not linked to a known commodity.[2] The growth of virtual currency is dependent on the number of users.[3]

The second danger of virtual currency is its lack of regulation by governments. The lack of regulation means that it is subject to risks associated with credit abuse, fraud and money laundering. This means that there is a constant threat in cybersecurity.[4] By regulating virtual currencies governments can implement necessary tax legislation

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1 NA Plassaras Chicago Journal of International Law (Vol 14) (2013) “Regulating Digital Currencies: Bringing Bitcoin within the reach of the IMF” 377 pg. 390.
2 Plassaras (2013) pg. 390.
3 Plassaras (2013) pg. 390.
4 Plassaras (2013) pg. 390.

to avoid damage to their fiscus, anti-money laundering legislation to prevent cybercrimes and the use of virtual currency within the illicit substance markets.

The third danger of virtual currency is network externalities, meaning that the benefit of virtual currency is dependent on the number of users thereof.[5] There is no benefit to virtual currencies if merchants do not accept payment in virtual currencies. This is closely linked to the danger of uncertainty referred to above.

3.2 REGULATION IN THE UNITED STATES OF AMERICA

There are mainly two manners in which virtual currencies can produce income and be subject to income tax levied by the United States government taxes income.[6] The first is the buying of cryptocurrencies when the market value is low and then selling the virtual currency when the market value is high.[7] The second manner in which cryptocurrencies can produce income is by using it as a payment method to merchants.[8] The unregulated status of virtual currencies means that there is a risk of tax evasion.[9] The United States Government has several means to identify and track virtual currency like the Bank Secrecy Act coupled with the IRS and FinCEN Regulations.

The United States adopted the Currency and Foreign Transactions Reporting Act of 1970, also known as the Bank Secrecy Act ("BSA").[10] The BSA is aimed at preventing money laundering and tax evasion.[11] The BSA requires money transmitters to register as Money Services Businesses ("MSB").

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[5] Plassaras (2013) pg. 390.
[6] M Kieng-Meng Ly (2014) 27 "Coining Bitcoin's Legal Bits: Examining the Regulatory Framework for Bitcoin and Virtual Currencies" Harvard Law Journal and Technology 587 pg. 595
[7] Kieng-Meng Ly (2014) 595.
[8] Kieng-Meng Ly (2014) 595.
[9] Kieng-Meng Ly (2014) 595.
[10] Currency and Foreign Transactions Reporting Act of 1970 31 of USC 5311.
[11] Currency and Foreign Transactions Reporting Act of 1970 31 of USC 5311, Chapter 2 Title 12, S121(a). See also J Gatto and E Broeker The Ohio State Entrepreneurial Business Law Journal (Vol 9.2) (2015) "Bitcoin and Beyond: Current and future regulation of virtual currencies at pg. 430.

A money transmitter is a natural or juristic person who provides “money transmission services” or transfers funds.[12] The term “money transmission services” “means the acceptance of currency, funds, or other value that substitutes for currency from one person and the transmission of currency, funds, or other value that substitutes for currency to another location or person by any means.”[13] Therefore, if a person accepts any value that substitutes real currency, such as Bitcoin and transmits that value he or she may qualify as a money transmitter.[14]

3.3 FINCEN REGULATIONS

On 18 March 2013, the Financial Crimes Enforcement Network (“FinCEN”) issued a guidance notice in respect of the BSA provisions and regulations and virtual currencies.[15] The FinCEN Regulations defines a “person” as “an individual, a corporation, a partnership, a trust or estate, a joint stock company, an association, a syndicate, joint venture, or other unincorporated organization or group, an Indian Tribe…and all entities cognizable as legal personalities”.[16] The FinCEN Guidance Notice applies to all persons who are using, exchanging or administrating virtual currencies. FinCEN differentiates between a “user” of virtual currency and an “exchanger” or “administrator”.[17] A “user” of virtual currency is not regarded as a money service business (MSB) and therefore need not comply with the registration requirements of the BSA. All ‘exchangers” and “administrators” of virtual currencies are regarded as MSB’s and are required to comply with registration and recordkeeping requirements.[18] It is important to note that the FinCEN Regulations only apply to convertible virtual currencies.[19]

[12] Section 1010 (ff) of the Currency and Foreign Transactions Reporting Act of 1970 31 of USC 5311 (“CFR”). See also Gatto and Broeker (2015) pg. 431.
[13] Section 1010.100(ff)(5)(i)(A) CFR.
[14] Section 1010 (ff) CFR. See also Gatto and Broeker (2015) at pg. 432.
[15] FinCEN-2013-G001 “Application of FinCEN’s Regulations to Persons Administering Exchanging or Using Virtual Currencies.
[16] 31 CF 1010.100(mm) CFR.
[17] FinCEN-2013-G001 pg. 1.
[18] FinCEN-2013-G001 pg. 1.
[19] FinCEN-2013-G001 pg. 1.

A "user" for purposes of the FinCEN Regulations is any person that obtains or receives a virtual currency to purchase goods or services. [20] An "exchanger" is a person who engages in the trading of virtual currencies and whose business relates to the conversion of virtual currencies into real currency. Finally, an "administrator" is a person who issues the virtual currencies and who was the authority to redeem virtual currency.[21]

The guidance specifically deals with three subjects in an attempt to provide clarity on the treatment of these subjects.

3.3.1 "E-PRECIOUS METALS AND E-CURRENCY"

This activity relates to the trading in virtual currencies by a dealer or broker between a customer of such dealer or broker and a third party.[22] It is important to note that the third party, such as the broker, is not required in the transaction of the sale and purchase of the currency. An example will be to allow the transfer of funds between a customer's account and another customer's account. The action described will fall within the ambit of a "money transmission" and the dealer and broker will be required to register as an MSB.[23] Thus, where a person deals in cryptocurrency on behalf of someone else and manages different ledgers on behalf of another, he will be in the business of money transmission and be required to register as an MS and comply with the registration and recordkeeping requirements.[24]

3.3.2 "CENTRALISED VIRTUAL CURRENCY"

One must be reminded that centralised virtual currency has a single administrative repository for example PayPal. The administrator of the repository is a money

[20] FinCEN-2013-G001 pg. 1.
[21] FinCEN-2013-G001 pg. 1.
[22] FinCEN 2013-G0001 pg. 3.
[23] Ficen-2013-G0001 pg. 4.
[24] FinCEN-2013-G001 pg. 3-4.

transmitter since it allows for the transfers of funds.[25] The purchase of an item who pays through PayPal will deposit the money into PayPal who will, in turn, make payment to the seller. The administrator thus acts as an intermediary which triggers the provisions of the BSA and the administrator must register as an MSB.

The exchanger will also be considered an MSB if it exchanges the virtual currency into real currency and vice versa for purposes of the administration of the virtual currency.[26] Therefore, if a purchaser uses centralised convertible virtual currency to pay for an item using PayPal and the seller only accepts real currency, PayPal will appoint an exchanger to exchange the virtual currency to real currency and then pay the real currency value to the seller. Therefore, both PayPal and the appointed exchanger will qualify as money transmitters and be subject to the BSA.

The activities of exchangers of virtual currency can take on two forms namely the transmission to another location and the transmission to another person.[27] The transmission to another location involves the exchanger acts as the seller of the virtual currency and accepts real currency from a user. The exchanger transmits the real currency's value to fund the user's virtual currency account with the administrator. The exchanger is involved in "money transmission services" and subject to the BSA. [28]

The transmission to another person involves the exchanger who accepts currency from a user and privately credits the user's virtual currency account held by the administrators. This activity by the exchanger will be regarded as "money transmission services".[29]

3.3.3 "CRYPTOCURRENCIES"

As stated above, the person that creates the virtual currency and purchases goods and services is a "user" of virtual currency and not an MSB. If a person, however,

[25] FinCEN-2013-G0001 pg. 4.
[26] FinCEN-2013-G0001 pg. 4.
[27] FinCEN-2013-G0001 pg. 4.
[28] FinCEN -2013-G0001 pg. 4.
[29] FinCEN-2013-G0001 pg. 5.

creates the virtual currency and sells it to another for real currency he or she is engaged in money transmitting services and subject to the BSA. [30]

From the above it is clear that the BSA read with the FinCEN regulations creates a reporting duty on persons actively involved as exchangers and administrators of virtual currency. This is important since this reporting duty will enable the Internal Revenue Service (IRS) to trace users, exchangers and administrators of virtual currency allowing them to collect the appropriate tax.

The advantage of a reporting duty created in alternative legislation is that the application thereof can be generalised. For instance, if the reporting duty was created in terms of the IRS laws and regulation it will be limited in its application. By creating the reporting duty in the BSA, the provisions of the BSA relating to the avoidance of money laundering and fraud is also applicable to virtual currencies.

In the State of New York, the Department of Financial Services supervises money transmitters. The department supervises persons engaging in virtual currency transactions by requiring that the user obtain a mandatory "Bit licence". The licence requirement is similar to the requirement to obtain a licence as a money transmitter.[31] This means that exchangers and administrators will be required to comply with the reporting and recordkeeping requirements of the BSA.[32]

FinCEN has issued three administrative rulings to clarify the regulatory treatment of virtual currency. In what follows these administrative rulings are briefly discussed.

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[30] FinCEN-2013-G0001 pg. 5.

[31] New York State Department of Financial Services, New York Codes, Rules and Regulations, Title 23 Department of Financial Services Part 200 S 200.3(a) and 200.4 (proposed on 2 June 2015) at https://on.ny.gov/2QkyPCa (accessed on 9 December 2018). See also Gatto and Broeker (2015) at pg. 461.

[32] New York State Department of Financial Services, New York Codes, Rules and Regulations, Title 23 Department of Financial Services Part 200 S 200.4.

3.3.3.1 RULING 1 - "CERTAIN MINERS OF CONVERTIBLE VIRTUAL CURRENCIES ARE NOT MSBS (MONEY SERVICE BUSINESSES)"

This administrative ruling was provided on 30 January 2014 in response to the guidance notice published by FinCEN.[33] Under this ruling, a user is not an MSB if he uses the virtual currency for his own benefit.[34] To use the virtual currency for one's own benefit means that the virtual currency is used for the purchase of goods or services to pay debts or to make distributions to other persons.

Therefore, a miner (the person verifying the transactions online and who is rewarded with virtual currency) who mines the cryptocurrency to use for his own benefit and not to trade with the currency will not be subject to the regulations of the BSA. The key is therefore not the way the user obtains the virtual currency, but rather for which activity it is used.[35] The fact that the user converts the virtual currency to purchase goods and services, does not bring it into the scope of the definition of an "exchanger".

3.3.3.2 RULING 2 - "CERTAIN VIRTUAL CURRENCY SOFTWARE PROVIDERS AND INVESTORS ARE NOT MSBS"

The second administrative ruling was also published on 30 January 2014.[36] The production and distribution of the virtual currency software do not constitute the acceptance and transmission of value.[37] The production and distribution of virtual currency coupled with the exchange of virtual currency into real currency will trigger the provisions of the BSA and the person will qualify as an MSB and be required to

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[33] FinCEN-2014-R001 "Application of FinCEN's regulations to Virtual Currency Mining Operations" dated 30 January 2014.
[34] FinCEN-2014-R001 pg. 3.
[35] FinCEN 2013 G001 pg. 2.
[36] FinCEN 2014-ROO2 "Application of FinCEN's Regulations to Virtual Currency Software Development and Certain Investment Activity" dated 30 January 2014.
[37] FinCEN 2014-ROO2 pg.2 . See also Gatto and Broeker (2015) pg.437.

registers as an MSB.[38] Once again the use and benefit of the virtual currency is the trigger for the application of the BSA and to qualify as a MSB.[39]

Therefore, if a person purchases and sells virtual currency for his or her own account it will not be a MSB. The reason is that the person is merely realising an investment made and is not engaged in the business of exchanging and administrating virtual currencies.[40]

3.3.3.3 RULING 3 - "LESSORS OF COMPUTER SYSTEMS FOR MINING VIRTUAL CURRENCY ARE NOT MSBS"

The mere renting of computer systems or the providing of prepaid access will not fall within the ambit of a money transmitter in terms of the BSA.[41]

FinCEN has identified different activities involving virtual currencies and has made determinations regarding the regulatory treatment of administrators and exchangers under these activities.[42] These activities are activities relating to dealers in e-currencies and e-precious metals, centralised virtual currency and decentralised virtual currency.[43]

3.4 DRAFT REGULATION OF VIRTUAL-CURRENCY BUSINESS ACT (RVCBA)

In 2015 the National Conference of Commissioners on Uniform State laws introduced a draft bill titled "Regulation Virtual Currency Businesses Act" ("RVCBA").[44] "Virtual Currency Business" is defined as the transfer and storage services of virtual currency,

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38 FinCEN 2013 G001 pg. 2.
39 FinCEN 2014-ROO2 pg.3. See also Gatto and Broeker (2015) pg.437.
40 FinCEN 2014-ROO2 pg.3. See also Gatto and Broeker (2015) pg.437.
41 FinCEN 2013 G001 pg. 2.
42 FinCEN 2-13-G0001 pg. 3.
43 FinCEN 2013-G0001 pg. 3.
44 National Conference of Comm'rs On Uniform State Laws, Draft Regulation of Virtual Currency Business Act at https://bit.ly/2E7OxKp (accessed on 20 September 2018).

conversion services.[45] The purpose of the RCVBA is not to regulate virtual currency per se but rather to regulate persons using the virtual currency.[46]

The RVCBA sets conditions to engage in virtual currency business activity. These conditions include that the person who intends to enter into virtual currency business activity must have a license issued by the relevant state and must be registered with the relevant department.[47]

To acquire a licence the applicant must comply with the following requirements:[48]

a) the application must be made in the standard form;[49]

b) the Applicant must provide his or her legal name and current address;[50]

c) the Applicant must provide his or her trading name used in the virtual currency transaction;[51]

d) if the Applicant is a company, the executive officer's personal details must be provided;[52]

e) The description of the business of the applicant;[53] and

f) the details of the person who manages the server of the applicant.[54]

The Applicant is also obliged to state any money transmitting licences it holds in any other state.[55] The RVCBA is basically the BSA version of virtual currencies.

The application of the RVCBA, if enacted, will be similar to the BSA and will enable the Internal Revenue Service to trace virtual currency business activity to enable efficient taxation and to prevent tax evasion.

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45 Section 102(a)-(d) of the RVCBA note 44. See also G Comizio 2017 "Virtual Currencies: Growing Regulatory Framework and Challenges emerging Fintech Ecosystem" *The North Carolina Banking Institute* vol 21 pg. 131 pg. 157.
46 RCVBA with commentary at https://bit.ly/2QiRCi0 (accessed on 20 September 2018) pg. 28.
47 Section 201 of RVCBA.
48 Section 202 of RVCBA.
49 Section 202(1) RVCBA.
50 Section 202(2)(A) RVCBA.
51 Section 202(2)(B) RVCBA.
52 Section 202(2)(C) RVCBA.
53 Section 202(2)(D) RVCBA.
54 Section 202(2)(D) RVCBA.
55 Section 202(2)(F) RVCBA.

3.5 THE INTERNAL REVENUE SERVICE

The IRS issued a Guidance Notice titled "Virtual Currency is treated as property for US Federal Tax Purposes; General Rules of Property Transactions apply".[56] The guidance notice on the treatment of virtual currency provides that cryptocurrencies are treated as property and that normal tax rules apply.[57] This means that:

a) Receipts of virtual currency as payment for goods and services including the successful mining of the virtual currency should be included in the taxpayer's gross income at fair market value.[58]

b) If the taxpayer exchanges virtual currency for other property with a fair market value that exceeds the taxpayer's basis cost in virtual currency the taxpayer has a taxable gain in the amount equal to the gain.[59]

The key to tax cryptocurrency is to consider the use of the cryptocurrency. As such the focus should not be on how the cryptocurrency is acquired. The FinCEN and the IRS regard cryptocurrencies as property and the general tax provisions are applicable.[60] The virtual currency transaction must be reported in US Dollars and the taxpayers are required to determine the fair market value in US Dollars at the date of receipt of the virtual currency.[61] The IRS indicated that taxpayers will be liable for penalties and interest in the event that they do not report virtual currency transactions, this sanction is also coupled with possible criminal sanction.[62] On 23 March 2018, the IRS issued a news release again reminded taxpayers of their reporting duty when entering and concluding virtual currency transactions.[63] The taxpayers who do not

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[56] IRS Guidance Notice 2014-21: "Virtual Currency is treated as property for US Federal Tax Purposes; General Rules of Property Transactions apply" 25 March 2014 at https://www.irs.gov/newsroom/irs-virtual-currency-guidance (accessed on 16 July 2018)

[57] Lee (2015) at pg. 29.

[58] Lee (2015) pg. 30.

[59] Lee (2015) pg. 30.

[60] IRS Guidance Notice 2014-21 pg. 2.

[61] IRS Guidance Notice 2014-21 pg. 3.

[62] IRS Guidance Notice 2014-21 pg. 6. See also IRS News Release dated 25 March 2014 IR 2014-36 pg. 1.

[63] IRS News Release "IRS reminds taxpayers to report virtual currency transactions" IR-2018-71 23 March 2018 available at https://bit.ly/2pGC34F (accessed on 12 December 2018)

report that there have been virtual currency transactions are subject to audits and are liable for penalties. One should be reminded that through the provisions of the BSA the IRS will able to track and trace the users, exchanger and administrators of the virtual currency.

The IRS stated that the virtual currency is treated as property which means that the general provisions are applicable. This means that payment made by means of virtual currency is subject to information reporting under the BSA as described above.

The use of the cryptocurrency plays a pivotal role in determining whether the virtual currency should be included in the taxpayer's gross income. One will, however, only be able to answer the question once regulations regarding the detecting of cryptocurrencies have been established.

Therefore, the introduction of a virtual currency licence or a reporting duty of the virtual currency transactions coupled with extreme penalties is a viable option to regulate virtual currency transactions.

The New York State Financial Services "Bitlicence" proposal is a regime that covers Bitcoin as a medium in which value is transmitted from one person to another in the form of property.[64] The Bitlicence provides for mandatory disclosure of customer identifications and the reporting of virtual currency transactions to Bank Secrecy Act.[65]

The critical issue when considering whether to regulate virtual currencies is the aim of the regulation and for whose protection is it aimed at.[66] Subsequently, any exchange of virtual currency such as bitcoin to pay for goods or services can attract a tax liability.[67] A taxpayer who exchanges or mines virtual currency as a trade or business as a form of self-employment will be taxed on their net-earnings in accordance with the self-employment tax. It must be borne in mind that a reporting duty will still be applicable to the taxpayer, despite him or her no qualifying as a MSB, this is as a result of the IRS Guidance Notice and the general reporting duty.[68] All payments received in

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[64] SJ Hughes (2014) 71 Washington and Lee Revenue Online 51 "Did New York State Just Anoint Virtual Currencies by Proposing to Regulate them or will Regulation Spoil them for Some" pg. 54.
[65] Hughes (2014) pg. 55.
[66] Hughes (2014) pg. 67.
[67] IRS Guidance Notice 2014-03 pg. 1.
[68] IRS Guidance Notice 2014-03 pg. 1. See also Gatto and Broeker (2015) at pg. 449.

virtual currency as an independent contractor constitutes gross income and the amount to be included is the fair market value as at the date of receipt.[69]

3.5.1 CONSEQUENCES OF THE TAX TREATMENT BY THE IRS

The interpretation by the IRS has two main consequences.[70] The first consequence is that by treating virtual currency as property taxpayers are not entitled to the personal use exemptions.[71] Secondly, each virtual currency coin will now have its own basis which means that taxpayers are required to track each individual coin.[72]

To determine the tax treatment of property in the United States of America a system called "basis" is used.[73] This is a mechanism to track previously taxed property to avoid double taxation.[74] The method to tax property is called the standalone basis, however, over time the IRS developed rules to allow for the pooling of certain assets, such as the sale of stocks, as a means to account for tax on property.[75]

The "standalone basis" which is the generally applied method, means that each asset held by the taxpayer has its own basis which is set at its costs.[76] The tax gain and loss are calculated using each individual asset's costs.[77] The second method, but not the generally applied method, is the so-called pooling method.[78] This requires taxpayers to report on the total of assets basis and then each asset forms a pro-rata proportion to the aggregate.[79]

The implication of the interpretation is that the general standalone basis applies which gives rise to possible tax evasion since using the stand-alone basis taxpayers can

69 IRS Guidance Notice 2014-03 2014-03 pg. 1. See also Gatto and Broeker (2015) at pg. 449.
70 Chodorow (2017) pg 373.
71 Chodorow (2017) pg 373.
72 Chodorow (2017) pg 373.
73 Chodorow A (2017) 36 "Rethinking basis in the age of virtual currencies" *Virginia Tax Review* 371 pg. 374.
74 Chodorow (2017) pg 374.
75 Chodorow (2017) pg 374.
76 Internal Revenue Code Title 26 1986 S 1012. IRS Treasury Regulation 2012 S1.1012-I(c)(i). See also Chodorow (2017) pg 374.
77 Chodorow (2017) pg 374.
78 Chodorow (2017) pg 374.
79 Chodorow (2017) pg 374.

manipulate the amount on which they pay tax without any real change in their economic position.[80] This is a typical tax shelter as a taxpayer can elect to dispose of a high-base virtual currency, which reduces its tax liability since he or she will account a "loss" and use the proceeds to further his or her investment in other virtual currency.[81] Thus, the taxpayer is enabled to manipulate its tax burden without changing his economic position.

The pooling-approach would require taxpayers to account for all virtual currencies owned and its aggregate basis.[82] The result is that the taxpayer will account for a proportional gain on each individual cryptocurrency.[83] Although in theory, the taxpayer ought to account for the same amount of tax if it used the stand-alone basis, the difference is that in the pooling method the taxpayer does not have the opportunity to manipulate its tax liability.[84] The reason is that it will not change the taxpayer's position if he or she chooses to sell the high-base virtual currency since the aggregate of the basis of all the virtual currencies is used to determine the tax liability. As a result, no shelter to account for a "loss" is created.[85] Therefore, the tax treatment would be based on the economic reality of the taxpayer.[86]

The IRS Treasury has not published a regulation prescribing the pooling method as a means to account for tax on cryptocurrencies. As a result, the standalone together with its risks applies to cryptocurrencies.

Although the proposal of the IRS to treat cryptocurrencies as property was in principle sound the practical effect of the accounting duty has undesired and onerous consequences which rendered the regulatory framework inefficient and easy to avoid. Thus, it is submitted that IRS should have proposed that taxpayers use the pooling method as opposed to the standalone method of accounting which is more favourable for purposes of tax evasion.

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80 Chodorow (2017) pg 375.
81 Chodorow (2017) pg 375.
82 IRS Treasury Regulation S1.1012-I(c)(i). Chodorow (2017) pg 385.
83 Chodorow (2017) pg 398.
84 Chodorow (2017) pg 375.
85 Chodorow (2017) pg 396-397.
86 Chodorow (2017) pg 398.

3.6 REGULATION IN CANADA

Cryptocurrencies are allowed in Canada and may be freely used for trade and investment.[87] The Canadian Currency Act,[88] defines the concept of legal tender in section 8 and recognises two types of legal tender namely the coins and monetary notes issued by the Bank of Canada.[89] Since cryptocurrencies are neither coins nor notes issued by the Canadian Bank it is not considered to be legal tender. Although cryptocurrencies are not regarded as legal tender it may still attract tax consequences. This is remarkably similar to the position in the USA in which the cryptocurrency is also not considered to be legal tender, but it may have tax consequences.[90]

The Canadian Financial Consumer Agency issued a notice on 12 February 2018 in which it was stated that cryptocurrencies are not regarded as legal tender but that the normal rules of taxation are applicable to cryptocurrency transactions.[91]

The notice dealt with “The Automated Exchangers” referred to as a Bitcoin ATM.[92] This ATM links to the Bitcoin-wallet of the user. The user will insert cash in exchange for Bitcoins and vice versa.[93] These Bitcoin ATMs do not work in a similar fashion as ATM’s connected to a central bank. Although the two concepts are similar the operation of Bitcoin ATMs differs fromthat of a normal bank ATM.

The Bitcoin ATM reads the bills as the user inserts it in the Bitcoin ATM. The Bitcoin ATM then connects to the Bitcoin Ledger which then, in turn, return the equivalent value of Bitcoins in the user’s wallet. This wallet is linked to a specific user number or name. The Bitcoin Ledger will still be verified in the manner described in chapter 1 of this study.[94] In contrast to the Bitcoin ATM, a normal ATM is linked to a host computer which is in turn connected to the relevant bank’s computers. Thus, the transaction is

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87 Ahmad T Regulation of Cryptocurrency: Canada 15 June 2018 *The Library of Congress* at https://bit.ly/2G58oMQ (accessed on 11 October 2018). See also Financial Consumer Agency of Canada: Digital Currency (“FCAC”) 12 February 2018 at https://bit.ly/2g3n5Ao (accessed on 11 October 2018).
88 The Canadian Currency Act C52 of 1985
89 Section 8 of the Canadian Currency Act C52 of 1985
90 Ahmad (2018).
91 FCAC at pg. 2.
92 FCAC at pg. 2.
93 FCAC at pg. 2.
94 See Chapter 1 paragraph 1.1.

verified by the bank through the use of these interlinked computers.[95] Thus. the transaction is not verified by the users of the ATM but by the bank as an administrative body.

The notice by the Canadian Financial Consumer Agency stated that the normal tax rules are applicable to digital currency transactions including cryptocurrencies. This means that digital currencies are subject to the Canadian Income Tax Act.[96] In this regard, the notice differentiates between the buying and selling of digital currencies and the buying and selling of digital currency as a commodity.[97]

The goods purchased and sold must be included in the user's income. The normal Goods and Services Taxes and Harmonized Sales Taxes will be applicable.[98] The Canadian Revenue Agency stated that-

"Where digital currency is used to pay for goods or services, the rules for barter transactions apply. A barter transaction occurs when any two persons agree to exchange goods or services and carry out that exchange without using legal currency. For example, paying for movies with digital currency is a barter transaction. The value of the movies purchased using digital currency must be included in the seller's income for tax purposes. The amount to be included would be the value of the movies in Canadian dollars."[99]

Barter transactions are dealt with in section 3 and 9 of the Canadian Income Tax Act.[100] The Canadian Revenue Agency issued an Interpretation Bulletin[101] on 5 July 1982 regarding the interpretation of section 3 and 9 with reference to barter transactions. A barter transaction can take the form of either an income or expense or a capital property.[102] The basic requirements for the inclusion of barter transaction in the income of the taxpayer are that goods must be purchased or services rendered at

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95 Bowen J "How do ATMs Work?" *HowStuffworks?* at https://bit.ly/2UuHRvR (accessed on 9 December 2018)
96 FCAC at pg. 2.
97 FCAC at pg. 3.
98 FCAC at pg. 2.
99 What You Should Know about Digital Currency, Canada Revenue Agency at https://bit.ly/2KaMvsI (accessed on 11 October 2018).
100 Income Tax Act R.S.C., 1985, c. 1.
101 The Interpretation Bulletin is similar to CSARS' Interpretation Notes published.
102 Interpretation Bulletin Barter Transactions IT-490 Income Tax Act pg. 1.

arm's length and at market value.[103] In other words, the transaction must be on the same basis as if it was sold to a complete stranger.[104] To apply this to cryptocurrencies means that the value of the cryptocurrency as at the date of acquisition must be used to calculate the taxpayer's income. By treating it as a barter transaction the Canadian Revenue Agency actually imports a reporting duty on the seller or service provider since they need to account for the income received. This means that even if the seller and purchaser agree to use the cryptocurrency through the Bitcoin ATM the transaction can be traced and verified by the Revenue Agency. The user name or number will be linked to the specific user in which the cash or cryptocurrencies was deposited.

The Canadian Revenue Agency went further to state that the digital currency may also be used as a commodity and as such the user must report any gains or losses from the selling and the buying of cryptocurrencies.[105] This means that the cryptocurrencies will be treated similarly to securities.[106] The Canadian Revenue Agency published an Interpretation Bulletin on the treatment of securities on 29 February 1984.[107] The purpose of this Interpretation Bulletin was to assist the taxpayer in determining whether the income from securities was income or capital in nature.[108]

Transactions of securities are treated in terms of section 39 of the Income Tax Act. The Income Tax Act in section 39(4) states that if the taxpayer disposed of a Canadian Security, he or she should include the disposal as capital property and that every subsequent disposal is capital property.[109]

The aforementioned provision is, however, not available to a taxpayer who at the time of the disposal was a:

a) trader in securities;

b) bank to which the Bank Act and the Quebec Savings Bank Act applies;

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[103] Interpretation Bulletin Barter Transactions IT-490 Income Tax Act pg. 1.
[104] Interpretation Bulletin Transactions in Securities 29 February 1984 NO: IT-479R.
[105] FCAC pg. 3-4.
[106] Ahmad (2018).
[107] Interpretation Bulletin Transactions in Securities 29 February 1984 NO: IT-479R pg. 1.
[108] Interpretation Bulletin Transactions in Securities 29 February 1984 NO: IT-479R pg. 1.
[109] S 39(4) of the Canadian Income Tax Act.

c) corporation who is registered under Canadian laws carry on the business of offering securities to the public;

d) credit union;

e) non-resident;

f) an insurance company; or

g) a corporation whose principal business is the lending of money.

To apply the concept to the trade in cryptocurrencies as suggested by the Revenue Agency would mean that any user of cryptocurrencies may elect to include the disposal of cryptocurrencies as deemed capital property in the year of the disposal and subsequent years. This will be subject to section 39 (95) which stipulates that if the user trades in cryptocurrencies and qualifies as a person who participates in the promoting or underwriting of the cryptocurrency or who holds himself or herself out to the public as an exchanger or administer will not be able to deem the disposals as capital in nature and it will be regarded as income.

To determine whether a person is carrying on a trade the Revenue Agency considers certain factors, namely:[110]

> "a) The frequency of transactions - a history of extensive buying and selling of securities or of a quick turnover of properties,
>
> (b) period of ownership - securities are usually owned only for a short period of time,
>
> (c) knowledge of securities markets - the taxpayer has some knowledge of or experience in the securities markets,
>
> (d) security transactions form a part of a taxpayer's ordinary business,
>
> (e) time spent - a substantial part of the taxpayer's time is spent studying the securities markets and investigating potential purchases,
>
> (f) financing - security purchases are financed primarily on margin or by some other form of debt,
>
> (g) advertising - the taxpayer has advertised or otherwise made it known that he is willing to purchase securities, and

[110] Interpretation Bulletin Transactions in Securities 29 February 1984 NO: IT-479R pg. 3.

(h) in the case of shares, their nature - normally speculative in nature or of a non-dividend type"[111]

If the taxpayer engages in an income-earning activity through trading in virtual currencies, then the amount will be accounted as income. If the taxpayer, however, keeps the investment for long term growth the virtual currency will be regarded as capital. Therefore, of vital importance is the intention of the taxpayer.[112]

The question then turns to how Canada intends to regulate the cryptocurrencies for purposes of taxation. In 2000, Canada promulgated the Proceeds of Crime (Money Laundering) and Terrorist Financing Act.[113] The purpose of the aforementioned act was to establish a Financial Transactions and Reports Analysis Centre to combat money laundering and the financing of terrorist activities.[114] The first objective of the Proceeds of Crime (Money Laundering) and Terrorist Financing Act is to implement measures to identify and deter money laundering and terrorist financing.[115] This would be achieved by implementing mandatory record keeping and client identification processes and mandatory reporting of suspicious transactions to the Financial Transactions and Reports Analysis Centre.[116] The second objective is to enhance the responsiveness of law enforcement to threats of organised crime whilst protecting the privacy of persons.[117] The third objective is to comply with international commitments to combat money laundering and terrorist financing.[118] The fourth objective is to safeguard Canada's financial systems and to mitigate the threats posed to the financial systems used as vehicles for money laundering.[119]

The objectives of the Proceeds of Crime (Money Laundering) and Terrorist Financing Act are of significant importance when one considers the threats posed by cryptocurrencies in relation to tax evasion, money laundering and terrorist financing.

[111] Interpretation Bulletin Transactions in Securities 29 February 1984 NO: IT-479R pg. 3. Own emphasis added.
[112] Al-Shikarchy M (2017) Canadian Taxation of Cryptocurrency Gowling WLG So Far, *Lexology* at https://bit.ly/2G6CwYdso-far/?lang=en-CA (accessed on 11 October 2018). See also Ahmed (2018).
[113] Proceeds of Crime (Money Laundering) and Terrorist Financing Act S.C.2000 c17.
[114] Preamble to Proceeds of Crime (Money Laundering) and Terrorist Financing Act.
[115] S 3(a) of Proceeds of Crime (Money Laundering) and Terrorist Financing Act.
[116] S 3(a)(i)-(iii) Proceeds of Crime (Money Laundering) and Terrorist Financing Act.
[117] S 3(b) Proceeds of Crime (Money Laundering) and Terrorist Financing Act.
[118] S 3(c) Proceeds of Crime (Money Laundering) and Terrorist Financing Act.
[119] S 3(d) Proceeds of Crime (Money Laundering) and Terrorist Financing Act.

The objectives can be used as an action plan by the Canadian government to combat the threats associated with cryptocurrencies. The mandatory recordkeeping of transactions by merchants as well as clients will enable the government and ultimately the Revenue Agency to track users of cryptocurrencies to bring them within the ambit of the applicable tax legislation. Once the cryptocurrency transactions can be traced and the users tracked, the officials of the Revenue Agency can respond to the transactions and raise their assessments. This would necessitate the training and education of the Revenue Agency's officials to ensure quick reactions when the transactions are traced or reported.

Section 6 of the Proceeds of Crime (Money Laundering) and Terrorist Financing Act deals with the duty of record keeping and client identification. This section states that every person listed in section 5 must keep a record in accordance with the prescribed regulations. Section 5 deals with the application of the act to certain persons and it applies to local Canadian and foreign banks, government departments, casinos and similar businesses, to persons, entities engaged in prescribed professions or activities and persons engaged in foreign exchange dealing or through "any person, entity or electronic funds transfer networks".[120] It follows that the Proceeds of Crime (Money Laundering) and Terrorist Financing Act will be applicable to persons engaging in electronic funds transfers such as the dealing in cryptocurrencies. The question is whether cryptocurrencies may be brought into the ambit of "electronic funds transfers". Essentially, in cryptocurrencies transactions value is shifted which is an argument in favour of the application of the act.

The Proceeds of Crime (Money Laundering) and Terrorist Financing Act creates an obligation in section 6.1 to verify the identity of contracting parties.[121] The measures to facilitate this verification is set out in section 9 and of importance to cryptocurrencies is the measures associated with electronic fund transfers.[122] Furthermore, every person listed in section 5, shall with regard to every electronic fund transfer within their

[120] S 5 of the Proceeds of Crime (Money Laundering) and Terrorist Financing Act.
[121] S 6.1 Proceeds of Crime (Money Laundering) and Terrorist Financing Act.
[122] S 9.5 Proceeds of Crime (Money Laundering) and Terrorist Financing Act.

financial activities, take reasonable measures to include the name, address, account number or another reference number of a client.[123]

Section 73(1) states that the Governor may make any regulation which it deems necessary with regard to-

a) dealing in virtual currencies;[124]

b) reporting in terms of section 6 and 6.1;[125] and

c) disclosing in terms of section 7 and 9.[126]

Considering the operation of cryptocurrencies, this would mean that the user name of the person to whom money or cryptocurrencies is transferred, the account number to which it was transferred and the blockchain encryption code must be disclosed to the Financial Transactions and Reports Analysis Centre. One must be reminded that the blockchain technology functions with an encryption code that is verified by different users.[127]

The consequences of non-compliance with the Proceeds of Crime (Money Laundering) and Terrorist Financing Act is a penalty payment. Every violation is classified as minor, serious or very serious.[128] The purpose of the penalties is to encourage compliance rather than to punish the violation thereof.[129] The maximum penalty for a violation by a natural person is $100 000 Canadian dollar and for entities, it is $500 000 Canadian dollar. This amounts to approximately R1,113,213.96 for a natural person which serves as a compelling incentive to ensure compliance.[130]

The proposed amendment in terms of section 256(2) of the Act seeks to amend section 5 to include persons who have a place of business in Canada and who is dealing in virtual currencies. A further proposed amendment to section 5 includes persons who do not have a place of business in Canada but is "dealing in virtual currencies". The

[123] S 9.5(a) and (b) Proceeds of Crime (Money Laundering) and Terrorist Financing Act.
[124] S 73(1)(a) Proceeds of Crime (Money Laundering) and Terrorist Financing Act.
[125] S 73(1)(b) Proceeds of Crime (Money Laundering) and Terrorist Financing Act.
[126] S 73(1)(c) Proceeds of Crime (Money Laundering) and Terrorist Financing Act.
[127] Chapter 2 paragraph 2.1.
[128] S 73.1 (1) Proceeds of Crime (Money Laundering) and Terrorist Financing Act.
[129] S 73.11 Proceeds of Crime (Money Laundering) and Terrorist Financing Act.
[130] As per the exchange rate of R11,13 per Canadian dollar on 13 October 2018.

broad scope for "dealing in virtual currencies" is not qualified in the act or its regulations. It is submitted that for the avoidance of doubt this blanket description should be qualified by the Canadian legislature.

These amendments would mean that any person who either uses, exchanges or trade using virtual currencies must register with the Financial Transactions and Reports Analysis Centre to avoid cybercrime and online money laundering.

The implication of the provisions of the Proceeds of Crime (Money Laundering) and Terrorist Financing Act is that Bitcoin dealers will be subject to record keeping of all their online transactions. Furthermore, Bitcoin dealers must register with the Financial Transactions and Reports Analysis of Canada. Although the Bitcoin ATM is aimed at facilitating easy access to cryptocurrencies, it does not detract from the duty imposed on the taxpayer to report the transaction. The local and foreign banks will also be prohibited from opening accounts for Bitcoin dealers who are not registered with Financial Transactions and Reports Analysis.[131]

3.6.1 TAX EVASION PRINCIPLES IN INCOME TAX ACT

The Canadian Revenue Agency has implemented the Proceeds of Crime (Money Laundering) and Terrorist Financing Act and accessed electronic funds transfers ("EFT") of more than $10 000 entering or leaving the country. This is done to boost the regulation of value shifting to enhance tax compliance.[132]

Tax compliance was also increased through Canada's commitment to the Co-operation and Development (OECD) and the Global Forum on Transparency and Exchange of Information for Tax Purposes (Global Forum) to access off-shore bank accounts held by Canadians.[133]

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[131] Suburg (2014) Canada Signs First Ever Official Law Regulating Bitcoin https://bit.ly/2UsKHBg (accessed on 26 April 2018).
[132] Canada Revenue Agency "Tax evasion and aggressive tax avoidance know no borders" at https://bit.ly/2RrL38T (accessed on 13 October 2018).
[133] Canada Revenue Agency "Tax evasion and aggressive tax avoidance know no borders".

The Canadian Income Tax Act makes provision for the General Anti-Avoidance Rule ("GAAR") in section 245.[134] Section 245(2) provides that if a transaction constitutes an avoidance transaction the tax consequences will be determined as is reasonable to deny a tax benefit that would result either directly or indirectly from the transaction. To unpack this section, one must consider the key definitions provided in section 245(1).

The first key term is "tax benefit", which is defined in section 245(2) as a:[135]

> "reduction, avoidance or deferral of tax or other amount payable under this Act or an increase in a refund of tax or other amount under this Act, and includes a reduction, avoidance or deferral of tax or other amount that would be payable under this Act but for a tax treaty or an increase in a refund of tax or other amount under this Act as a result of a tax treaty".

The second key definition is that of a "tax consequence" which is defined as:[136]

> "the amount of income, taxable income, or taxable income earned in Canada of, tax or other amount payable by or refundable to the person under this Act, or any other amount that is relevant for the purposes of computing that amount"

The third key definition is "transaction" which includes any arrangement or event.[137]

Section 245(3) provides that an avoidance transaction is:

a) a single transaction that result in a direct or indirect tax benefit, unless it can be reasonably considered that it was entered into for a *bona fide* purpose;[138] or

b) a series of transactions that result in a direct or indirect tax benefit, unless it can be reasonably considered that it was entered into for a *bona fide* purpose.[139]

In *Canada Trustco Mortgage Co ("CTMC") v Canada*[140] CTMC purchased a number of trailers, which it leased back to the original owner to offset revenue from its leased assets and claimed a substantial capital cost allowance as a result of the sale-

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[134] PART XV.1 S 245 Canadian Income Tax Act C1 R.S.C. 1985. See also D Rotfleisch (2017) "Canada: Tax Avoidance & Tax Planning- General Anti-Avoidance Rule-Canadian Tax Lawyer Analysis" *Mondaq* at https://bit.ly/2SzCjOL (accessed on 13 October 2018).
[135] S 245(1) Canadian Income Tax Act.
[136] S 245(1) Canadian Income Tax Act.
[137] S 245(1) Canadian Income Tax Act.
[138] S 245(3) Canadian Income Tax Act.
[139] S 245(3) Canadian Income Tax Act.
[140] *Canada Trustco Mortgage Co. v Canada* 2005 SCC 54.

leaseback transaction. The court had to consider the application of the GAAR.[141] The Canadian Supreme Court held that intention of the legislature by including the GAAR was to address those transactions which complies with the literal interpretation of the law, and which result in a tax benefit but constitutes an abuse of the Act.[142] The court developed a three-step test to determine whether the GAAR applies to a transaction.

The first step is to determine whether there is a tax benefit, meaning that the taxpayer's taxable amount is reduced, the obligation to pay is deferred or the tax obligation is avoided.[143]

The second step is whether the transaction that gives rise to the tax benefit, constitutes an avoidance transaction for purposes of section 245(3).[144]The court held that the purpose of the GAAR was not to create uncertainty in tax planning but as last resort to combat abusive tax practices.[145] The standard which must be met for a transaction to be immune to GAAR is that it must be entered into for a *bona fide* purpose.[146] To determine whether the taxpayer had a *bona fide* purpose the court must consider the relationships between the parties and the actual transactions concluded between them. As such it is a factual inquiry that the presiding officer must make to determine whether a *bona fide* purpose existed when the transaction was concluded.[147]

The third step is to determine whether the avoidance transaction is abusive.[148] The court held that a unified interpretative approach is required which means that the provisions giving rise to the tax benefit must be interpreted within their context, spirit and purpose.[149] This is a mixture of both a factual inquiry and a legal question.[150] The court held that the transaction may be motivated by economic, commercial, family or other non-tax purposes, but that this fact alone, is not indicative of an abuse of the provisions of the Income Tax Act.[151] Although the transaction may be categorised as

[141] *Canada Trustco Mortgage Co* par 2-3. A sale-leaseback transaction is a transaction in which the purchaser buys an asset and leases it from the seller on a long term.
[142] *Canada Trustco Mortgage Co.* par 16.
[143] *Canada Trustco Mortgage Co.* par 17 and 18. See section 241(1)'s definition of a "tax benefit".
[144] *Canada Trustco Mortgage Co.* par 21.
[145] *Canada Trustco Mortgage Co.* par 21.
[146] S 245(3) Canadian Income Tax Act.
[147] *Canada Trustco Mortgage Co.* par 29 -30.
[148] *Canada Trustco Mortgage Co.* par 29 -30.
[149] *Canada Trustco Mortgage Co.* par 29 -30.
[150] *Canada Trustco Mortgage Co.* par 29-30.
[151] *Canada Trustco Mortgage Co.* par 57-58.

having a lack of substance or that it is artificial, the test is whether it is against the spirit, object and purpose of the applicable provision of the Income Tax Act, and only then will it be abusive.[152]

The Canadian Revenue Agency will make use of the Proceeds of Crime (Money Laundering) and Terrorist Financing Act to identify the users of cryptocurrency and to trace the transactions. The tax consequences of the use of cryptocurrencies will be dealt with by the provisions of the Income Tax Act in conjunction with the GAAR.

3.7 CONCLUSION

The regulation of cryptocurrencies cannot be effectively done by only applying the GAAR in the respective income tax Acts due to the anonymity of the cryptocurrencies. A unified approach between different sets of legislation aimed at preventing money laundering which provides measures regarding record keeping, reporting and penalties must be implemented to assist the revenue agencies in their quest to combat tax evasion.

The power of the reporting centres for financial crimes such as the Financial Transactions and Reports Analysis of Canada and FinCEN in the United States must be used in conjunction with those of the IRS and the Canadian Revenue Agency. By implementing a joint task force consisting of a forensic team from the reporting centres and the tax officials for the treatment of cryptocurrencies may result in cryptocurrencies being efficiently identified and promptly taxed.

[152] *Canada Trustco Mortgage Co.* par 60.

CHAPTER 4: THE EXISTING ANTI-AVOIDANCE PROVISIONS AND TAX EVASION IN SOUTH AFRICA

In the South African Income Tax Act,[1] ("IT Act") and Tax Administration Act,[2] ("TAA") there are various provisions which prevent avoidance structures and tax evasion. In what follows the existing anti-avoidance provisions will be discussed and evaluated in the context of cryptocurrencies.

As a point of departure, a brief discussion on the general difference between tax evasion and tax avoidance is provided. This is followed by a general discussion of the principles relating to the interpretation of fiscal legislation is provided as background for the interpretation of the IT Act and TAA that follows.

4.1 TAX EVASION AND AVOIDANCE VERSUS TAX PLANNING

"In this world, nothing is certain, except death and taxes."[3]

The above quote paints a bleak picture regarding the perspective of taxpayers when it comes to paying taxes. It is true that most people dislike paying taxes and often feel that the Commissioner takes more than its pound of flesh, however, what infuriates taxpayers, even more, is knowing that someone else in a similar position is paying significantly less tax.[4] Tax planning has evolved into a strategic field of both law and accounting to enable the taxpayer to effectively plan tax to achieve a positive result. The flipside to tax planning is, of course, the failure to maintain an effective tax plan which might result in non-compliance with the tax legislation leading to hefty penalties and even criminal prosecution.[5] The question is then when does tax planning overstep its legal parameters and become tax evasion or avoidance. If a taxpayer chooses to

1 Income Tax Act 58 of 1962
2 Tax Administration Act 28 of 2011.
3 Benjamin Franklin in a letter to Jean-Baptiste Le Roy in November 1789 at https://bit.ly/2pz8oZ2 (accessed on 9 December 2018)
4 Kruger D et al (2012) 5th Edition Broomberg on Tax Strategy pg.1.
5 Kruger D (2012) pg. 1.

rather pay in cryptocurrency as a means to shift value, does it result in tax evasion or merely good tax planning by extorting the loopholes in the current legislation?

To understand the difference between tax evasion and tax avoidance my third-year Tax Law lecturer described the difference by way of the following example:[6]

> Imagine that person A needs to be at point B at a certain time but he or she must go through a heavy traffic area. A can decide to speed through an intersection and ignore the red traffic light and thereby arrive on time. Alternatively, A may use an alternative route with the same estimated time of arrival without breaking the traffic laws.

From the above example, if A *chooses* to ignore the red traffic light and to speed through the intersection, he or she would be contravening many road traffic laws and he would be guilty of an offence.[7] This scenario can be equated with the act of tax evasion. Tax evasion is the *deliberate* decision by a taxpayer to structure his or her affairs in such a manner so that the taxpayer is freed from tax liability.[8] Tax evasion can take many forms such as the falsification to submit a return or it can be disguised in a complex commercial transaction which as no commercial sense.[9] Tax evasion may result in both a civil penalty imposed by SARS, or it might result in criminal prosecution since it constitutes an offence. It is similar to disregarding a red traffic light that may result in a fine being imposed alternatively it may result in criminal prosecution under the Criminal Procedure Act 51 of 1977.

In our scenario, if A decides to use an alternative route to arrive at his or her destination the situation is akin to tax avoidance. It is not necessarily an offence or impermissible. Tax avoidance refers to the situation in which the taxpayer legitimately arranges his or her affairs in such a manner that a reduced or zero tax liability is created.[10] In managing his or her tax affairs the taxpayer must remain cautious not to overstep the legal limits of permissible tax avoidance which will trigger the impermissible tax

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[6] Editorial April 2012 Vol 61 "'A Short-Cut Analogy for Tax Avoidance" *The Taxpayer* 61 pg. 62.
[7] Within the South African context, the Road Traffic Act provides for certain statutory crimes such as inconsiderate driving.
[8] Divaris C and ML Stein (2018) South African Income Tax Guide 2017/2018 Edition Chapter 18 par 18.8.
[9] Divaris (2018) par 18.8.
[10] Divaris (2018) par 18.8.

avoidance provisions. The anti-avoidance provisions in the tax legislative body which are more fully dealt with hereunder.

The question then turns to what is considered to be good tax planning or an effective tax plan. In *CIR v Conhage,*[11] Hefer JA held that there is nothing wrong with a taxpayer arranging his financial affairs in such a manner to pay the least tax permissible. There is in principle nothing wrong with arrangements that are tax effective. But there is something wrong with dressing up or disguising a transaction to make it appear to be something that it is not, especially if it has the purpose of tax evasion or of the avoidance of a peremptory rule of law.[12] Good tax planning is using the tax legislation to your best advantage without abusing the provisions to avoid liability. There is always inherent risk in tax planning that the Commissioner may construe the tax plan as an impermissible tax structure.

4.2 INTERPRETATION OF FISCAL LEGISLATION

The golden rule of interpretation of statutes has evolved on the quest to avoid absurdities which are likely to result from consistent adherence to literalism.[13] This means that one should not look at the literal meaning of the word but rather its meaning within the context in which it is used.

It is equally trite that a statutory provision should be interpreted *ex visceribus actus*. Thus, a statute must be interpreted using the aim and purpose of the legislation as the basis for interpretation. Thus, one is entitled and indeed bound, when construing the terms of any provision found in a statute, to consider any other parts of the legislation which throws light upon the intention of the legislature and which may serve to show that a particular provision ought not to be construed as it would be, if construed alone and apart from the remainder of the statute.[14]

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11 *CIR v Conhage* 1999 (4) SA 1149 (SCA).
12 *CIR v Conhage* pg. 67
13 *Natal Joint Municipal Pension Fund v Endumeni Municipality* 2012 (4) S 593 (SCA).
14 *Ndlabathi v Adjunk Prokureur Generaal Transvaal en Andere* 1978(3) SA 620(W).

In *Protective Mining & Industrial Equipment Systems (Pty) Ltd (formerly Nampo (Pty) Ltd v Audiolens (Cape) (Pty) Ltd* Grosskopff JA followed this approach by stating as follows:[15]

> "In ascertaining this intention, regard is to be had both to the language of the enactment and to the context, using this word in a wide sense ... However, it has often been laid down that where the language of a statute is unambiguous, and its meaning is clear, the court may only depart from such meaning –'if it would lead to absurdity so glaring that it could never have been contemplated by the Legislature, or where it would lead to a result contrary to the intention of the Legislature, as shown by the context or by such other considerations as the court is justified in taking into account.'"

Another aspect to be considered is the difference between the use of peremptory and directory terms in the legislation. If a regulation is couched in the positive such as "the taxpayer must" rather than in the negative form as "no taxpayer may" that it could be taken as being directory and not peremptory.[16] It, therefore, remains a matter of statutory interpretation whether the lawmaker intended the verb "must" to be as categorical imperative.

In the case of *Glen Anil Development Corporation v SIR,*[17] the court held that where a statute imposes a burden on its subject, the statute must be construed in favour of the subject.[18] This is commonly referred to as the *contra fiscum*-rule of interpretation. It is against the aforementioned basic principles of interpretation, that the relevant provisions of the IT Act and TAA will be discussed.

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[15] *Protective Mining & Industrial Equipment Systems (Pty) Ltd (formerly Nampo (Pty) Ltd v Audiolens (Cape) (Pty) Lt* 1987(2) SA 961 (A) at 991 G-H.
[16] *Intertrade v MEC for Roads and Public works* [2008] 1 All SA 142 (Ck) at par 28.
[17] *Glen Anil Development Corporation v Secretary for Inland Revenue* 1975(4) SA 715 (A).
[18] *Glen Anil Development Corporation v Secretary for Inland Revenue* 1975(4) SA 715 (A) pg. 626.

4.3 THE ANTI-AVOIDANCE PROVISIONS IN THE IT ACT

4.3.1 SECTION 80A- THE ANTI-AVOIDANCE PROVISIONS IN THE CONTEXT OF "BUSINESS"

Section 80A of the IT Act reads as follows:

> "**Impermissible tax avoidance arrangements. —**An avoidance arrangement is an impermissible avoidance arrangement if its sole or main purpose was to obtain a tax benefit and—
>
> (a) In the context of business—
>
> (i) it was entered into or carried out by means or in a manner which would not normally be employed for *bona fide* business purposes, other than obtaining a tax benefit; or
>
> (ii) it lacks commercial substance, in whole or in part, taking into account the provisions of section 80C;
>
> (b) In a context other than business, it was entered into or carried out by means or in a manner which would not normally be employed for a *bona fide* purpose, other than obtaining a tax benefit; or
>
> (c)in any context—
>
> (i) it has created rights or obligations that would not normally be created between persons dealing at arm's length; or
>
> (ii) it would result directly or indirectly in the misuse or abuse of the provisions of this Act"

The elements of an impermissible avoidance arrangement can be summarised as:

a) An arrangement entered by a taxpayer;
b) With the sole purpose to obtain a tax benefit;
c) Which is abnormal in the context or lacks commercial sense.

By applying the principles of interpretation laid down in the case *Natal Joint Municipal Pension Fund*[19] the words used in the provision must be given their ordinary meaning unless it would lead to an absurdity. It is important to note that each word in a provision must bear a specific meaning which must be ascertained when determining the application of the provision.

[19] *Natal Joint Municipal Pension Fund v Endumeni Municipality* 2012 (4) S 593 (SCA).

To understand section 80A certain operative terms must be considered. These operative terms are:

a) Arrangement;
b) Tax benefit; and
c) Commercial substance.

4.3.1.1 “ARRANGEMENT”

The first term that warrants describing is “arrangement” which is defined in section 80L as “any transaction, operation, scheme, agreement or understanding (whether enforceable or not) including all steps therein or parts thereof and includes any of the foregoing involving the alienation of property”.[20] This definition sets the stage for the application of section 80A. It is formulated in the broadest sense to include all types of transactions.

The phrase “understanding (whether enforceable or not)” suggests that even if the agreement is not reduced to writing and does not comply with formal requirements it may still constitute an “arrangement” for purposes of tax avoidance.[21] Interestingly, section 80A will also apply to agreements which are not enforceable by operation of law. As such illegal contracts will also be in the ambit of the avoidance provisions. One can argue that it may form the basis of the principle in the *MP Finance* -case that illegal receipts may still attract a tax liability.[22]

When applying the contextual setting of the meaning of “arrangement” to cryptocurrency related transactions, the fact that cryptocurrencies are not legal tender for the payment for goods sold and delivered or services rendered must be considered. The status of legal tender relates to whether merchants are obliged to accept it as value. Thus, the mere fact that cryptocurrencies are not regarded as legal tender does not mean that it cannot be the subject of an impermissible avoidance arrangement. The relevance of the consideration of whether cryptocurrencies are regarded as legal

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[20] S 80L “arrangement” of IT Act.
[21] De Koker (2018) par 19.3.6.
[22] *MP Finance Group CC* referred to above. See Chapter 2 par 2.3.

tender relates to the usage of the word “funds” in the avoidance provisions will be more fully discussed hereunder.[23]

Furthermore, there exists no general prohibition on merchants to decline the offer of cryptocurrencies as tender. As a result, cryptocurrencies may be exchanged for goods sold and delivered or services rendered. Thus, a barter transaction that includes the payment in cryptocurrencies meets the requirement of an ‘arrangement”.

Cryptocurrencies are also used as a manner of compensation for the fulfilment of an obligation. This can take on many forms such as compensation for the sale of shares, or as a dividend distribution by a company or the transfer of a business. The use of cryptocurrencies by individuals and corporates in these corporate settings are not prohibited and even if the transaction is unenforceable due to non-compliance with statutory requirements or for any other reason the transaction is not excluded from the term “arrangement”.

From the definition of arrangement, which includes unenforceable agreements or arrangements, it is submitted that should it be found that arrangements in which cryptocurrencies are the subject matter are unenforceable, the anti-avoidance provisions of the IT Act will remain applicable.

As more fully discussed hereunder, the avoidance provisions stand on two legs being either that the transaction is abnormal or it lacks commercial substance. In this context, it is interesting to consider whether the use of cryptocurrencies in normal transactions or the buying and selling thereof should be regarded as a “trade”. The effect of the classification as a “trade” means that the buying and selling of cryptocurrencies will not be considered as “abnormal” and therefore should cryptocurrencies be used in corporate settings to obtain a tax benefit the anti-avoidance provisions will not be triggered. The legislature attempted to address this issue in the draft amendment bill which is detailed further below .

23 See paragraph 4.3.3

4.3.1.2 "TAX BENEFIT"

The second operative term is a "tax benefit".[24] Section 1 of the IT Act describes a tax benefit to include "any avoidance, postponement or reduction of any liability". Thus, the taxpayer's intention when entering into the arrangement must be to obtain a benefit, which it would not have under normal circumstances. This benefit must be to either postpone the liability, avoid the tax liability in *toto* or it must result in a reduced liability.

The postponement of the liability is not *per se* an impermissible avoidance since various rules in the IT Act allows for the postponement of a tax liability. An example of a legal postponement of the liability can be found in the application of the roll-over relief mechanism in respect of the corporate rules relating to capital gains taxes charged in terms of the Eighth Schedule to the IT Act.[25] The roll-over relief in the corporate rules, in essence, provides that the base cost and the proceeds are deemed to be the same amount in value. This allows the taxpayer to only become liable for the capital gains on further disposal of the assets. The roll-over relief mechanisms have their own set of specific avoidance rules but the general provisions of section 80A still apply.

The question then turns to whether the mere use of cryptocurrencies will result in a "tax benefit" as contemplated in the IT Act. The use of cryptocurrencies can, in the current tax legislative framework, result in a tax benefit. As previously alluded, the main attraction to cryptocurrencies and related transactions is the anonymity and the fact that it falls outside government control. This makes it extremely difficult for the SARS to trace these transactions. Therefore, taxpayers are successful in evading their tax obligation in respect of the cryptocurrencies bought and sold.

However, it cannot be said that *all* traders in cryptocurrency trade for purposes of obtaining a tax benefit. In this regard, the intention of the taxpayer must be established in accordance with the general principles detailed below.[26]

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[24] S 80L(a)(i). See also LAWSA Vol 22(1) 2nd Edition par 703.
[25] S 41-47 of IT Act.
[26] See Chapter 4 paragraph 4.4.1.

4.3.1.3 “COMMERCIAL SUBSTANCE”

The third term that must be kept in mind is that of “commercial substance”.[27] An arrangement would lack commercial sense if it results in a tax benefit without influencing the business risks or the net cash flows of the business.[28] For purposes of this paragraph, the reader’s attention is merely drawn to the definition of “commercial substance” and the application thereof is dealt with further in this chapter due to convenience.[29]

The various terms and requirements must be read in conjunction with the whole of section 80A to determine their application and interpretation.

4.3.2 SECTION 80A(a)(i)

Section 80A(a)(i) reads:

> “(a) In the context of business—
>
> (i) it was entered into or carried out by means or in a manner which would not normally be employed for *bona fide* business purposes, other than obtaining a tax benefit; or”

This section relates to the form of the transactions.[30] The legislature introduced the words “not normally” when describing the form of the transaction. Therefore, the focus is on whether there is an abnormality in the transaction and that abnormality must be tested objectively.[31] The abnormality can take on any means or manner and includes the chosen payment method, the structure of the agreement or the status of the parties to the agreement. In this regard, one must consider whether the use of cryptocurrencies would be considered as “abnormal” for purposes of section 80A.

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27 S 80L(a)(ii) of IT Act.
28 S 80C(1).
29 This paragraph must be read with paragraph 4.3.3.
30 De Koker A *et al* (2018) Silke on South African Income Tax Chapter 19: Tax Avoidance par 19.39.
31 De Koker (2018) par 19.39.

Section 80A(a)(i) also requires that the arrangement must be employed in a *bona fide* purpose of furtherance of the business. The avoidance provisions are not triggered if the benefit is obtained through the ordinary course of business.[32] Thus, a tax benefit which was not the sole purpose of the transaction is permissible.[33] Once again it is reiterated that this provision relates to the form of the transaction and not to the commercial substance of the transaction. The use of the word "purpose" in this context relates to the manner in which the transaction is executed.[34] Therefore, the test is a comparison between the impugned transaction and the normal manner of carrying out the transaction.[35]

When one considers the form of the transaction it must be kept in mind that cryptocurrencies are used in a digital world and mostly in the context of e-commerce. In the context of e-commerce, the structure of the agreement might not be traditional (meaning written on paper) and may take on many forms such as digital requests sent between a purchaser and a seller.[36] As society progress towards a digitalised world, the consumer behaviour will change.[37] This could result in the exchange of cryptocurrencies as a trade or as a means of value, might be considered to be "normal" and it will then not trigger the anti-avoidance provisions. The problem is that the issue of misuse of cryptocurrencies and related transactions remains unaddressed.

The problem arises when ordinary businessmen,[38] deliberately use cryptocurrency to enter into commercial transactions to avoid the tax consequences that they would have incurred had they entered into a normal agreement. For instance, if a sale of a business is concluded to which the roll-over relief mechanisms do not apply, and the purchase price is paid by means of cryptocurrencies to avoid the capital gains taxes on the receipt of the purchase price. In that scenario the use of the cryptocurrency is abnormal and that would trigger the requirement of section 80A(a)(i). In the example,

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32 De Koker (2018) par 19.39.
33 De Koker (2018) par 19.39.
34 De Koker (2018) par 19.39.
35 De Koker (2018) par 19.39.
36 Van Zyl, SP (2014) Vol XLVII No 2 The collection of Value Added Tax on Cross-Border Digital Trade-Part 1 : Registration of Foreign Vendors *The Comparative and International Law Journal of Southern Africa* 154 pg. 155.
37 Van Zyl (2014) pg.155.
38 Reference to one gender will include the other, unless otherwise indicated or appears from the context otherwise.

the form used is solely to obtain a tax benefit, which is the avoidance of the liability to account for capital gains tax. It is important to note that this requirement does not relate to the commercial sense of the transaction and only focus on the form or structure of the transaction. Thus, when determining whether the use of cryptocurrencies change the form of the transaction it must be compared to what the consequences of the actual transaction would have been.

The problem is that there is no general obligation to report the use of cryptocurrencies, and the anti-avoidance provisions can be evaded and thereby the efficacy of the provisions are destroyed.

4.3.3 SECTION 80A(a)(ii)

The second part of section 80A(a)(ii) reads as follows:

> (a) In the context of business—
>
> (ii) it lacks commercial substance, in whole or in part, taking into account the provisions of section 80C;

Commercial sense or substance means that the transaction must make sense from a business perspective. In other words, the transaction must be for the benefit of the taxpaying company or taxpayer in a manner that would for example likely increase profitability, increase the cash flow or sustain future developments.

The legislature highlighted certain specific factors which are indicative of an arrangement that would lack commercial substance in section 80C(2), although the listed arrangements is not a closed list. These factors include:

a) If the effect of the transaction is inconsistent with the legal form of the steps forming the transaction;[39]
b) The inclusion of funds through roundtrip financing in the transaction;[40]
c) The accommodating of a tax indifferent party;[41] or

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[39] S 80C(2)(a) of the IT Act.
[40] S 80C(2)(b)(i) of the IT Act.
[41] S 80C(2)(b)(ii) of the IT Act.

d) The transaction involves elements that effect off-setting.[42]

As alluded to above, the provisions of the IT Act must be contextualised to understand its true meaning. To understand the application of section 80A(a)(ii) the provisions of section 80C must be considered. In what follows the factors listed above are discussed to evaluate the application of the provisions to cryptocurrencies.

4.3.3.1 Section 80C(2)(b)(i): The legal form of the transaction

The first factor indicative of an avoidance arrangement that lacks commercial substance once again relates to the form of the transaction. In the case of *Dadoo and others v Krugersdorp Municipal Council*[43] the court held that there is in principle nothing wrong with parties arranging their affairs to fall outside the application of certain provisions.[44] Thus, the mere fact that an arrangement operates outside the ambit of certain provisions does not necessarily mean that it lacks commercial substance. The court went further to state that the problem is when the arrangement falls within the ambit of a provision and both the parties disguise it as something else to preclude the relevant tax provisions. In that circumstance, the courts are entitled to consider the substance of the agreement over the form of the agreement.[45] In the case of *Zandberg v Van Zyl*,[46] the court held that it must be established that there exists a real intention between the parties to enter into an agreement which intention is different from the simulated intention.[47] Thus, the court must consider whether there is a sound commercial reason for the transaction other than to obtain a tax benefit and the form of the transaction is irrelevant.

Section 80C(2)(a)(i) concludes that there is a presumption that an arrangement which is abnormal will be considered to be without commercial substance. Thus, if parties conclude a transaction with cryptocurrencies either as the subject of the transaction or

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42 S 80C(2)(b)(iii) of the IT Act.
43 *Dadoo and others v Krugersdorp Municipal Council* 1920 AD 530.
44 *Dadoo* pg. 548.
45 *Dadoo* pg. 548. See also *CSARS V NWK Ltd* 2011 (2) SA 67 (SCA) which is discussed below in par 4.3.2.3.
46 *Zandberg v Van Zyl* 1910 AD 302.
47 *Zandberg* at 309.

as the payment terms and it is not likely to be used in the ordinary course of business it would be presumed that the transaction lacks commercial substance.

4.3.3.2 Section 80C(2)(b)(ii): Round-trip financing

Section 80C(2)(b)(ii) must be read with section 80D which regulates round-trip financing schemes. Round trip financing means that funds are transferred between parties that would reduce the tax liability. The aim of section 80D is to eliminate arrangements in which there is no genuine business arrangement and no actual flow of money.

It is important to note that section 80D provides for “funds” transferred in terms of round-trip financing scheme. The term ‘funds” is defined in section 80D(3) as “cash or cash equivalents or any right or obligation to receive or pay the same”.

The definition of “funds” does not include cryptocurrencies since cryptocurrencies are not considered to be legal tender. This means that cryptocurrencies used in a round-trip financing scheme will not be subject to the anti-avoidance provisions. The risk is that the taxpayer will be able to move his or her cryptocurrencies without really parting with the benefit thereof and obtain a tax benefit. This effectively creates a tax shelter for the users of cryptocurrencies.

Round trip financing is an indicator of lack of commercial substance in section 80C(1)(b) if it complies with section 80D. Section 80C(1)(b) refers the taxpayer to the provisions of section 80D which was shown to be inapplicable to cryptocurrencies. It is submitted that the IT Act through the inclusion of round-trip financing in section 80C(1)(b)(i) and the specific provisions of section 80D is directory in nature. Thus, the broad scope of section 80C does not apply to round trip financing in respect of cryptocurrencies.

4.3.2.3 Section 80C(2)(b)(iii): A tax indifferent party

The third factor indicative of an arrangement that lacks commercial substance is when a tax indifferent party is involved.[48] Section 80C(2)(b)(iii) must be read with section 80E. To accommodate a tax indifferent party means that the party that receives the amount is not subject to normal tax or is entitled to offset the loss against the amount received. The result, if the anti-avoidance provisions apply, is that the amount would give rise to revenue or capital gains and be subject to tax. [49]

There are two exclusions in section 80E which would provide relief against the anti-avoidance provisions. The first exclusion is if the amount is subject to tax as foreign income tax in a different jurisdiction. The second exclusion is if the party actively engage in trading activities in connection with the avoidance arrangement for at least 18 months. The second exclusion is subject to limitation since the trading activities must be linked to a principal place of business or premises that would constitute a "foreign business establishment".[50]

Section 80C(2)(b)(ii) provides for a tax indifferent "party" and not a tax indifferent "asset". This is important because it sets the scene for the application of the provision. Thus, the party receiving the benefit must not be subject to the IT Act. Section 80L defines "party" as "any person, permanent establishment in the Republic of a person who is not a resident, permanent establishment outside the Republic of a person who is a resident, partnership, or joint venture".[51] There is no mention of the nature of the benefit received for purposes of application of the provision. The provision does not provide for a benefit received with no tax obligation. Thus, the possibility exists that the application of section 80A(a)(ii) is excluded in respect of cryptocurrency. Consequently, the anti-avoidance provisions will not aid in preventing tax evasion offences committed through the use of cryptocurrencies.

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[48] S80C(2)(b)(iii) of the IT Act.
[49] De Koker (2018) par 19.39.
[50] S 80E(4).
[51] S 80L(a)-(e).

When one considers the status of cryptocurrencies as not being regarded as legal tender, the fact that it operates in a digital world and it is anonymous the application of this provision proves to be difficult. This difficulty relates to the identification of cryptocurrencies and the classification thereof. The application of this provision to the use and trade of cryptocurrencies is hampered by the fact that SARS must first be able to identify the cryptocurrency in the hands of the taxpayer before this provision can be applied.

Although the income gained from trading in cryptocurrency may still form part of the taxpayer's gross income there exists no double-taxation agreement between South Africa and other jurisdictions in respect of cryptocurrency trading and cryptocurrency transactions. This means that the taxpayer is at risk of a tax duty in multiple jurisdictions for the same profit.

The question is then whether a taxpayer that trades in cryptocurrencies will be regarded as a tax indifferent party since the income or profit will not be included in the gross income or the proceeds for purposes of capital gains taxes due to the difficulties in applying the current tax provisions to cryptocurrencies. The difficulty is also that the taxpayer as the "party" may not necessarily tax indifferent, but SARS is unable to identify the cryptocurrency as there is no general reporting duty for cryptocurrency transactions.

Section 80A(a) read with the listed factors indicative of an avoidance arrangement is a mirror image of the common law rule of substance over form.[52] In the case of *CSARS v NWK,*[53] the court decided the matter on the common law rule of substance over form instead of the anti-avoidance provisions. In this case, First National Bank ("FNB") advanced an amount of 96 million rands to the taxpayer. The loan was repayable over five years when the taxpayer would deliver maize to FNB. The parties agreed that interest would be calculated per annum. The taxpayer then made deductions in respect of the interest from a subsidiary company. The court considered the concept of a simulated transaction".[54] The court indicated that the question is whether the

52 De Koker (2018) par 19.39.
53 *CSARS V NWK Ltd* 2011 (2) SA 67 (SCA) ("NWK").
54 *NWK* pg. 68.

transaction makes commercial sense.[55] The court held that the test to determine whether a transaction is simulated is the purpose of the transaction.[56] The court went further to state that a transaction will be regarded as simulated if the only purpose was to obtain a tax benefit irrespective whether there was actual performance of the agreement.[57]

In *CSARS v Bosch,*[58] the taxpayers exercised contractual options given to them by their employer in terms of a deferred deliver share incentive scheme. The option was to purchase shares in the employer's middle-market company. The taxpayers could instead of taking delivery of the shares, dispose of the shares and keep the balance after deduction of the cost of sale of the shares.[59] In the present case, Mrs Bosch elected to dispose of the shares and to receive the proceeds, whilst Mr McClelland transferred the shares and paid the consideration.[60] The taxpayers contended that they exercised a right to acquire shares and that payment and delivery were postponed.[61] The question was whether the taxpayer exercised an option as contemplated in section 8 of the Income Tax Act.[62] The court held that the court must consider all factors relevant to the dispute to reach its conclusions and among these considerations is the tax consequence of a transaction.[63] The court held that the taxpayer must have gained an advantage for the substance over form rule to apply.[64] As a result, the court held that the taxpayer gained an advantage since they could have exercised their rights without any postponement of payment and delivery.[65]

In the recent case of *Sasol Oil Proprietary Limited v CSARS*,[66] the court had to consider the test for a simulated transaction and the rule of substance over form in

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55 *NWK* pg.81.
56 *NWK* pg. 80.
57 *NWK* pg. 80. See also Legwaila T, (2016) "The substance over form doctrine in taxation: The application of the doctrine after the judgment in commissioner for the *South African Revenue Service v NWK Ltd* 2011 (2) SA 67 (SCA)" *MERC LJ* 112 pg.115.
58 *Commissioner, South African Revenue Service v Bosch And Another* 2015 (2) SA 174 (SCA).
59 *Bosch* pg. 177 -178.
60 *Bosch* pg. 179.
61 *Bosch* pg. 179.
62 *Bosch* pg. 180.
63 *Bosch* pg. 192.
64 *Bosch* pg. 192.
65 *Bosch* pg. 192.
66 *Sasol Oil Proprietary Limited v CSARS* (923/2017) 2018 ZASCA 153 (9 November 2018).

respect of a series of transactions within the same group of companies.[67] The contracts in issue were entered into between Sasol Oil and Sasol International Services Limited (SISL) and in turn between SISL and Sasol Oil International Limited (SOIL). SOIL is a company incorporated in the Isle of Man. SISL is a United Kingdom group of companies. SOIL sold oil to SISL who in turn sold to Sasol Oil. The gist of the issue is that if SOIL sold directly to Sasol Oil the provisions related controlled foreign companies would apply and Sasol Oil will be liable for tax. In the current structure, Sasol Oil has a reduced tax liability.[68] The Commissioner contended that the agreements were simulated and that there was no commercial reason for the agreements and the scheme was introduced to obtain a tax benefit.[69]

The majority court held that the test in the *NWK*-case suggests that the contract terms, the probabilities and context of the terms must be considered. In the circumstances there existed sound commercial reasons for the agreements. The court held that there was no obligation on SOIL to procure oil to sell to Sasol Oil and even if SOIL did sell to Sasol Oil it does not automatically render the agreements abnormal and a simulation.[70] The court considered that in the oil industry it is not abnormal for groups of companies to implement these type of restructurings of agreements to obtain savings and tax benefits.[71] In the separate, but concurring majority judgement of Ponnan, JA it was held that the evidence surrounding the impugned transactions must be viewed holistically and not in piecemeal.[72]

It is clear that to determine the commercial substance of a crypto-transaction that the transaction as a whole must be considered. However, the problem of identification of cryptocurrencies and related transactions still subsist.

[67] *Sasol Oil* par 1 and 2.
[68] *Sasol Oil* par 3-6.
[69] *Sasol Oil* par 52.
[70] *Sasol Oil* par 91.
[71] *Sasol Oil* par 80.
[72] *Sasol Oil* par 144.

4.3.4 SECTION 80A(b) AND (c): THE ANTI-AVOIDANCE PROVISIONS IN ANY OTHER CONTEXT THAN "BUSINESS"

Section 80A(b) and (c) provide:

> "(b) In a context other than business, it was entered into or carried out by means or in a manner which would not normally be employed for a *bona fide* purpose, other than obtaining a tax benefit; or
>
> (c)in any context—
>
> (i) it has created rights or obligations that would not normally be created between persons dealing at arm's length; or
>
> (ii) it would result directly or indirectly in the misuse or abuse of the provisions of this Act"

In contrast to what is described above, section 80A(b) does not provide for an inquiry into the "business purpose" or the commercial substance of the arrangement. The only test which is applied is whether a tax benefit was obtained.[73]

In section 80A(c) there is no mentioned of the commercial substance of the agreement or purpose, the only requirement is that the arrangement would have resulted in creating abnormal rights and obligations for parties dealing at arms' length or resulting in misuse or abuse of the IT Act.[74] Thus, the scope of application of these provisions is much wider than the scope of section 80A(a).

For arrangements in any other context than business, the form of the transaction is not the determining factor, but whether there was a misuse or abuse of the provisions of the IT Act.[75] The use of the terms "misuse" and "abuse" stems from the Canadian Income Tax which is used to determine whether there was a *bona fide* purpose.[76] Unlike the Canadian Income Tax Act, the overarching requirement for the application of the anti-avoidance provisions in section 80A is whether the arrangement was

[73] De Koker (2018) par 19.39.
[74] De Koker (2018) par 19.39.
[75] De Koker (2018) par 19.39.
[76] S 245(4) Canadian Income Tax Act. *Canada Trustco Mortgage Co. v Canada* 2005 SCC 54. See also De Koker (2018) par 19.39.

entered into with the sole purpose of obtaining a tax benefit.[77] The problem the wording in section 80A(b) and (c) creates is that the misuse and abuse of the provisions of the Act might be present whilst the anti-avoidance provisions are not triggered.[78]

When applying these provisions, one must constantly be reminded that cryptocurrencies are used mainly in a business setting and therefore these provisions do not really assist in the regulation of cryptocurrency.

4.3.5 SECTION 80B - THE TAX CONSEQUENCES OF IMPERMISSIBLE TAX AVOIDANCE

The main consequence of the avoidance provisions is that the arrangement is disregarded, and the normal tax consequences will follow. Thus, if the avoidance arrangement, for example, resulted in an amount to be excluded from the calculation the amount will now be included.[79]

These consequences will naturally only follow once SARS has been successful in identifying the impermissible avoidance arrangement and by extent the cryptocurrencies.

Thus, the conundrum the legislature finds itself in is that it cannot effectively identify the cryptocurrencies in the hands of the taxpayer, and in circumstances when the cryptocurrency was identified, the anti-avoidance provisions' application is problematic.

4.4 THE ANTI-AVOIDANCE PROVISIONS IN THE TAX ADMINISTRATION ACT 28 OF 2011 ("TAA")

The provisions of the IT Act discussed above, are not the only avoidance arrangements within the South African tax legislative framework. The TAA was

[77] S 80A Income Tax Act.
[78] De Koker (2018) par 19.39.
[79] S 80B(d) IT Act.

assented to on 2 July 2012 and the date of commencement was 1 October 2012. The purpose of the TAA is to enhance tax collection.[80]

To achieve this purpose the Act, provide *inter alia* for reportable arrangements and it criminalises tax evasion.[81] The provisions of the TAA must be read in conjunction with the IT Act and not as an alternative.[82] Section 4 of the TAA provides that any inconsistency between a tax Act and the TAA must be interpreted to give effect to the relevant tax Act.

4.4.1 SECTION 34 TO 36- REPORTABLE ARRANGEMENTS

The TAA introduces a reporting duty in respect of certain "reportable arrangements" in section 34 to 36.

The purpose of the introduction of a reportable arrangement is to enable SARS to determine whether the anti-avoidance provisions must be applied to a certain set of facts.[83] The aim of sections 35 is to create reporting duty in respect of the terms of the arrangement, the tax benefit and the identity of the parties involved.[84]

4.4.1.1 SECTION 35 - REQUIREMENTS FOR A REPORTABLE ARRANGEMENT

Section 35 introduces the reportable arrangements and reads as follow:

> "(1) An 'arrangement' is a 'reportable arrangement' if a person is a 'participant' in the 'arrangement' and the 'arrangement'-
>
> (a) contains provisions in terms of which the calculation of interest as defined in section 24J of the Income Tax Act, finance costs, fees or any other charges is wholly or partly dependent on the assumptions relating to the tax treatment of that 'arrangement' (otherwise than by reason of any change in the provisions of a tax Act);

80 S 2 and preamble of TAA.
81 S 34 and 235 TAA.
82 S 4 of TAA.
83 De Koker (2018) par 18.87.
84 S 38 of TAA. See also De Koker (2018) par 18.87.

(b) has any of the characteristics contemplated in section 80C (2) (b) of the Income Tax Act, or substantially similar characteristics;

(c) gives rise to an amount that is or will be disclosed by any 'participant' in any year of assessment or over the term of the 'arrangement' as-

(i) a deduction for purposes of the Income Tax Act but not as an expense for purposes of 'financial reporting standards'; or

(ii) revenue for purposes of 'financial reporting standards' but not as gross income for purposes of the Income Tax Act;

(d) does not result in a reasonable expectation of a 'pre-tax profit' for any 'participant'; or

(e) results in a reasonable expectation of a 'pre-tax profit' for any 'participant' that is less than the value of that 'tax benefit' to that 'participant' if both are discounted to a present value at the end of the first year of assessment when that 'tax benefit' is or will be derived or is assumed to be derived, using consistent assumptions and a reasonable discount rate for that 'participant'."

The operative terms for section 35 are as follows:

a) There must be an "arrangement;"
b) The arrangement must be "reportable" in terms of section 35(1) and (2) of the Act; and
c) The taxpayer must be a "participant" in the arrangement.

The operative terms are defined in section 34 of the TAA. As stated above, when interpreting legislation, the context of the provision must be considered to determine the application. In this instance, the definitions contained in section 34 provides this context and is prudent in the interpretation of section 35.

4.4.2 SECTION 34 – DEFINITIONS

4.4.2.1 MEANING AND DEFINITION OF "ARRANGEMENT"

An "arrangement" refers to any "transaction, operation, scheme, agreement or understanding (whether enforceable or not)."[85] It is noteworthy that this is the same definition as that which can be found in the IT Act. Accordingly, the interpretation of this term is consistent with what is already discussed above.

[85] S 34 of TAA.

4.4.2.2 MEANING AND DEFINITION OF "REPORTABLE"

The TAA does not define the term "reportable" before introducing section 35 which deals with reportable arrangements. Therefore, the discussion on the meaning and definition of "reportable" will be included in the discussion of section 35.

4.4.2.3 MEANING AND DEFINITION OF "PARTICIPANT"

The taxpayer is a "participant" if he or she is either responsible for the general organising and management of the transaction alternatively if he or she stands to obtain a tax benefit (directly or indirectly) from the transaction.[86] It is also important to understand the meaning and circumstances when the taxpayer will obtain a "tax benefit." A tax benefit in the context of a reportable arrangement means the avoidance or evasion of the tax or a reduction of the amount of tax payable by the taxpayer.[87]

4.4.3 SECTION 35 - FACTORS INDICATIVE OF REPORTABLE ARRANGEMENTS

An arrangement is considered "reportable" in terms of section 35(1) if:

1. The calculation of interest and costs are wholly or partially dependant on the tax treatment of the arrangement;[88]
2. It has characteristics of an agreement in terms of section 80C(2)(b) of the IT Act;[89]
3. It gives rise to an amount that a participant will disclose as either a deduction for income tax or as revenue in terms of "financial reporting standards;"[90]
4. It does not result in a pre-tax profit for any participant;[91] or

[86] S 34 of TAA.
[87] S 34 of TAA.
[88] S 35(1)(a) TAA.
[89] S 35(1)(b) of the TAA.
[90] S 35(1)(c)(i) and (ii) of TAA.
[91] S 35(1)(d) of TAA.

5. It results in a reasonable expectation of pre-tax profit that is less than the value of the tax benefit.[92]

For purposes of cryptocurrencies and related transactions, the only factor that may aid in creating a reporting duty is that of section 35(1)(b). The reason for this is that the remainder of the factors rely on the fact that the arrangement or the subject matter of the arrangement can be identified by SARS. The problem with the reporting duty related to cryptocurrency is that it must be all-encompassing and cannot be limited to certain scenarios.

Section 35(1)(b) provides that where the transaction has similar characteristics of section 80C of the IT Act, the arrangement will be reportable. Thus, the arrangement must lack commercial substance. Without repeating the above discussion of commercial substance, the difficulty in applying this provision to cryptocurrencies remains the same as stated above. Thus, section 35 does not aid in creating a general reporting duty for arrangements involving cryptocurrencies for the same reasons as indicated earlier. A further problem that arises is the section dealing with the excluded arrangements in section 36, which will be canvassed below.

4.4.4 SECTION 36 -THE EXCLUDED ARRANGEMENTS

There are four categories of arrangements that are excluded from the list of reportable arrangements in terms of section 36.

a) Arrangements that constitute a debt which is repayable or the asset returnable on a future determined date;[93]
b) Leases;[94]
c) A transaction though exchange in terms of the Financial Markets Act 19 of 2012;[95] or

[92] S 35(1)(e) of TAA.
[93] S 36(1)(a)(i) and (ii) of TAA.
[94] S 36(1)(b) of TAA.
[95] S 36(1)(c) of TAA.

d) a transaction in participatory interest in a scheme in terms of the collective investment schemes control act 45 of 2005. [96]

These exclusions exist irrespective of whether the arrangements are concluded as a once-off transaction or as part of a series of transactions.[97] However, the exclusions are not applicable if the transaction was entered with the main purpose of obtaining a “tax benefit”.[98] In this regard, the application section 36(3) is discussed followed by section 36(4).

4.4.4.1 SECTION 36(3)

Section 36(3) reads as follows:

> “(3) Subsection (1) does not apply to an 'arrangement' that is entered into-
>
> (a) with the main purpose or one of its main purposes of obtaining or enhancing a 'tax benefit'; or
>
> (b) in a specific manner or form that enhances or will enhance a 'tax benefit'.”

The overarching requirement is that the purpose of the arrangement must be to obtain a tax benefit. In what follows the concept of “tax benefit” and “purpose of the arrangement” must be considered to place the section 36(3) in context.

4.4.4.2 A “TAX BENEFIT”

Once again, the definition of a “tax benefit” is a mirror of the IT Act. The acquisition of a tax benefit is not the determining factor to determine whether the IT Act’s anti-avoidance provisions apply. As alluded to above, the obtainment of a tax benefit must be accompanied by a transaction that is abnormal in the ordinary course of business

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96 S 36(1)(d) of TAA.
97 S 36(2)(a) of the TAA.
98 S 36(3) of TAA.

or it must lack commercial substance.[99] Therefore, the fact that the arrangement's purpose is to obtain a tax benefit, triggers section 35(1) of the TAA.

4.4.4.3 "PURPOSE OF THE ARRANGEMENT"

The legislature uses the word "purpose" in section 36(3). The context of this provision is that the intention of the taxpayer must be to obtain a tax benefit. The phrase "purpose of the arrangement" in section 36(3) turns to the question of the taxpayer's intention when entering into the transaction. To determine the intention of the taxpayer the South African courts have laid down a number of factors to be considered.[100]

In the case of *Elandsheuwel Farming (EDMS) Bpk v Secretary for Inland Revenue*[101] the Appellate division, as it was then known, also considered when a taxpayer had the intention to use the property as a capital investment. In the case of *Elandheuwel Farming,* the appellant entered into a pre-incorporation agreement with a third party in respect of a portion of the farm called Elandsheuwel. A change in ownership of the appellant led to the farm being subdivided and sold by a developer.[102] The court held that a change in shareholders may change the intention of the taxpayer and that the proceeds of the sale may then be included in the taxpayer's gross income.[103] The court went further by stating that to determine the intention of the taxpayer the following factors must be considered:

a) The activities carried on by the taxpayer in respect of the asset;
b) The reason for the realisation of the asset;
c) The manner of realisation of the asset;
d) The length of time the asset was held;
e) The other activities conducted by the taxpayer; and

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[99] S 80A of IT Act.
[100] These factors are similar to the factors considered by the Canadian courts. See Chapter 3 paragraph 3.2.1.
[101] *Elandsheuwel Farming (EDMS) Bpk v Secretary for Inland Revenue* 1978 (1) SA 101 (A).
[102] *Elandsheuwel Farming* pg. 108.
[103] *Elandsheuwel Farming* pg. 127-128.

f) The frequency of similar transactions.[104]

In *Natal Estates Ltd v Secretary for Inland Revenue,*[105] the taxpayer was the owner of a property on which sugar cane was farmed. The taxpayer entered into two transactions. The first transaction consisted of the selling of part of the land. The second transaction consisted of the developing of the land into real estate. The court held that the taxpayer's intention to realise the land in the first transaction did not change to that of an income generating activity and that the proceeds of the sale will be considered as capital in nature and excluded from the taxpayer's income. In terms of the second transaction, the court held that the taxpayer's intention changed to generate income. The court held that the factors to be considered whether the taxpayer intends to use the asset as a so-called capital asset or whether it is income in nature. The court highlighted the following considerations:

a) The intention of the owner both when the asset was acquired and when it was sold;

b) The activities carried on by the taxpayer leading up to the disposal of the property;

c) The *ipse dixit* of the taxpayer;

d) The organisation and marketing of the enterprise carried on by the taxpayer; and

e) The relationship of the aforementioned and the commercial concept of carrying on a trade.

Therefore, when determining whether there was the intention to obtain a tax benefit, the matter must be viewed holistically considering the abovementioned factors.[106]

In the absence of a reporting duty in the current South African regulatory framework, the application of these factors is hindered by the anonymous nature of cryptocurrencies. However, once the cryptocurrency transaction is identified it should, at least in theory, be possible to apply the listed factors to determine the intention of the taxpayer and whether the intention to obtain a tax benefit was present.

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[104] *Elandsheuwel Farming* pg.125-126. See also Griessel R *"Nature of the Proceeds Derived from the Sale of an Asset for the purposes of Income Tax"* (1997) SA Merc LJ 138 at pg. 144-150. See also Croome (2013) pg. 86.

[105] *Natal Estates Ltd v Secretary for Inland Revenue* 1975 (4) SA 177 (A).

[106] A discussion on the principles related to the determination of a taxpayer's intention falls outside the ambit of this dissertation.

4.4.4.4 SECTION 36(4)

Section 36(4) reads as follows:

> "(4) The Commissioner may determine an 'arrangement' to be an excluded 'arrangement' by public notice."

A further complication is the fact that reportable arrangements have a monetary threshold.

On 16 March 2015 the Commissioner of SARS determined in accordance with section 36(4) that any reportable arrangement in terms of section 35(1) will be excluded if the value of such transaction is below R5 million.[107] The implication is that irrespective of whether the arrangement was entered into for the sole purpose of obtaining a tax benefit or if it constitutes the abuse or misuse of the provisions, if the monetary value is below R5 million there is no reporting duty.

Thus, the application of the IT Act's anti-avoidance provisions and the avoidance provisions contained in the TAA are negated. In the context of cryptocurrencies and related transactions, this is a major concern since the taxpayer can consider each cryptocurrency transaction separately enabling him or her to come in below the monetary threshold. The result is that no obligation to disclose the arrangement is created.

The interpretation of section 34, 35 and 36 is that if an arrangement shares characteristics with an arrangement under section 80C of the IT Act, the transaction will be a reportable arrangement. In this regard, one should note that the inverse of this interpretation does not create the same duty. Thus, a transaction can trigger the anti-avoidance provisions but there is no obligation to report the transaction due to the restricting monetary threshold.

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[107] GN 212 GG 38569 dated 16 March 2015.

4.4.5 SECTION 235 TAX EVASION

Section 235 states that any person who intentionally evades or assist another to evade tax or to obtain an undue benefit is guilty of a criminal offence. The following actions are included in the act of tax evasion:[108]

> " a) The making of a false statement or entry in a return without reasonable grounds for believing the same to be true;
>
> b) By giving a false answer, whether orally or in writing, to a request for information made under this Act;
>
> c) To prepare, maintain or authorise the preparation or maintenance of false books of account or other records
>
> d) To make use of or to authorise fraud or contrivance;
>
> e) To make any false statement for the purposes of obtaining any refund of or exemption from tax."

The criminalisation of tax evasion is an incentive for taxpayers to comply with the provisions of the tax Acts. Although the non-disclosure of cryptocurrencies might be brought within the ambit of section 235 as making a false state or return, the issue is that there is no obligation to disclose the cryptocurrencies. As a result, the statements made by taxpayers cannot be verified to enable SAR to ascertain whether an offence was committed.

Consequently, the offence in terms of section 235 is only a deterrent if there is an obligation to disclose transactions pertaining to cryptocurrencies. In this regard, one must consider whether a reporting duty similar to the that in in the Financial Intelligence Centre Act 31 of 2001 ("FICA") should be imported in the tax legislation. The reporting duties in the FICA will be discussed in Chapter 5 as a possible remedy for the current problem relating to cryptocurrencies.

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[108] S 235(1)(a) –(e) of TAA.

4.5 CURRENT DEVELOPMENTS IN THE SOUTH AFRICAN TAX LEGISLATIVE FRAMEWORK RELATED TO CRYPTOCURRENCIES

As stated earlier,[109] in the 2018 Budget Speech the then Minister of Finance, Gigaba, indicated that the regulation of cryptocurrencies will be addressed.[110]

SARS indicated on 6 April 2018 that the normal tax rules will be applicable to cryptocurrencies. Taxpayers are also expected to declare cryptocurrency gains or losses as part of their taxable income.[111]

Although cryptocurrencies do not constitute cash and it is not regarded as legal tender, they do possess a value and as should be subject to tax. The determination of whether a receipt or accrual is revenue or capital in nature will be determined by the existing jurisprudence. Taxpayers will be entitled to deduct expenses which are incurred in the production of the taxpayers' income.[112]

The receipts or accruals that do not form part of "gross income" will be regarded as capital gains. Base cost adjustment will be made in accordance with the Capital Gains Tax framework.[113]

The discussion on whether cryptocurrencies are classified as revenue or capital in nature is beyond the scope of this dissertation. What is clear though, is that irrespective of the classification of cryptocurrencies, the provisions relating to the duty to report and the consequences of a failure to do so falls short to adequately prevent tax evasion and to limit tax avoidance.

On 6 July 2018, the South African National Treasury introduced a Draft Taxation Law Amendment Bill ("TLAB"),[114] in which cryptocurrencies are addressed. The TLAB addresses cryptocurrencies in the following respects:

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[109] Chapter 1 paragraph 1.1.
[110] 2018 Budget Speech at 21.
[111] SARS' Stance On The Tax Treatment Of Cryptocurrencies- 6 April 2018 http://www.sars.gov.za/Media/MediaReleases/Pg.s/6-April-2018---SARS-stance-on-the-tax-treatment-of-cryptocurrencies-.aspx .
[112] SARS (2018).
[113] SARS (2018).
[114] National Treasury Draft Taxation Law Amendment Bill (TLAB) dated 16 July 2018.

a) By introducing cryptocurrencies as part of the definition of a "financial instrument" in a section of the IT Act;[115]

b) The inclusion of the acquisition or disposal of cryptocurrency as a trade whose assessed losses are ring-fenced;[116] and

c) The inclusion of the issue, acquisition or disposal of cryptocurrencies in the definition of "financial services" in the Value-Added-Tax Act.[117]

To understand the effect of the proposed inclusions one must consider the contextual setting of the provisions to be amended.

4.5.1 SECTION 1 - INCLUSION OF CRYPTOCURRENCIES AS A FINANCIAL INTRUMENT

The inclusion of cryptocurrency in the definition of a "financial instrument" will place cryptocurrencies in the same category as debts, loans and stocks.[118]

This proposed status of cryptocurrency will have the effect that transactions related thereto will be considered excluded arrangements for purposes of reportable arrangements under the TAA.[119] Thus, the use of cryptocurrencies as financial instruments will not be reportable, which might result in the tax consequences thereof not being accounted for.

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115 See S 1 of IT Act and TLAB pg. 3.
116 See S 20A of IT Act and TLAB pg. 40.
117 S 2 of Value-Added Tax Act 89 of 1991 and TLB pg. 76.
118 S1 of IT Act "Financial instrument". See also Gogo J (2018) South Africa's Draft Tax Law Could Affect Cryptocurrency Use at https://news.bitcoin.com/law-firm-south-africas-draft-tax-law-could-affect-cryptocurrency-use/ (accessed on 26 November 2018).
119 S 36 of TAA.

4.5.2 SECTION 20A - RING FENCING OF ASSESSED LOSSES OF CERTAIN TRADES

Section 20 provides that where a natural person's taxable income is calculated certain amounts may be deducted against the income derived.[120] The amount that may be deducted is either the balance of an assessed loss incurred in the previous year of assessment or an assessed loss in the same year of assessment in respect of any other trade.[121]

Section 20A provides for a list of so-called "suspect trades" in which the deduction of an assessed loss from any other trade than those listed are prohibited.[122] The effect of Section 20A is to limit the instances in which assessed losses may be deducted.[123]

The effect of including the trade in cryptocurrencies in section 20A is that crypto-transactions will be considered a "suspect trade" and the losses incurred may only be deducted from the income generated from the trade. Thus, the taxpayer will not be able to deduct the loss incurred from the trade in cryptocurrencies from his or her total income (inclusive all income-earning activities). Due to the volatile fluctuations in the value of cryptocurrencies losses are often expected and the proposed inclusion of crypto-transactions will limit the deduction of those losses.[124] Accordingly, the SARS revenue collection targets will not be influenced.[125]

The taxpayer is obliged to disclose the nature of his business.[126] Section 20A(8) incorporates the reporting of suspect trades in the taxpayer's annual return. The inclusion of cryptocurrencies in the "suspect trade" list will require disclosure of the

[120] S 20 of IT Act. See Also Stiglingh (2018) pg. 140.
[121] S 20(1)(a) read with s20(2A)(a) and S 20(1)(b) read with s 20(2A)(b) of IT Act.
[122] S 20A(2)(b).
[123] Stiglingh (2018) pg. 142.
[124] Toost T (2018) Understanding tax amendments for cryptocurrencies at http://www.itnewsafrica.com/2018/07/understanding-tax-amendments-for-cryptocurrencies/ (accessed on 26 November 2018).
[125] Toost (2018).
[126] S 20A(8).

trade in cryptocurrencies by individuals who trade in cryptocurrencies and who intends to deduct losses from their income associated with the trade.

It is submitted that the inclusion of cryptocurrency transactions in section 20A is a step in the right direction to regulate the trading in cryptocurrencies from a tax perspective. South Africa follows a self-assessment regime since taxpayers are required to submit their annual return to SARS for an assessment. Therefore, the inclusion of crypto transactions in the IT Act means that a failure to comply with the relevant tax acts, that requires a declaration crypto-transactions, will result in penalties and criminal sanctions.

4.6 CONCLUSION

It is evident from the above evaluation that there are no pre-emptory or directory provisions relating to cryptocurrencies. Furthermore, by applying the *contra fiscum*-rule in determining whether a transaction involving cryptocurrencies triggers the anti-avoidance provisions, the benefit of the doubt will be in favour of the taxpayer. It is submitted that, in the current South African tax dispensation, there is no general reporting duty aimed at cryptocurrencies that brings it within the ambit of the IT Act or the TAA to prevent tax evasion and to limit tax avoidance.

It is suggested that to avoid doubt or absurdities that the legislature must consider importing a general reporting duty relating to any transaction involving cryptocurrencies. As alluded to above, the South African government has taken steps to include cryptocurrencies in the tax legislative framework. It is submitted, that these steps are baby steps and will not be sufficient to address the issue of proper regulation of cryptocurrencies. It is recommended that more radical steps are required to deal with the increasing popularity of cryptocurrencies.

It is recognised that the burden of a general and all-encompassing reporting duty will increase the administrative burden of the state which may result in increased costs associated with revenue collection. It is submitted that by the implementation of proper

technology and information systems this burden can be alleviated. In this regard, one must consider the fact that the United States of America's IRS uses blockchain technology to alleviate the burden of sifting through the transactions for purposes of preventing tax evasion.[127]

Consequently, the technology to aid SARS is available and must be implemented to combat tax evasion in respect of cryptocurrencies. The implementation of innovative technology and systems to track cryptocurrency will require the training of units to combat offences related to the use of cryptocurrency.[128]

[127] See Chapter 3 paragraph 3.2 and 3.3.
[128] Van Jaarsveld I (2004) pg. 702.

CHAPTER 5: REPORTING DUTIES IN OTHER LEGISLATION

"The key to change is perhaps in recognising the way in which Bitcoin interacts with regulation."[1] Govender opines that Bitcoin specifically requires regulation to legitimise its use.[2] This is based on the SARB position paper of 2014 in which it was determined that cryptocurrencies are not regarded as legal tender.[3] This article by Govender seeks to address cryptocurrency from a financial law point of view. It is submitted that the interaction between different regulatory legislation and regulatory bodies might be a useful tool to aid in the identification of cryptocurrency for purposes of taxation.

Considering the approach of the United States of America, to combine the application of the Bank Secrecy Act with the Income Tax Act to create a reporting duty that the IRS can use to track cryptocurrency, it becomes clear that to attempt to regulate cryptocurrency, from a tax perspective, through a single Act is both unrealistic and short-sighted.[4] As previously stated the risk for governments associated with cryptocurrency is tax evasion and money laundering,[5] commonly referred to as financial terrorism.[6]

In the South African legal dispensation, financial terrorism is dealt with in terms of the Financial Intelligence Centre Act 38 of 2001 ("FICA"). The purpose of this piece of legislation is to address financial terrorism through a range of offences and reporting duties of transactions. In what follows FICA will be discussed as a basis for establishing a reporting duty for cryptocurrencies as a means to assist SARS in identifying cryptocurrencies.

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1 Govender S (2017) April BitCoin: Prettier in a shiny regulated wrapper? *Without Prejudice* pg. 24 at 24.
2 Govender (2017) at 24.
3 Governder (2017) at 24. See also SARB Position Paper 2014.
4 See Chapter 3 paragraph 3.2 and 3.3 on the inter-regulatory approach followed by the USA.
5 Plassaras (2013) pg 390. See Chapter 3 paragraph 3.1 for a discussion on the risks associated with cryptocurrencies.
6 Lagarde (2018).

5.1. FICA

The purpose of the FICA is to combat financial crimes such as money laundering and to impose certain duties and responsibilities on institutions which might be used for financial terrorism.[7]

The FICA creates the Financial Intelligence Centre ("Centre") which at its core acts as the regulating body to assist with the identification of unlawful activities and to combat financial terrorism.[8] The information gathered by the Centre is then distributed to SARS to aid in the enforcement of the law.[9]

Chapter 3 of the Act deals with the control measures for money laundering and financing of terrorist and related activities. There are various controls established by the FICA to achieve its purpose.

5.1.1 CONTROL 1 - IDENTIFICATION

The first control measure implemented by the FICA is that of identifying clients of institutions.[10] There is a duty on all accountable institutions to verify the identity of its clients prior to establishing a business relationship or to conclude a single transaction.[11] Section 20A of the FICA prohibits the conclusion of transactions in circumstances where the client or other party uses a fictitious name. Section 21 of the FICA creates an obligation on institutions to verify the identity of contracting parties.[12] The FICA goes further to state that when an institution cannot determine the identity of a contracting party no business relationship or transaction may be concluded, and the institution must consider reporting the circumstances to the Centre.[13]

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7 FICA preamble.
8 S 3(1) of FICA.
9 S 3(2)(a)(iv) and s 3(2)(b) of FICA.
10 S 20A and 21 of FICA.
11 S 20A of FICA.
12 S21(1) of FICA.
13 S 21E of FICA.

Considering the nature of cryptocurrencies and the fact that it is traded on an online platform anonymously, this type of reporting duty may aid to identify users of cryptocurrencies. Although the FICA only creates this obligation on institutions listed in its schedules, the principle of identifying contracting parties can be a useful tool.

This duty to identify users and crypto-transactions, currently only applies when the cryptocurrency user intends to receive the value of the currency his or her bank account. The bank will then have a duty to verify his or her identity but not his or her username on online platforms. It should be noted, that this does not necessarily create an obligation to verify the origin of the funds received.

Thus, this duty to identify the client in respect of cryptocurrencies must go further to require that his or her username on the online platforms also be disclosed. This will enable SARS to trace transactions on the online platforms. It is recognised that this inclusion might spark a debate regarding the right to privacy in terms of section 14 of the Constitution.[14] It is submitted, without entering into an evaluation of the right to privacy, that this limitation might be justified in terms of section 36 of the Constitution. The limitation of the right to privacy in terms of section 36 must be proportional and in relation to a legitimate government purpose of the legislature.[15] In this instance, the limitation will be linked to the purpose of preventing financial terrorism and tax evasion which is a legitimate government purpose.

5.1.2 CONTROL 2 - DUTY TO KEEP RECORD

The second control measure implemented by the FICA is the duty to keep a record of transactions.[16] Section 22 of FICA provides that the documents provided to identify the contracting parties,[17] the source of the funds and the purpose of the business

[14] S 14 of Constitution of RSA 1996.
[15] S 36(1)(c) and (d) of the Constitution of the Republic of South Africa 1996. See also *S v Makwanyane* 1995 (6) BCLR 665 (CC) par 104. See also *Harksen v Lane* (1998) 1 SA 300 (CC) at pg 324.
[16] S 22 of FICA.
[17] S 22(2)(a) of FICA.

relationship or transaction must be kept as due diligence.[18] Section 22A of FICA provides that the records must reflect the following:

a) The amount and the currency involved;[19]

b) Transaction date;[20]

c) The contracting parties;[21]

d) Nature of the transaction;[22] and

e) Business correspondence.[23]

Considering cryptocurrencies, the duty to keep the aforementioned records will be helpful to enable SARS to properly evaluate the transaction and to determine the tax consequences flowing therefrom. This duty must be extended to all persons and must require persons engaging in cryptocurrency to provide these records to the Centre, who in turn will provide it to SARS.

5.1.3 CONTROL 3 - DUTY TO REPORT UNUSUAL TRANSACTIONS

Section 29(1) creates an obligation when a person has a suspicion regarding unusual transactions which might be linked to unlawful activities to disclose the suspicion together with the grounds of the suspicion to the Centre.[24] The net of this provision is cast very wide to include any activity which might be linked to financial terrorism. This interpretation can be found by the use of terms such as activities “related” to financial terrorism.

This provision would include the use of cryptocurrencies as a means to commit crimes of money laundering or fraud. It is submitted that this general duty to report unusual transactions must be broadened to include the reporting of all transactions in which

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[18] S 22(2)(b) of FICA.
[19] S 22A(2)(a) of FICA.
[20] S 22A(2)(b) of FICA.
[21] S 22A(2)(c) of FICA.
[22] S 22A(2)(d) of FICA.
[23] S 22A(2)(e) of FICA.
[24] S 29(1) of FICA.

cryptocurrencies are involved irrespective of whether it is linked to an unlawful activity or not. This is in line with the approach followed by the United States of America's Fintech.[25] This all-encompassing reporting duty will require a sieving process for crimes of money laundering. The result, however, is that SARS would be able to track the transaction back to its records to determine whether the cryptocurrencies transactions were disclosed by the taxpayer and the tax thereon has been duly accounted for. [26]

5.1.4 CONTROL 4 - OFFENCES AND PENALTIES FOR FAILING TO COMPLY WITH FICA

This discussion does not intend to deal with each offence or conduct warranting an administrative penalty. The purpose of this discussion is to indicate and show how the Act attempts to enforce compliance.

The FICA uses a combination of administrative penalties and criminal offences to ensure enforcement of the Act.[27] The Act distinguishes between conduct that warrants an administrative penalty and conduct that justifies a criminal offence.

Conduct relating to non-compliance with the Act such as the failure to keep records will be subject to an administrative penalty.[28] In contrast, conduct relating to the intentional destruction of records or the failure to advise the Centre of suspicious transactions will be an offence.[29] The gist of the differentiation is whether there is an intention to undermine the Act. Thus, conduct which is not necessarily aimed at undermining the FICA will only be subject to an administrative penalty.

Due to the nature of cryptocurrencies and the fact that its use and possession is easily concealed, the penalty or offence for the non-reporting of transactions must be severe to create an incentive to rather disclose the transaction.

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[25] See chapter 3 paragraph 3.2 and 3.3.
[26] Cryptocurrency transactions refer to the trading in and mining of cryptocurrencies and related transactions such as the exchange of cryptocurrency for real currency.
[27] Chapter 4 of FICA.
[28] S 45C of FICA.
[29] S 48 to 71.

5.2. CONCLUSION

The FICA application is limited to certain types of persons or institutions and certain circumstances. Cryptocurrencies are not only traded by corporations but by individuals as well. This means that the reporting duty to be created must be general in nature and application.

The FICA as it currently reads falls short of creating a general duty on all persons to disclose transaction involving cryptocurrencies. This is based on the following:

a) Its application is limited to certain listed institutions;

b) The requirement of identification does not require the disclosure of online usernames;

c) The duty to keep record should be imposed on all contracting parties or persons engaging in a transaction involving cryptocurrencies; and

d) The duty to report unusual transactions must be extended to include the reporting of all transactions related to the use or acquisition of cryptocurrencies.

To conclude, the FICA is limited in its application of persons on whom the duties are imposed. As such, it is advised that the FICA be amended to include cryptocurrencies alternatively, a general reporting duty must be included in the IT Act or TAA coupled with penalties or offences to create an incentive to comply with the acts.

It is suggested that similar to the approach followed by the United States of America to combine the application of their Income Tax Act and Bank Secrecy Act to track and trace crypto-transactions for purposes of taxation, the South African legislature can combine the forces of FICA, the IT Act and the TAA.

CHAPTER 6: CONCLUSION

6.1 INTRODUCTION

The primary objective of this study was to determine the efficacy of the existing anti-avoidance provisions in the IT Act and the TAA.[1] This was done through a doctrinal approach to the interpretation of the provisions contained in the IT Act and TAA.[2]

The tax regulatory provisions in the United States of America and Canada were comparatively explored to determine the tax treatment of cryptocurrencies. The study also addressed the secondary objectives such as the application of the FICA as a means to regulate the use of cryptocurrencies.[3] The tender status of cryptocurrencies was examined to determine whether it should attract tax consequences.

6.2 THE NATURE AND FUNCTIONALITY OF CRYPTOCURRENCIES

Chapter Two set out to establish the nature and functionality of cryptocurrencies.[4] It was determined that cryptocurrency is a representation of value that is transferred using a technology called "blockchain" which allows its users to transfer value safely and anonymously.[5] The anonymity of cryptocurrencies prompts the primary research question of determining the efficacy of the anti-avoidance provisions and the reporting duty in respect of cryptocurrency.

It was established that cryptocurrencies do not enjoy legal tender status in Canada, China, Netherlands, South Africa, Russia or the United States of America. This is due

[1] See par 1.3.
[2] See par 1.5.
[3] See par 1.3.
[4] See par 2.1.
[5] See par 2.1.

to the volatilely in the fluctuations of the value of cryptocurrencies.[6] It was also established that illegal receipts of cryptocurrencies can attract a tax consequence.[7]

6.3 REGULATION AND IDENTIFICATION OF CRYPTOCURRENCIES IN THE UNITED STATES OF AMERICA AND CANADA

It was established that the United States of America treats cryptocurrency as property for purposes of tax.[8] The IRS uses a combination of the BSA, FinCEN regulations and the Income Tax Act to regulate cryptocurrencies.

The Canadian government, on the other hand, has completely legalised the use of cryptocurrencies and it is regulated through the application of the Canadian Income Tax and the Proceeds of Crime (Money Laundering) and Terrorist Financing Act.[9]

The conclusion reached in Chapter 3 is that due to nature of cryptocurrencies and the inherent dangers associated therewith a joint approach by specialised task forces such as the Transactions and Reports Analysis of Canada and FinCEN in the United States can be effectively used to track, trace and tax cryptocurrencies.[10]

6.4 THE EFFICACY OF THE EXISTING ANTI-AVOIDANCE PROVISIONS

It was established that the existing anti-avoidance provisions in the IT Act and TAA falls short in their application to cryptocurrencies.[11] There is also no general reporting duty related to cryptocurrencies. It was also established that the rules of interpretation of fiscal legislation will favour the taxpayer and in light of the difficulties highlighted in the application of the existing anti-avoidance provisions, the courts will have no

[6] See par 2.2.
[7] See par 2.3.
[8] See par 3.1.
[9] See par 3.2.
[10] See par 3.3.
[11] See par 4.3 and 4.4.

alternative than to rule that taxpayers are not evading tax through the use of cryptocurrencies.

The secondary objective in this chapter was to set out the difference in tax evasion and tax avoidance.[12] It was established that the main difference can be found in the intention with which the taxpayer arranges his or her affairs.[13]

The latest developments in the tax legislation to bring cryptocurrencies within the ambit of the IT Act and TAA were investigated. It was determined that the inclusions do not aid in the prevention of tax evasion.[14]

6.5 THE REPORTING DUTY IN OTHER LEGISLATION RELATING TO ONLINE TRANSACTION

The objective in Chapter 5 was to determine the applicability of the FICA to cryptocurrency as a means for SARS to track and trace cryptocurrency. It was established that FICA's limited application to crypto-transactions are problematic in creating a general reporting duty for cryptocurrencies. In the absence of proper regulation, the use of cryptocurrencies in acts of financial terrorism remains an imminent risk.

6.6 CONCLUSION

In conclusion, it is submitted that the existing anti-avoidance provisions are inadequate to ensure the proper taxation of cryptocurrencies. Therefore, a real risk of tax evasion and impermissible tax avoidance through the use and trade of cryptocurrencies exists.

Considering the research conducted it is concluded that to effectively regulate from a tax perspective is to implement a combination of the FICA and the anti-avoidance

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12 See par 4.2.
13 See par 4.2.
14 See par 4.5.

provisions. It is recommended that the IT Act, TAA and FICA be amended to include cryptocurrencies to create a reporting duty.

The IT Act and the TAA should be amended to cater for cryptocurrencies in the anti-avoidance provisions to create focussed provisions relating to cryptocurrencies addressing the problems with the identification and regulation thereof. FICA can also be amended to include a general reporting duty of cryptocurrencies by removal of the monetary threshold in respect of cryptocurrencies. Further, the application of FICA can be widened to all persons and not just the listed institutions.

Through the effective use of the blockchain and other modern technology the burden on the government to track and trace cryptocurrencies can be alleviated. This would necessitate specialised training of government officials to enable them to identify cryptocurrencies. This could be addressed by creating a task team in SARS and the Centre that specialise in the tracking and tracing of cryptocurrencies. This would in turn address tax evasion and financial terrorism risks.

The alternative is to consider drafting a new bill focussed on the tax treatment of cryptocurrencies. It would not be considered strange to draft a specialised bill in the tax dispensation. It is common for the legislature to enact specialised legislative pieces such as the Value-Added Tax Act 89 of 1991 or the Customs and Excises Act 91 of 1964 that deals with specialised fields of tax. In the same manner, the risks, identification, regulation and accounting for cryptocurrencies can be addressed.[15]

To conclude, cryptocurrencies are not impossible to regulate and tax. The remedy for the current unregulated stance is for the legislature to actively seek out methods in which the risks can be alleviated.

[15] The proposal of a new bill and the provisions thereof falls outside the scope of this dissertation.

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