Certificate in Digital Economy Tax

Tax Implications of Cryptocurrency

Airdrop: An airdrop is the distribution of free cryptocurrency tokens or coins to a large number of wallet addresses. Airdrops are often used as a marketing strategy by new cryptocurrency projects to gain visibility and users. From a tax perspective, airdropped cryptocurrency is generally considered taxable income at the time it is received, and is subject to capital gains tax when it is sold or exchanged.

Capital Gains Tax: Capital gains tax is a tax on the profit realized from the sale or exchange of a capital asset, such as cryptocurrency. The tax rate for capital gains in the UK is either 10% or 20%, depending on the individual's income tax bracket. In the US, the capital gains tax rate can be as high as 20% for long-term capital gains and 37% for short-term capital gains. It is important to keep accurate records of all cryptocurrency transactions to determine the cost basis and holding period for each asset, as this information is needed to calculate the capital gain or loss.

Cryptocurrency: Cryptocurrency is a digital or virtual currency that uses cryptography for security and operates independently of a central bank. The most well-known cryptocurrency is Bitcoin, but there are thousands of other cryptocurrencies in existence. Cryptocurrencies can be used for a variety of purposes, including buying and selling goods and services, transferring funds, and investing. From a tax perspective, cryptocurrency is treated as property in many countries, including the UK and US, and is subject to capital gains tax when it is sold or exchanged.

Decentralized Finance (DeFi): Decentralized finance, or DeFi, refers to the use of blockchain technology to create decentralized financial systems and applications. DeFi platforms allow users to lend, borrow, and trade cryptocurrency without the need for intermediaries such as banks. From a tax perspective, DeFi transactions are generally treated in the same way as other cryptocurrency transactions and are subject to capital gains tax.

Fiat Currency: Fiat currency is government-issued currency that is not backed by a physical commodity, such as gold or silver. Examples of fiat currency include the US dollar, the British pound, and the Euro. Cryptocurrency can be exchanged for fiat currency on various online platforms, and the value of cryptocurrency is often quoted in terms of fiat currency. From a tax perspective, the exchange of cryptocurrency for fiat currency is a taxable event and is subject to capital gains tax.

Fork: A fork is a change to the underlying code of a cryptocurrency that creates a new version of the currency. Forks can be either "hard" or "soft." A hard fork creates a completely new cryptocurrency, while a soft fork is a backwards-compatible update to the existing currency. From a tax perspective, a fork can be treated as a taxable event, as it may result in the receipt of new cryptocurrency.

Hodl: Hodl is a term used in the cryptocurrency community to refer to the practice of buying and holding cryptocurrency for the long term, rather than trying to profit from short-term price fluctuations. From a tax perspective, hodling can be a tax-efficient strategy, as it allows the individual to defer paying capital gains tax until the cryptocurrency is sold.

Initial Coin Offering (ICO): An initial coin offering, or ICO, is a fundraising event in which a new cryptocurrency project sells tokens or coins to investors. ICOs are similar to initial public offerings (IPOs) in the traditional financial market. From a tax perspective, ICOs can be complex, as they may involve the receipt of multiple types of cryptocurrency and may be subject to various tax rules and regulations.

Mining: Mining is the process of using powerful computers to solve complex mathematical problems in order to validate transactions on a blockchain and earn cryptocurrency as a reward. From a tax perspective, mining

can be treated as self-employment income and may be subject to income tax and self-employment tax.

Smart Contract: A smart contract is a self-executing contract with the terms of the agreement between buyer and seller being directly written into lines of code. Smart contracts are stored on a blockchain and can be used to facilitate, verify, and enforce the negotiation or performance of a contract. From a tax perspective, smart contract transactions are generally treated in the same way as other cryptocurrency transactions and are subject to capital gains tax.

Stablecoin: A stablecoin is a type of cryptocurrency that is pegged to the value of a stable asset, such as a fiat currency or a commodity. Stablecoins are designed to reduce the volatility that is often associated with cryptocurrency. From a tax perspective, stablecoins are generally treated in the same way as other cryptocurrencies and are subject to capital gains tax when they are sold or exchanged.

Taxable Event: A taxable event is a transaction or event that triggers a tax liability. In the context of cryptocurrency, taxable events include the sale or exchange of cryptocurrency, the receipt of cryptocurrency as income, and the use of cryptocurrency to purchase goods or services. It is important to keep accurate records of all taxable events in order to calculate the tax liability and file accurate tax returns.

Transfer: A transfer is the movement of cryptocurrency from one wallet to another. Transfers are generally not considered taxable events, as long as they are made between the individual's own wallets and no other transactions are taking place. However, it is still important to keep accurate records of all transfers for accounting and tax purposes.

Wallet: A wallet is a digital or virtual storage location for cryptocurrency. Wallets can be either "hot" or "cold." A hot wallet is connected to the internet and can be used for everyday transactions, while a cold wallet is not connected to the internet and is used for long-term storage. From a tax perspective, it is important to keep accurate records of all transactions taking place in each wallet in order to calculate the cost basis and holding period for each asset.

Wrapped Token: A wrapped token is a type of cryptocurrency that is wrapped, or bundled, with another cryptocurrency in order to facilitate the use of the wrapped token on a different blockchain. For example, a wrapped Bitcoin (WBTC) is a wrapped version of Bitcoin that can be used on the Ethereum blockchain. From a tax perspective, wrapped tokens are generally treated in the same way as other cryptocurrencies and are subject to capital gains tax when they are sold or exchanged.