



Date 31.07.2019

DLT ASSETS AND ASSOCIATED TAX IMPLICATIONS **webinar – Malta the Blockchain Island**

Mr Chris Borg
Dr Malvina Mulliri
CSA Group

ABOUT US



CSA Group has grown from a family oriented accounting practice into one of the leading financial services providers here in Malta.

With over twenty five years of expertise in the financial services industry, CSA Group operates from Malta providing tailor made solutions for clients across the globe. Our portfolio of clients include high net worth individuals, companies, businessmen, firms and international players. Different companies have been set up to ensure a truly one stop shop solution is provided to our clients.



Bastille Malta
Trustees



Legal framework on DLT & DLT Assets

Dr Malvina Mulliri

WHY MALTA



➤ **A holistic legal framework**

A number of jurisdictions have worked, during the last few years, to regulate the DLT related businesses. However, even the most active jurisdictions, have been mainly focused on blockchain based cryptocurrencies and initial coin offering without embracing the sector in its entire extent.

➤ **Well established financial sector**

Malta is an internationally recognised financial services hub. The sector's integrity and stability are critical contributing factors to the impeccable reputation of Malta in the global scenario and are expected to fuel further growth in DLT ecosystem.

➤ **World-class information and communications technology infrastructure**

It has always been considered strategically important to the country's human and economic advancement to be well connected with the rest of the world. As such, there has been a great deal of investment and consolidation in order to create and ensure a reliable Information Communication Technology (ICT) infrastructure.

➤ **Efficient tax regime**

Malta is the only EU member state with full imputation system. A long-standing, full imputation tax system has existed in Malta since 1948 and has gained approval by EU when Malta acquired the status of a member state. The rate for corporate taxation in Malta stands currently at 35%, however, upon the distribution of dividends, shareholders receive credit for any tax paid by the company and may qualify for a refund generally equivalent to 6/7ths of the relevant tax paid in respect of trading income and 5/7ths of the relevant tax paid in the case of passive interest and royalties, thus resulting in most of the times in a combined net effective tax rate of just 5%.

WHY MALTA



➤ **Innovation friendly authorities**

Malta the Blockchain Island has made a brilliant strategic move by positioning itself as a refuge for Blockchain companies to pursue to their ambitions in an environment where they feel safe and free to do so. The regulating authorities in Malta offer a firm but yet flexible frame of mind. While no standard is compromised, ideas and project are openly discussed with the regulator, whilst new stakeholders and innovative proposals are always welcomed to the Maltese shores.

➤ **Biggest name in the industry**

Hard work pays off, and as a result Malta has managed to attract the attention of the largest Blockchain and innovative technologies players in the industry. Binance, OKEx, ZB.Com, Neufund, Bitbay, Waves, just to mention a few have all publically stated their relocation to Malta. Thus generating thousands of new jobs on The Island.

➤ **Possibility to certificate DLT platforms**

A framework and an ad hoc authority, that is the first of its kind in the world, is set up in Malta to ensure that the innovative technology arrangements are suitably designed and are operating effectively. The authority, relaying in the tests performed and reports drafted by registered auditors, will grant recognition only to those platforms, or parts thereof, that meet the high standards set in relation to security, processing integrity, availability of information, confidentiality and protection of data.

➤ **Malta's future banking system**

It is always promising to hear the likes of Revolut and other banks offering new solutions in Malta. Founders Bank will be the newest addition to the rapidly growing, full-value Blockchain ecosystem on Blockchain Island. Once licensed, this bank will offer the first step towards an offering through the blockchain-based equity fundraising platform Neufund and issuing its own legally-binding equity tokens. Binance, the world's largest crypto exchange, is one of the first and major investors in the company.

BLOCKCHAIN NATIONAL STRATEGY



Malta – The Blockchain Island

Public services in Blockchain

Formation and Innovation

Smart Governance

Virtual Residence

Blockchain Authority

Regulation of cryptocurrencies

LEGAL FRAMEWORK



1st November 2018

- ***MALTA DIGITAL INNOVATION AUTHORITY ACT (MDIA ACT)***
- ***INNOVATIVE TECHNOLOGY ARRANGEMENTS AND SERVICES ACT (ITAS ACT)***
- ***VIRTUAL FINANCIAL ASSETS ACT (VFA ACT)***

MALTA DIGITAL INNOVATION AUTHORITY ACT



- *Establishes Malta Digital Innovation Authority*
- *Certification of ITA and ITS*



MDIA
Malta Digital Innovation Authority

INNOVATIVE TECHNOLOGY ARRANGEMENTS AND SERVICES ACT



Definition of ITA and ITS

DLT Platforms

Smart Contracts

Systems Auditors

Technical Administrator

Resident Agent

VIRTUAL FINANCIAL ASSETS ACT



- *Definition of DLT Assets and Virtual Financial Assets*
- *Initial VFA Offering*
- *VFA Service Providers*
- *VFA Agents*

VIRTUAL FINANCIAL ASSETS ACT



➤ Definition of DLT Assets and Virtual Financial Assets

Under Article 2 Distributed Ledger Technology (“DLT”) is defined as “a database system in which information is recorded, consensually shared, and synchronised across a network of multiple nodes”.

When the above mentioned technology is utilised in the financial sector, the digital assets that are executed on a DLT platform, are classified, for the purpose of Maltese law as:

- *electronic money;*
- *a financial instrument;*
- *virtual token;*
- *virtual financial asset;*

E-money and financial instruments are well known concepts and already defined by legislation in force in accordance with the Financial Institutions Act and Investment Services Act. While the concept of virtual token and virtual financial asset have been introduced by the newly enacted VFA Act.

*The latter defines VFA by way of exclusion as a “form of digital medium recordation that is used as a digital medium of exchange, unit of account, or store of value and that is **not** - (a) electronic money; (b) a financial instrument; or (c) a virtual token”.*

MFSA has issued a particular test procedure to be followed in order to deduce the nature of the asset and in turn, trigger the application of the respective legal regime

VIRTUAL FINANCIAL ASSETS ACT



➤ Initial VFA Offering

No issuer shall offer a virtual financial asset to the public in or from within Malta or shall apply for a virtual financial asset's admission to trading on a DLT exchange unless such issuer draws up a whitepaper which complies with the law requirements and is registered with the Authority.

The Issuer wishing to issue VFA shall make sure to meet a number of requirements and as such shall:

- Appoint a VFA Agent registered with MFSA and shall make all communications, meetings, notifications and/or submissions to the authority through his VFA Agent;*
- Prove to meet the fitness and properness requirements during issuing stage as well as on an ongoing basis;*
- Perform the Financial Instrument Test the purpose of which is to determine whether a DLT asset shall qualify as VFA and as such be subject to the VFAA regime*

VIRTUAL FINANCIAL ASSETS ACT



➤ VFA Service Providers

When provided in relation to a DLT asset qualified as VFA, can be undertaken in Malta or from within Malta, only if a licence is granted to the interested service provider by MFSA.

The services that acquire relevance under the VFA Act and are subject to licensing are as follows:

- 1. Reception and Transmission of Orders;*
- 2. Execution of orders on behalf of other persons;*
- 3. Dealing on own account;*
- 4. Portfolio management;*
- 5. Custodian or Nominee Services;*
- 6. Investment Advice;*
- 7. Placing of virtual financial assets;*
- 8. The operation of a VFA exchange.*

Exemptions are set forth determined persons for the purpose of the requirement for a license, mainly due to the nature of the service provider or of the service offered.

VIRTUAL FINANCIAL ASSETS ACT



➤ VFA Agent

VFA Agent shall guide the Issuer on the requirements, information and disclosures which are required to be included in the White Paper before such are submitted to the MFSA for approval.

VFA Agent shall ensure that the Service Provider has a robust and significant business plan and shall also guide on the requirements, information and disclosures which are required to be included in the license application submitted to the MFSA.

VFA Agent performs the Financial Instruments Test to determine the nature and classification of the DLT Asset.



Taxation on DLT Assets

Chris Borg

TAXATION ON DLT ASSETS

*In accordance with the CFR guidelines published 1st November of last year, **DLT assets** are **defined** as:*

- **1. Coins** - DLT assets designed to be used as a **means of payment** or **medium of exchange**, or function as a **store of value without the characteristics of a security** eg. Bitcoin.
- **2. Financial Tokens** - DLT assets **exhibiting qualities** that are similar to **equities, debentures** units in CIS or derivatives including Financial Instruments.
- **3. Utility tokens** - DLT assets whose **utility, value** or **application** is **restricted solely to the acquisition of goods or services** either solely within the DLT platform.
- **4. Hybrids** – Coins + tokens

INCOME TAX TREATMENT OF DLT ASSETS



- *The **value of the DLT assets** must be determined by using the market value composed by using the **rate established by the Maltese authority**, or, the **average price on reputable exchanges**.*
- *The value expressed in a cryptocurrency will need to be **presented in the reporting currency** in which DLT assets providers present their **financial statements**.*
- ***Payments made or received in a cryptocurrency** should be treated in the **same manner as payments in any other currency for income tax purposes**. When a payment is made or received in a **financial** or a **utility token**, it should be treated like any other **payment in kind**.*

INCOME TAX TREATMENT OF DLT ASSETS



➤ *Transactions involving coins:*

***Transactions** involving **coins** are to be treated for tax purposes in the **same way** as the transactions **involving fiat currency**.*

***Proceeds** from the **disposal of coins** held for **trading purposes** will be deemed to be a **trading income**, the same treatment applies to gains or profits from **mining of cryptocurrency**.*

*However, **capital gains** derived from the disposal of coins held as a long term investment will **fall outside the scope** of income tax.*

INCOME TAX TREATMENT OF DLT ASSETS



➤ Return on financial tokens

*Income derived by investors by way of **dividends, interest, premiums** etc., in a **cryptocurrency** or in **another currency, or in kind**, will be treated as **ordinary income** in terms of the provisions of Article 4 of the ITA.*

INCOME TAX TREATMENT OF DLT ASSETS



➤ Transfers of financial and utility tokens

- The tax treatment of **proceeds from the disposal** of a **financial** or **utility token** will depend on whether it is a transaction of a **trading** or a **capital nature**. Profits from the disposal of tokens, acquired with **the intention of resale at a profit**, will be treated as **trading profits**. However, in order to distinguish whether a transaction is of a trading or capital nature it might be necessary to use the **badges of trade tests**.
- If the transfer of **financial tokens** is **not** considered as a **trading transaction**, one must distinguish whether the tokens meet the definition of “**securities**” and whether they participate in any way in the profits of the company. If the financial tokens qualify as “**securities**” **they will subject to tax as prescribed by the ITA**.
- On the other hand, the transfer of **tokens** that do **not** fall within the definition of “**securities**”, such as transfers of **utility tokens**, will **fall outside the scope of the tax on capital gains**.

INCOME TAX TREATMENT OF DLT ASSETS



➤ Treatment of Initial Offerings

*An initial coin offering is a **crowdfunding mechanism** to raise funds for the development of future products and services which will be offered at a later stage by the issuing company. The **proceeds of an ICO** will **not** be treated as **income** and the **issue of new tokens** will **not** be treated as a **transfer** for the purposes of **taxation of capital gains**.*

*Any **future use** of the **issued utility tokens** to serve as a **payment** and **access to products and services** developed and offered by the company will be deemed to represent **gains or profits subject to tax in terms** of the ITA.*

VAT TREATMENT OF DLT ASSETS



*The general approach to VAT treatment of **DLT assets** follows the rules and principles applicable in terms of the VAT Act, Chapter **406 of the Laws of Malta**, the **EU Directive** (2006/112/EC) and the relevant regulations, as well as any relevant **case law of the CJEU**.*

*The first step to be taken in order to determine whether a transaction involving DLT assets falls within the scope of Maltese VAT, is to **determine the place of supply** of the goods and services. **If the place of supply is not Malta the rules of the other country will apply.***

VAT TREATMENT OF DLT ASSETS



When a transaction is in the scope of VAT?

- *supply of a good/services*
- *for a consideration*
- *within the territory of a Member State*
- *Carried out by a taxable person acting as such*

VAT TREATMENT OF DLT ASSETS



*Where transactions involving DLT assets are considered to be supplies of **electronically supplied services**, the **place of supply of services** provided to **non-taxable individuals** established in other MS is considered to be the place **where the customer is established** and where the reverse charge mechanism is **not** applicable.*

*In such cases the supplier **may opt to register** and account for VAT under the **MOSS System** in terms of Part Eight of the 14th Schedule to the VAT Act.*

VAT TREATMENT OF DLT ASSETS



➤ Coins

- Coins which are used as a **means of payment** must be treated like **traditional currency** for **VAT purposes** in terms of **Hedqvist case**.
- Accordingly, the exemptions provided for transactions in currency will apply to “**transactions, including negotiation**” in cryptocurrencies where these serve as a means of payment. The exchange of cryptocurrencies for other cryptocurrencies or for fiat money will be covered by the **said exemptions**.

VAT TREATMENT OF DLT ASSETS



➤ Digital Wallets

- *The payment of fees required by digital wallet providers for allowing users to **hold and operate** a cryptocurrency will be **exempt without credit** according to item 3(4), Part Two, 5th Schedule to the VAT Act.*
- *However, services which do **not constitute transactions concerning currency** and which **cannot be regarded as transactions concerning payments** or transfers, or transactions in securities, will be **subject to VAT** accordingly.*

VAT TREATMENT OF DLT ASSETS



➤ Mining

- For VAT purposes a **chargeable event** arises where a **supply of services** is made for a **consideration** by a **taxable person** acting as such. Supplies of services can be subject to VAT, only if a direct link exists between the services supplied and the consideration received by the taxable person, and where, there is a reciprocal performance between the supplier and the recipient of the services.
- **Mining** normally does **not** have a **particular recipient** and therefore **falls outside the scope of VAT**.
- However, should **miners** receive **payment for other services**, such services **will be considered as taxable for VAT purposes**. If the services are deemed to take place in Malta Maltese standard VAT will apply.

VAT TREATMENT OF DLT ASSETS



➤ Exchange platforms

- The provision of a **trading/exchange facility in consideration** for the **payment** of a **transaction fee** or **commission** will be deemed to be a **supply of services for VAT purposes**.
- The VAT treatment will depend on the nature of the service supplied:
 - a. The provision of an **electronic facility allowing to trade/exchange**, will be deemed to be a **technological services subject to VAT**.
 - b. However, if the DLT Assets traded classify as “**currency**” or “**securities**” for VAT purposes and where the platform’s services go beyond the mere provision of a trading facility, such services may **fall within the exemption** applicable to transactions concerning currency, transactions in securities and intermediation/negotiation in connection with transactions in currency and securities.

VAT TREATMENT OF DLT ASSETS



➤ Tokens:

Financial tokens

- *Financial tokens grant the rights to dividends, interest payments or other rights. If a financial token is **issued to raise capital**, the issue will **not be subject to VAT**, because the raising of finance does **not constitute a taxable supply** of services and **falls outside scope** of Maltese VAT.*
- *Services supplied by exchange platforms to buyers and sellers will have the same treatment applicable to coins.*

VAT TREATMENT OF DLT ASSETS



➤ Tokens:

Utility tokens

- Token issued **against a payment** which **carries an obligation** to be accepted as a **payment for goods or services**, and the goods or services to be supplied or the **identity of the supplier is known**, will have the **characteristics of a voucher** and will be treated for VAT purposes accordingly.

VAT TREATMENT OF DLT ASSETS



➤ Tokens:

Utility tokens

Single-purpose Voucher (SPV)

- In the case of a **single-purpose voucher** the **place of supply** and the **VAT due are known** at the time of the **voucher's issue**. As such the payment for the voucher will be deemed to be a payment for the good or service and will be **immediately subject to Maltese VAT**.

Multi-purpose Voucher (MPV)

- In the case of a **multi-purpose voucher** the **place of supply** and the **VAT due** for the **good or service** to be purchased is **not known** at the time of the issue of the voucher, and therefore the VAT will be due at the time of the **voucher's redemption**.

VAT TREATMENT OF DLT ASSETS



➤ Treatment of ICO

- Since during the ICO **no specific good or service** is identified, nor a corresponding **price** for a supply could be fixed, nor is it possible to determine whether the project will be realised and the investors will **receive a return**, such transactions will be **outside the scope of VAT**.
- There will be **no transaction subject to VAT** if the **money invested** will serve **to acquire a security in the issuing company**.
- However, any **future use** of the issued tokens to serve as a **payment and access to products and services developed** and offered by the issuer **will then be subject to VAT**

ANY QUESTIONS?



THANK YOU

chris.borg@csagroup.mt
malvina@csagroup.mt

**CSA Group
The Penthouse,
Carolina Court,
Giuseppe Cali' Street,
Ta' Xbiex, XBX1425,
Malta**

email: info@csagroup.mt
phone: [+356 21374747](tel:+35621374747)