

Monday, June 17, 2019

Tax Policy Branch  
Department of Finance Canada  
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Ottawa, Ontario  
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**By email:** [fin.gsthst2019-tpstvh2019.fin@canada.ca](mailto:fin.gsthst2019-tpstvh2019.fin@canada.ca)

**Re: Department of Finance Canada Legislative Proposals Released May 17, 2019 to treat virtual currency as a financial instrument for GST/HST purposes**

Dear Madams and Sirs:

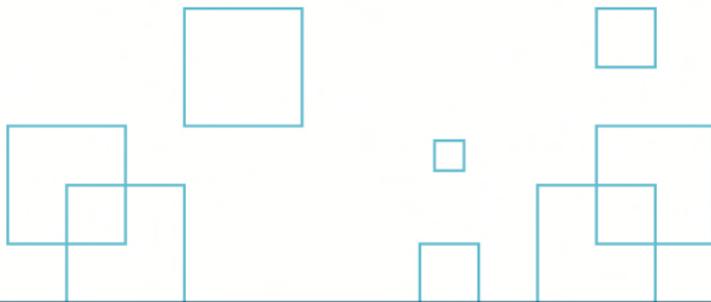
We thank the Department of Finance (the “**Department**”) for inviting Canadian stakeholders to participate in this important consultation. This submission sets out comments of the Chamber of Digital Commerce Canada (the “**Chamber**”) on the Goods and Services Tax/Harmonized Sales Tax (“**GST/HST**”) proposals (the “**Proposals**”) released May 17, 2019 to amend the *Excise Tax Act* (Canada) (the “**ETA**”) to treat virtual currency as a financial instrument for GST/HST purposes.

The transformative potential of digital assets, blockchain, and distributed ledger technologies (“**DLT**”) presents tremendous cross-sectoral and economic advancement opportunities that have been recognized globally by government and industry alike. Fundamentally, the technology reshapes the ownership of assets, how we interact with each other digitally, and how we transfer value. As a result, the ways in which companies in all sectors conduct business - from financial services, digital identity and privacy, healthcare, insurance, intellectual property, real estate, commerce, and supply chain management, among others - are being rapidly transformed and establishing a new Internet infrastructure dedicated to the digital exchange of value.<sup>1</sup>

The Chamber provides dedicated support for Canada’s emerging and rapidly growing blockchain ecosystem. Today, the Chamber represents some of the most significant companies operating in the blockchain and digital asset industry in Canada.<sup>2</sup> Our mission is to promote the acceptance and use of digital assets and blockchain-based technologies in Canada, while working to ensure that Canadian-based companies remain competitive in the global digital economy. Through education, advocacy, and working closely with policy makers, regulatory agencies, and industry, we are helping develop an environment that fosters innovation, jobs, and investment. As such, the Chamber has a significant interest in the Proposals as they directly impact a number of our members.

<sup>1</sup> Deloitte, The Internet of Value-Exchange: <https://www2.deloitte.com/content/dam/Deloitte/uk/Documents/Innovation/deloitte-uk-internet-of-value-exchange.pdf>.

<sup>2</sup> See Chamber of Digital Commerce, Membership: <https://digitalchamber.org/membership/>.



The Chamber is pleased to see the efforts of the Department to clarify the tax treatment of virtual currency. With the goal of offering constructive and practical feedback, we respectfully submit the following comments for your consideration.

### **1. Establish an Industry Expert Task Force**

Virtual currency and digital assets are under review in relation to current tax legislation and the tax treatment of virtual currencies has been partially addressed in the existing administrative guidance issued by the Canada Revenue Agency (the “CRA”).<sup>3</sup> While aspects of the digital asset landscape might fit under the ETA, the *Income Tax Act* (Canada), and CRA’s current administrative guidance, a broader systemic shift in technological advancement is occurring, such that any effort to categorize and define digital assets and virtual currency for tax purposes is an exercise that demands holistic study and review with industry experts at the table. To ensure Canada takes a strong national and global position regarding definitional classifications and treatment of digital assets, the Chamber strongly encourages the Department to establish an expert-led industry task force to facilitate collaborative dialogue and to position Canada to serve the best interests of Canadian digital asset and virtual currency stakeholders, who stand to benefit from participation in this rapidly growing global market.

### **2. Ensure National and Global Definitional Clarity and Consistency**

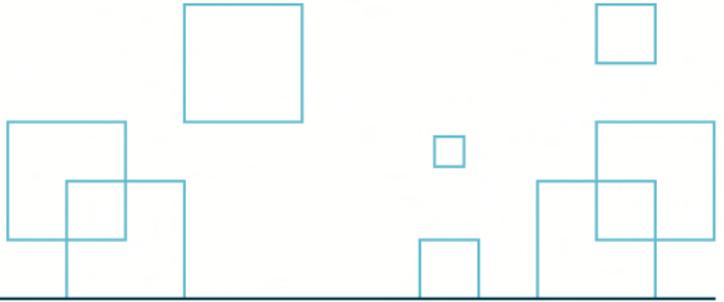
As we have seen for many years, the way in which we characterize digital assets and the activities that utilize these assets has a significant impact for industry growth and the achievement of economic and innovation policy objectives. Unintended consequences can result from vague definitions that fall short, or over-reach, policy goals, resulting in interpretive or practical challenges later for the government, industry, and Canadians. These types of consequences chill and harm the prosperity of industry (by creating confusion or unintentional administrative obstacles) and unintentionally stifle innovation and drive business out of Canada. As Canada seeks to compete in the global digital economy, we ask that policy makers take notice of the unintended consequences impacting our national potential for prosperity, technological innovation, and confident participation in the future forward economy.

While the intention behind the Proposals is welcome as it addresses an area of significant uncertainty for both our members and the general public, the Proposals appear to be ad-hoc measures at a time when comprehensive reform is necessary to ensure that existing tax concepts in both the ETA and the *Income Tax Act* (Canada) do not create tax impediments and uncertainties that impede the growth, innovation, and use of blockchain technology in Canada.

Blockchain technology is not a single wave of innovation that merely introduces a new contractual or financial product or service. Rather, it is a fundamental technological advancement that will impact

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<sup>3</sup> Canada Revenue Agency, *Guide for Cryptocurrency Users and Tax Professionals* (March 8, 2019): <https://www.canada.ca/en/revenue-agency/programs/about-canada-revenue-agency-cra/compliance/digital-currency/cryptocurrency-guide.html>.



all industries and the way we exchange with others digitally going forward. In our view, it is insufficient for the Department to graft a “virtual payment instrument” onto the definition of “financial Instrument” because such expression does not adequately reflect, in the sales tax scheme or otherwise, the variety of uses and characteristics virtual currency may have.

The Chamber asks that the Department ensure it has reviewed other legislative and regulatory initiatives currently underway globally and in Canada regarding virtual currency, virtual payment instruments, and other digital assets. A depth and breadth of understanding, coupled with holistic policy application, is essential to ensure that definitional clarity and consistency, along with harmonization nationally and globally, is prioritized and used to position Canada competitively in the global economy.

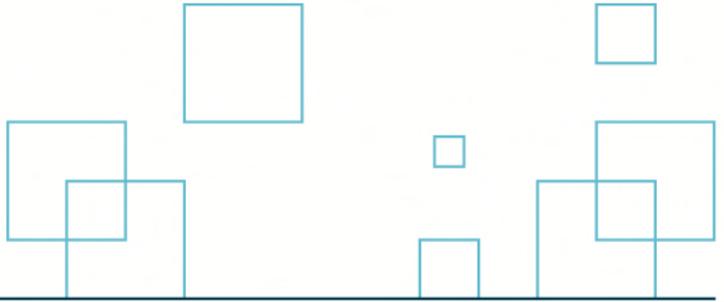
***The Definition of “Virtual Payment Instrument” Is Unduly Narrow and Appears to Arbitrarily or Unintentionally Exclude Certain Virtual Currency and Tokens***

One of the principal benefits of blockchain technology is its capability to facilitate an exchange for value between a purchaser and a vendor without the complexity of involving a third-party intermediary (such as a bank or payment processor) to identify and evaluate the parties and process the exchange of value. For these reasons, blockchain technology is known to drive efficiency and lower transaction costs.

CRA currently treats “virtual currencies” as commodities for purposes of the *Income Tax Act* (Canada).<sup>4</sup> Absent adoption of the Proposals, if this view were to extend to the treatment of virtual currency as a form of “property” for ETA purposes, it would result in a significant tax compliance and reporting burden on users of virtual currency as the ETA generally requires GST/HST registrants who make taxable supplies (other than zero-rated supplies) to charge, collect, and remit GST/HST on the supply. Under current law, subsection 123(1) of the ETA provides that, subject to sections 133 and 134, a “supply” requires the provision of “property” or a “service” in any manner. Both the definition of “service” and the definition of “property”, for purposes of the ETA, expressly exclude “money”.

The CRA’s historic position gives rise to an anomaly when consideration for a taxable supply is paid by a customer in the form of virtual currency rather than fiat currency because, in certain circumstances, both the customer and the merchant will be required to charge, collect, and remit GST/HST from one another on the transaction. More particularly, if virtual currency is considered to be a “property” or a “service” (rather than “money”) for ETA purposes, where a customer pays a GST/HST registered merchant for a supply of goods or services using virtual currency as a method of payment, not only would the merchant be obliged to charge, collect, and remit GST/HST from the customer, but the customer might also be regarded as having made a taxable supply of the virtual currency to the merchant. As such, the customer would be obliged to charge, collect, and remit

<sup>4</sup> See CRA Views, 2013-051470117 – Bitcoins (December 23, 2013).



GST/HST from the merchant, provided the customer was a GST/HST registered person and paid for the goods or services in the course of a commercial activity carried on by the customer.

In the view of the Chamber, forcing customers who pay for supplies using virtual currency to charge, collect, and remit GST/HST each time they wished to purchase goods or services would eliminate the efficiency and transaction cost benefits of virtual currencies and make virtual currency payments unworkable from a commercial perspective. Merchants would be disinclined to accept virtual currency as a medium of exchange because doing so would cause the merchants to both: (a) charge, collect, and remit GST/HST on their own supply (as usual); and (b) pay reciprocal GST/HST for having received a supply of virtual currency (which would not be the case if the merchant demanded cash or payment by means of a traditional financial instrument). Virtual currency users currently face a thicket of tax compliance and reporting obligations discouraging adoption of virtual currencies, particularly impacting new and small businesses, and businesses that want to partake in this new medium of exchange.

The Department proposes to address this issue by introducing a “virtual payment instrument” as a new class of “financial instrument” into the definition of “financial instrument” in subsection 123(1) of the ETA. Based on the foregoing and pursuant to the definition of “financial service” in subsection 123(1) of the ETA, sales of virtual payment instruments, use of virtual payment instruments as a payment medium, and a number of other common transactions using virtual payment instruments would either be exempt from tax under the ETA or zero-rated if provided to a non-resident.

While the Chamber supports the intent of the Proposals, which would relieve the GST/HST burden associated with carrying out routine transactions involving virtual currencies by bringing such transactions within the ambit of “financial service,” the Chamber disagrees with the approach taken by the Department to accomplish this intent.

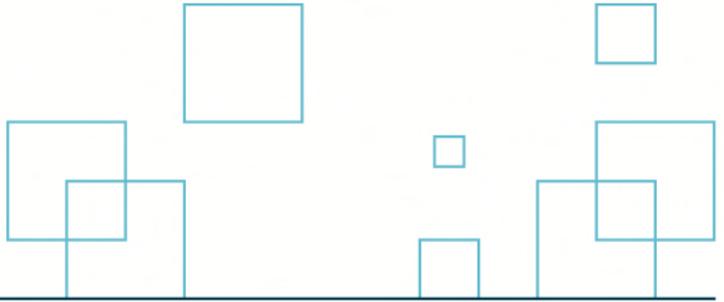
First, the definition of “virtual payment instrument” inherently conflicts with itself and includes confusing and inaccurate terminology. The Proposals define “virtual payment instrument” as follows (emphasis added):

***virtual payment instrument*** means **property** that is a digital representation of value, **that functions as a medium of exchange** and that only exists at a digital address of a publicly distributed ledger, **other than property** that

(a) confers a right, whether immediate or future and whether absolute or contingent, to be exchanged or redeemed for money or specific property or services or to be converted into money or specific property or services,

(b) is primarily for use within, or as part of, a gaming platform, an affinity or rewards program or a similar platform or program, or

(c) is prescribed property[.]



The definition of “virtual payment instrument” requires that a “digital representation of value” (e.g., a virtual currency) be treated as “property.” The definition of “property” in subsection 123(1) expressly excludes “money”, which is itself defined in subsection 123(1) of the ETA to include “currency.” The Oxford English Dictionary defines currency as (emphasis added) “[t]hat which is current **as a medium of exchange**; the circulating medium (whether coins or notes); the money of a country in actual use”. The definition of “virtual payment instrument” in the Proposals requires that, in order to be a virtual payment instrument, a digital representation of value must function as a medium of exchange. The issue raised is that a “medium of exchange” by definition may consist of either property or currency, but the definition provided in the Proposal arbitrarily narrows the application only to property, failing to recognize the ability of virtual currency to serve as a medium of exchange. It is our position that the definition is too narrow and must also recognize and include the term currency given that virtual currency is also an important medium of exchange and not property per se.

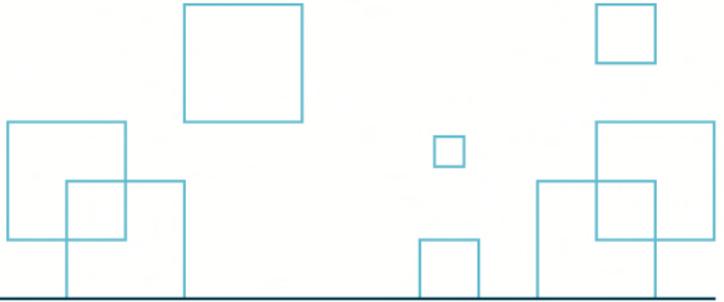
Second, by positioning a “virtual payment instrument” as a form of property, the Department has presupposed that virtual currency does not and will not serve other purposes, such as the economic function of a medium of exchange. By requiring a “virtual payment instrument” to be property rather than currency in order to qualify as a “virtual payment instrument” ignores the many companies that are accepting virtual currencies as payment for goods and services. In fact, central banks around the world, including the Bank of Canada, are contemplating and testing central bank-issued virtual currencies (CBDC).<sup>5</sup>

Third, the definition of “virtual payment instrument” is not broad enough to cover all forms of virtual currencies given that the digital representation of value must “only exist at a digital address of a **publicly** distributed ledger” (emphasis added). This definition already appears not to take into account certain innovations within blockchain such as transactions carried out on private or semi-private side chains. This could effectively leave several situations in limbo.

The Proposals contain a definition for “virtual payment instrument” that excludes certain digital assets from being considered virtual payment instruments if such digital assets (i) have an absolute or contingent right to be exchanged, redeemed, or converted for money or specific property or services or (ii) have a primary use as part of a gaming platform, an affinity or rewards program, or a similar platform or program. These exclusions use unclear language that could cause confusion in the marketplace. For example:

- Some digital assets, such as stable coins, may be asset-backed as to a portion of their value but have the same economic use as a virtual currency such as bitcoin. These assets could

<sup>5</sup> See for example: Bank of Canada, “Central Bank Digital Currency and Monetary Policy” (July 2018), available online: <https://www.bankofcanada.ca/wp-content/uploads/2018/07/swp2018-36.pdf>; Christian Barontini and Henry Holden (Bank for International Settlements), “Proceeding with caution – a survey on central bank digital currency” (January 2019), available online: <https://www.bis.org/publ/bppdf/bispap101.pdf>; and World Economic Forum, “Central Banks and Distributed Ledger Technology: How are Central Banks Exploring Blockchain Today?” (March 2019), available online: [http://www3.weforum.org/docs/WEF\\_Central\\_Bank\\_Activity\\_in\\_Blockchain\\_DLT.pdf](http://www3.weforum.org/docs/WEF_Central_Bank_Activity_in_Blockchain_DLT.pdf).



be excluded from treatment as a financial instrument based on the present wording of the Proposals.

- Other digital assets in development are intended to tokenize conventional equity securities or bonds or the token itself is the security. This affords many benefits such as reducing securities settlement time and counterparty risk as well as increase liquidity (in some cases by fractionalizing the security for trading purposes). If these equity securities were openly traded outside of a token-based platform (through a traditional securities exchange), they would qualify as financial instruments and transactions including issuances, grants and allotments would be financial services under the definition thereof in subsection 123(1) of the ETA. The present definition of virtual payment instrument in the Proposals would appear to exclude the same transactions carried out through the use of a DLT-based token from the treatment otherwise afforded to a financial instrument for ETA purposes.

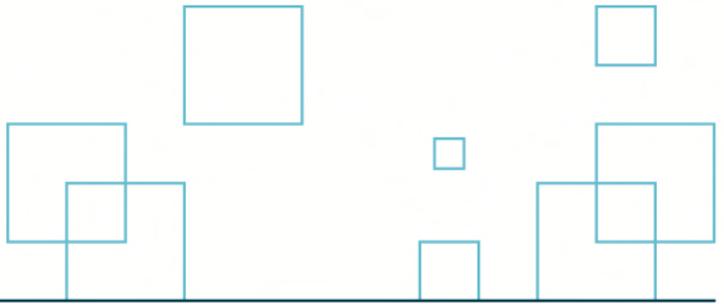
We urge the Department to engage additional industry participants to ensure consistency, enhance clarity, and to better forecast future developments.

### **3. *Additional Considerations***

#### **a. Mining**

While the Department seeks to resolve the potential for merchants and customers who carry out transactions using virtual currencies to have to reciprocally charge, collect, and remit GST/HST against one another, by classifying digital assets as a form of financial instrument, the Department has created ambiguity for miners and other persons who provide hashing power to support blockchains. Miners incur significant expenses subject to GST/HST in order to obtain and operate the infrastructure necessary to process transactions involving certain digital assets. Under the Proposals, it is unclear whether the activities of the miners will be regarded as commercial activities entitling miners to claim input tax credits (“ITCs”) in respect of their costs and GST/HST incurred in such context.

As the capability to claim ITCs is dependent on whether an expense is incurred in order to make taxable supplies (including zero-rated supplies) versus exempt supplies (including financial services), the Chamber believes that additional clarity is required in order to determine the ITC entitlement in respect of the hashing power provided by miners with infrastructure assets in Canada. Where the supplies being made are the processing of transactions through a blockchain and the consideration obtained is a “mining” fee, it is unclear if such supplies are financial services themselves. If such supplies are taxable, it is unclear who the recipient should be and where such supplies are being made. Further clarity is required to determine if such activities can be zero-rated if supplies are exported. All of these questions would affect the capability of a miner to claim ITCs and ultimately impact the competitiveness of the blockchain mining industry in Canada.



The Proposals should be clarified in regard to their impact on miners, as the capability to claim ITCs will factor into investment decisions by firms who are considering whether or not to operate in Canada.

b. Implications under the *Income Tax Act* (Canada)

While the Chamber acknowledges that the Proposals are intended to address the pressing issue of whether or not a transaction carried out using virtual currency would obligate the payor of the virtual currency to charge, collect, and remit GST/HST on a supply of virtual currency, the Chamber believes that any legislative amendments made to the ETA by the Department must be made with a broader policy lens in order to ensure that law and policy in Canada is consistent between legislative regimes. In this regard, it would be difficult to reconcile a divergent treatment of digital assets as between the ETA and *Income Tax Act* (Canada). Treatment of digital assets under one legislative regime impacts how other legislative regimes will be applied to digital assets. In this regard, certain policy gaps exist in the *Income Tax Act* (Canada) that may be influenced by the Department's decision to treat certain digital assets as property for ETA purposes. As discussed, the Proposals treat certain digital assets as a form of "property". The Department should consider the impact of any parallel income tax treatment of virtual currencies as "property". Depending on the context, virtual currencies (and digital assets more generally) serve a variety of different functions within a business. Virtual currencies may represent inventory, collateral, or capital, for example, to a business and serve a growing number of uses ranging from payment instruments to transferable equity to digital contracts.

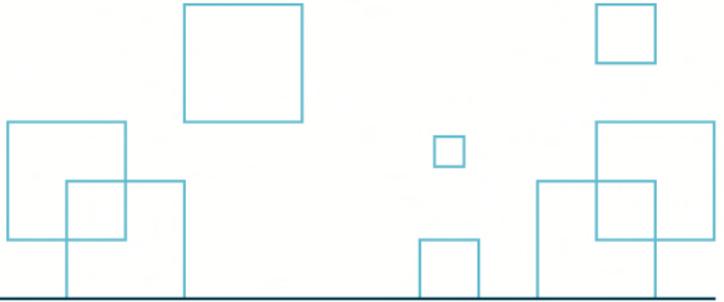
Presently, a transaction transferring one virtual currency (e.g., BTC) for another (e.g., Ether), despite having acquired no fiat currency in the transaction, triggers reporting of any gain on the transaction for income tax purposes. As the CRA presently only accepts payments of tax obligations in fiat currency, in order to pay tax on the potential gain, the person who incurred the gain may have to convert virtual currency to fiat currency, resulting in a second taxable event and a further tax liability to the CRA.<sup>6</sup> As a result, we believe that exchanges of one virtual currency for another should not result in a taxable event. From an *Income Tax Act* (Canada) perspective, the present treatment of transactions involving virtual currency will cause even simple transactions, such as buying a cup of coffee, to result in a taxable capital gain (or loss) or a business income (or loss) – which can be avoided with holistic review and consistent treatment across Canadian laws and regulation.

It is our sincere hope that this consultation is the first in an ongoing dialogue with the industry and that we may serve as a valuable partner in this, and future, consultation processes.

Should you have any further questions, we would be pleased to discuss them with you.

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<sup>6</sup> In this regard, we note that several governments have started to accept the payment of tax obligations in virtual currency. See, e.g.: <https://business.financialpost.com/pmnp/press-releases-pmnp/business-wire-news-releases-pmnp/town-of-innisfil-first-municipality-in-canada-to-accept-cryptocurrency-in-partnership-with-coinberry>, and <https://www.governing.com/topics/finance/gov-ohio-seminole-county-accepting-bitcoin.html>.



Sincerely,

A handwritten signature in black ink, appearing to read 'Tanya Woods'.

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