Digital Tokens in Singapore

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The Rise of Digital Tokens and the Digital Economy

Since the inception of cryptocurrencies, the number of businesses all around the world using such alternative currencies has been inexorably on the rise. In addition, the escalating shift towards a digital global economy fuelled by the recent global pandemic has called for an imminent change in traditional tax principles.

Singapore has always taken a cautious approach towards the ever-changing global business landscape and for a start, the Inland Revenue Authority of Singapore ("IRAS") had released an E-Tax Guide on 17 April 2020 on the income tax treatment of digital tokens.

The IRAS' E-Tax Guide seeks to provide a certain level of clarity on the treatment of digital tokens and their tax implications. As expected, there is no deviation from traditional approaches and the fundamental tax principles are still largely preserved.

This Alert summarises the guidance provided in the IRAS' E-Tax Guide and highlights some food for thoughts.

What are Digital Tokens?

Digital Tokens are perceived as intangible assets that are representations of value that can be transferred, stored or traded electronically. The IRAS classify digital tokens into 3 types:

- Payment Tokens
  - Used by token holders as means of payment.
  - Akin to a fiat currency.
- Utility Tokens
  - Represents token holders' rights to consume specific goods or services after pre-payment.
  - Akin to a pre-payment arrangement.
- Securities Token
  - Grants token holders rights and obligations to certain degree of control or economic entitlement.
  - Akin to a debt or equity security.

Taxation / Deduction of Tokens

Receipt or payment of Payment Tokens for goods and services rendered or consumed by businesses

Taxable or deductible like normal fiat currency transactions, subject to the fundamental taxation or deduction rules in the Singapore Income Tax Act ("SITA").

HOW CAN BDO HELP?

At BDO, we have the expertise in providing comprehensive corporate tax advisory services. We also have experience in rendering tax opinions for digital token businesses in Singapore. Please feel free to contact us and let us know how we can serve you.

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- Source of Income
  - Where the businesses / key activities are carried out.
- Point of Taxation / Deduction
  - Receipt of payment tokens for goods and services rendered are taxable at the point when the rights to the payment tokens are earned / obligations to provide the goods and services are fulfilled.
  - Payment of payment tokens for goods and services consumed are deductible when the obligations to pay for the goods and services arise.
  - The above are subject to the fundamental taxation / deduction rules in the SITA.
- Value to Tax / Deduct
  - Open market value of underlying goods and services provided / consumed.

Acquisition of Utility Tokens

Treated like a prepayment for goods or services to be provided for in the future, subject to the fundamental deduction rules in the SITA.

- Point of Deduction
  - At the point of fulfilment of promised good and services.
- Value to Deduct
  - Acquisition value of the tokens.

Yield of Security Tokens

Depending on the rights and obligations associated with the tokens, they may be accounted for as a debt or equity.

- Point of Taxation
  - The fundamental taxation rules in the SITA apply on the interest or dividends.
- Value to Tax
  - Amount of interest or dividend earned.

Holding and disposal of Payment Tokens / Utility Tokens / Security Tokens

Taxability depends on the nature of the tokens i.e. fundamental tax principles of Revenue VS Capital.

- Source of Income
  - Where the trading of the tokens are carried out.
- Point of Taxation
  - Only at point of realisation.
  - Unrealised fair value gains are not taxable, even if the tokens are revenue in nature.
- Value to Tax
  - Open market value of the tokens.

What is an Initial Coin Offering ("ICO")?

An ICO is the issuance of new digital tokens in exchange for other Payment Tokens or fiat currency, to raise funds or to avail access to an existing or future supply of goods or service.

- Payment Token
  - Proceeds may be taxable at the point of issuance depending on facts and circumstances.

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- Utility Token
  - Proceeds are treated as deferred revenue i.e. taxable when obligations are fulfilled.
- Securities Token
  - Akin to issuance of debt or equity and hence, capital in nature i.e. not taxable. Where dividends / interests are paid, deductibility is subject to the fundamental deduction rules in the SITA.

Other ICO tax implications

- Source of Income

  The factors below (non-exhaustive) would determine the source of income:
  - Physical presence of the issuer
  - Location of marketing done by the issuer
  - Location of ICO participants
  - Location of the blockchain technology's developers
- ICO Failure
  - If ICO proceeds are refunded to investors, the proceeds will not be taxable.
  - If ICO proceeds are not refunded to investors, the taxability depends on whether the ICO is a capital or revenue transaction.
- Pre-commencement expenses
  - Where the ICO is conducted prior to the commencement of business, the normal deduction rules in the SITA relating to pre-commencement expenses will apply.
- Founder's Token

  ICO tokens awarded to the Founder will be regarded as:
  - Revenue in nature if it has a nexus to the services performed by the Founder; and
  - Capital in nature if it corresponds to the Founder's capital contribution to the Company and / or ICO.

  Where the Founder's Tokens are revenue in nature:
  - Point of taxation: When the founder is entitled to the tokens i.e. entitlement arises after a lock-in period or moratorium.
  - Value to tax: Value of tokens at the point of entitlement.

Final Words

With the issuance of the E-Tax Guide by the IRAS, it is a signal that Singapore acknowledges the potential growth of digital tokens and the commercial applications that follow and has attempted to clarify on the application of fundamental tax rules to Digital Tokens.

While the E-Tax Guide has indeed provided some clarity and certainty to the income tax treatment associated with digital tokens, there still exists room for ambiguity and vagueness (e.g. in the token valuation methodology, source of income, etc.). As the industry is still in its adolescence stage and traditional tax approaches may soon be out-dated, certain pertinent issues should be urgently addressed. Sourcing rules, especially, are critical and should be looked at using a multilateral approach to tackle the issues arising from the digitalisation of economy.

Nonetheless, with the Organisation for Economic Co-operation and Development ("OCED") actively implementing frameworks and Singapore's willingness to participate, we could potentially observe a shift in the fundamental principles that drive our tax legislation.

Over time, we should be expecting more specific guidelines and refinement of existing legislations by the IRAS to ensure consistency and equitability in the tax treatments as we transit inevitably into a globalised digital economy.

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