Inland Revenue
Te Tari Taake

ISSUES PAPER | PUKA TAKE

Income tax – wrapping, bridging, lending, borrowing and staking cryptoassets

A Tax Counsel Office discussion document

Issued | Tukuna: 29 January 2026

IRRUIP18

Cryptoassets are increasingly being used in a variety of peer-to-peer transactions on the blockchain without the involvement of a central party. These transactions are known as decentralised finance (DeFi) transactions. This issues paper sets out the Commissioner's initial views on the income tax consequences arising from common DeFi transactions such as wrapping, bridging, lending, borrowing and staking. The main issue that arises is whether these activities involve disposals of cryptoassets and acquisitions of different cryptoassets for tax purposes.

All legislative references are to the Income Tax Act 2007 unless otherwise stated.

Contents | Ihirangi

About this document | Mō tēnei tuhinga

The Tax Counsel Office release issues papers where sufficient uncertainty exists around a particular issue and we want to hear from interested parties before we prepare a public statement.

Issues papers represent the Commissioner's initial views on a particular tax issue. They are intended to stimulate discussion, invite feedback from interested parties, and help us gain a better understanding of the issues, including the practical concerns of taxpayers.

Inland Revenue officers, taxpayers and practitioners cannot rely on issues papers, as they are not authoritative statements of the Commissioner's stance on the issues covered. Views presented in an issues paper do not change the Commissioner's current position or practices.

If an issues paper results in the issue of a public statement, public consultation will occur on the draft statement in the usual manner.

LET US KNOW WHAT YOU THINK | WHAKAMŌHIOHIA MAI Ō KOUTOU WHAKAARO

We want to know what you think about our initial views presented in this issues paper.

We would like to know:

- if you think the initial interpretation of the relevant tax laws is correct, including our interpretation of how the various DeFi protocols operate.
- if you have any other views on when there is a disposal of a cryptoasset in these transactions.
- if you have any practical concerns about the interpretation, including compliance costs and calculation issues. For example, do crypto tax calculators you use accurately deal with DeFi transactions?
- if you think the result is correct from a tax policy perspective (that is, whether the tax law needs changing).
- your ideas on how to administer the tax laws.

More specific questions may appear in the body of the paper.

Send feedback to | Tukuna mai ngā whakahokinga kōrero ki
Public.Consultation@ird.govt.nz

Deadline for comment | Aukatinga mō te tākupu: **12 March 2026**

Please quote reference | Whakahuatia te tohutoro: **IRRUIP18**

Introduction | Whakataki

1. Cryptoassets are cryptographically secured digital representations of value that can be transferred, stored or traded electronically. They use some form of distributed ledger technology such as blockchain. Cryptoassets may also commonly be referred to as cryptocurrencies, digital tokens or virtual currencies.

2. Cryptoassets can increasingly be used in different transactions across different blockchains and protocols. This issues paper provides the Commissioner's initial view of the income tax consequences arising from particular decentralised finance (DeFi) transactions. DeFi is an umbrella term for financial transactions made peer-to-peer on the blockchain without any central intermediary being involved. Transactions are usually self-executed through smart contracts.

3. The words commonly used to describe types of DeFi transactions may vary across different protocols. The words used to describe these transactions do not always reflect what the transaction is legally. In this issues paper, we have used the words most commonly used, however we also describe the legal effect of each type of transaction.

4. The DeFi transactions we focus on are referred to as:

   - wrapping and bridging;
   - lending;
   - borrowing; and
   - staking.

5. We also explain briefly what we consider the tax consequences are for a person who provides collateral for a loan in a centralised lending transaction.

6. This issues paper does not provide specific guidance on particular protocols. Given the number and variation in DeFi transactions, this paper instead applies general principles to general types of transactions or arrangements.

The initial conclusions reached in this issues paper are based on our understanding of commonly used protocols and DeFi transactions.

We are particularly interested in submissions:

- that highlight gaps in our understanding about how DeFi transactions operate; and

- about other common DeFi transactions that differ to the ones we discuss.

Issues | Take

7. The issues addressed in this paper are as follows:
   - When is the receipt of rewards taxable?
   - When are cryptoassets disposed of in DeFi transactions?
   - What income tax rules could apply to a disposal of a cryptoasset?
   - How do the tax rules apply to particular DeFi transactions?

Summary of initial conclusions | Whakarāpopoto o ngā whakataunga Tuatahi

8. Cryptoassets are personal property for tax purposes, so the tax rules that apply to personal property apply to cryptoassets. Under the personal property rules, receipts of money or money's worth and the disposal of personal property may be taxable. When considering how these tax provisions apply to DeFi arrangements, each transaction entered into must be considered, rather than the arrangement's overall economic substance.

9. The tax consequences of DeFi transactions depend on the terms, conditions and operation of the relevant protocol and their legal effect. Terms and conditions, or an explanation of how the relevant transaction works, can usually be found on the protocol's webpage.

Disposals of cryptoassets in DeFi transactions

10. Disposing of cryptoassets is a significant part of many DeFi transactions. Generally, a disposal of personal property occurs when the person loses ownership rights over the property. A disposal covers all forms of alienation such as a sale, assignment or transfer of property. Ownership of cryptoassets is not recorded on any register. A person disposes of a cryptoasset when they are alienated from it. Alienation occurs when a person no longer has the cryptoasset (ie, when the cryptoasset is no longer in the person's wallet and they no longer hold its private key). A person will be alienated from a cryptoasset when the cryptoasset is transferred out of the person's wallet to a

pool, vault, wallet or a smart contract that is not controlled by that person (and to which they do not hold the private key), and where another person or entity holds the private key and can deal with that cryptoasset as they choose. This could potentially be shown by a transaction hash showing the transfer from the person's wallet to another address.

11. There will not be a disposal of cryptoassets for tax purposes if, while being used in a DeFi transaction, cryptoassets are:

- locked in a separate part of a person's own wallet; or
- transferred into an individual vault or individual smart contract (that is, the cryptoassets are not transferred into a pool with other users' cryptoassets) and the person retains a private key to the assets.

12. Different income tax provisions may apply to a disposal of a cryptoasset where a person:

- has a cryptoasset business (ss CB 1, CB 2 and CB 5);
- acquired the cryptoassets as part of a profit-making undertaking or scheme (s CB 3); or
- acquired the cryptoassets for the dominant purpose of disposal (s CB 4).

13. Determining whether transactions are taxable, and which income tax provision applies, depends on the individual's circumstances. Generally, it is likely that either s CB 3 or s CB 4 would apply. A person may use cryptoassets they already own in DeFi transactions, or they may acquire new ones specifically for certain transactions, for example cross-chain transactions. In many cases, cryptoassets acquired for, or in, DeFi transactions will be acquired for the purpose of disposal because disposals of cryptoassets are essential elements of many DeFi transactions. We therefore consider disposals of cryptoassets in DeFi transactions are likely to be taxable under s CB 4. Alternatively, disposals of any cryptoassets may be taxable under s CB 3 if the person has a profit-making undertaking or scheme.

14. When the person receives another cryptoasset in consideration for that disposal, the relevant amount received is the market value of the new cryptoasset when it is received. Market value can usually be obtained by looking up the value on a centralised exchange. Some cryptoasset tax calculators may also provide the market value of cryptoassets. A deduction is allowed for the cost of acquiring the original cryptoasset disposed of. If these disposals and acquisitions occur within a close period, there may be no net tax liability.

Receiving "rewards"

15. In DeFi transactions, a person can receive rewards for the use of their cryptoassets. Rewards or other amounts may be commonly described as "interest". However, this term is not used in this issues paper. The term "interest" has a specific meaning for tax purposes, generally in relation to money lent. To avoid confusion, we call payments or increases in cryptoassets arising from DeFi transactions "rewards". Rewards are money's worth and are usually taxable when received.

Record-keeping obligations

16. A person must keep clear detailed records of their DeFi transactions to determine whether a tax liability arises from their DeFi transactions. Details required include dates of acquisitions and disposals, receipts of "rewards" and values of the cryptoassets for each transaction. Cryptoasset tax calculators may assist with meeting record-keeping obligations.

Structure of this issues paper

17. For the tax treatment of:

- rewards from DeFi transactions, see [21]–[28];
- wrapping and bridging, see [71]–[76];
- lending, see [77]–[85];
- borrowing, see [86]–[94]; and
- staking, see [95]–[108].

Analysis | Tātari

18. Cryptoassets are personal property. This was confirmed in *Ruscoe v Cryptopia*.[1] Therefore, the tax provisions that apply to personal property apply to cryptoassets. The relevant provisions, discussed below, are ss CA 1(2), CB 1 to CB 5 and DB 23. Receipts and amounts derived from disposals of personal property may be subject to tax under these provisions.

19. DeFi transactions generally involve the receipt and transfer of cryptoassets, sometimes in quick succession. In this issues paper, we summarise the tax provisions and how

[1] *Ruscoe v Cryptopia Ltd (in liq)* [2020] NZHC 728.

they apply to DeFi transactions. We do not cover all DeFi transactions, focusing only on common ones.

20. First, we discuss when a person receives cryptoassets in a DeFi transaction, focusing on rewards. Second, we discuss when a person disposes of cryptoassets by transferring them. Finally, we summarise the relevant law and how we consider it applies to particular DeFi transactions. For a more detailed discussion of the relevant provisions, see QB 21/06: **Income tax – tax treatment of cryptoassets received from an airdrop** and QB 21/07: **Income tax - tax treatment of cryptoassets received from a hard fork**.[2]

When is the receipt of rewards taxable?

21. A person receives a cryptoasset when the person has ownership rights over it. In the context of cryptoassets, this is usually when they have possession and control of the cryptoasset, and can deal with it.[3] A person usually has possession and control of a cryptoasset when they hold the private key to it.

22. Cryptoassets may appear available in a person's wallet but not be able to be used. This could be when rewards accrue to a person but have not been claimed by them or are not yet payable to them. If the person cannot use cryptoassets, the person has not derived them for tax purposes.

23. Some form of reward is usually paid to people who use their cryptoassets in DeFi transactions. Rewards are usually paid in the form of new, additional cryptoassets. Rewards can also be an increase in the value of tokens given to the person in exchange for their original cryptoassets or in the exchange rate when redeeming those tokens.

24. Rewards can be paid frequently, sometimes more than once a day. Payment is usually automatic, although sometimes, rewards may need to be claimed.

25. Generally, we consider a person has derived income from rewards when the person has ownership of them and can deal with them, for example, they are able to use them in other cryptoasset transactions. If rewards need to be collected through some action,

[2] QB 21/07: Income tax – tax treatment of cryptoassets received from a hard fork *Tax Information Bulletin* Vol 33, No 7 (July 2021): 57.

[3] See QB 21/07: Income tax – tax treatment of cryptoassets received from a hard fork *Tax Information Bulletin* Vol 33, No 7 (July 2021): 57. See also comments made by the UK Jurisdiction Taskforce's Legal Statement on Cryptoassets and Smart Contracts (November 2019) at chapter 4 when discussing ownership and transfer of cryptoassets. The Legal Statement has been referred to with approval by Gendall J in *Ruscoe v Cryptopia Limited (in liquidation)* [2020] 2 NZLR 809 (HC).

derivation is when the person has collected the rewards (being the final step taken to have received the rewards and be able to use them).

26. For cryptoasset businesses, receipts of rewards are taxable under s CB 1 as amounts received from a business.

27. For non-businesses, rewards may be income under s CB 3 if the receipts are part of a profit-making undertaking or scheme. These provisions are discussed from [36]. For most people, the most likely provision to apply to the receipt of rewards is s CA 1(2).

28. Section CA 1(2) provides that an amount is income of a person if it is their income under ordinary concepts. An amount is income under ordinary concepts if it is a periodic or recurrent amount; it arises from ownership of property, from capital, or as a result of labour. Where a person receives cryptoassets on a periodic basis as a result of the use of cryptoassets in DeFi transactions, the amount received is likely to be income under ordinary concepts. The amount received is generally the market value of the cryptoassets at the time of receipt.

When are cryptoassets disposed of in DeFi transactions?

29. The term "dispose" is not defined in the Act for the purposes of the provisions addressed in this issues paper (such as ss CB 4 or CB 5). The general principle from case law is that a disposal of property occurs when there is a complete alienation of the property from the owner.[4] This includes a sale, assignment or transfer of the property. One indicator of an asset being alienated from the disposer is where the asset is no longer in the use, control or possession of the disposer in any capacity.[5]

30. In the context of cryptoassets, there is no register of ownership of the asset. The person that holds the private key is the only person that can deal with the cryptoasset.[6] Generally, transfers of cryptoassets are shown by a transaction hash (blockchain record) showing the transfer from one wallet address to another address. In our view, a transfer of a cryptoasset occurs when it is no longer in the person's wallet and they no longer hold the private key. After such a transfer, the cryptoasset is in the control of, and able to be used by, another person who controls the private key. As long as

[4] See: *Northumberland v AG* [1905] AC 406 (HL), *Ward v CIR* [1955] NZLR 361 (SC), *FCT v Wade* [1951] HCA 66; (1951) 84 CLR 105, *Henty House Pty Ltd (in vol liq) v FCT* (1953) 88 CLR 141 (HCA) and *Chapman Bros v Verco Bros and Co Ltd* (1933) 49 CLR 306 (HCA).

[5] *Victory Hotels Ltd v MNR* [1963] Ex CR 123. In the context of cryptoassets, see UK Jurisdiction Taskforce's Legal Statement on Cryptoassets and Smart Contracts (November 2019) at chapter 4.

[6] Other than for a multi-sig situation where multiple keys exist.

the parties are consenting, the transfer of the control of a cryptoasset is generally equivalent to a transfer of ownership of the cryptoasset.[7]

31. In *Ruscoe v Cryptopia*, Gendall J concluded that cryptoassets are property, and linked the necessary control over the asset necessary for ownership with the private key:

> [120] I am satisfied that cryptocurrencies meet the standard criteria outlined by Lord Wilberforce to be considered a species of "property". They are a type of intangible property as a result of the combination of three interdependent features. They obtain their definition as a result of the public key recording the unit of currency. The control and stability necessary to ownership and for creating a market in the coins are provided by the other two features – the private key attached to the corresponding public key and the generation of a fresh private key upon a transfer of the relevant coin.
>
> [121] This identical point is made in the Legal Statement on Cryptoassets and Smart Contracts which says that a cryptoasset is "a conglomeration of public data, private key and system rules."

32. Therefore, for tax purposes, a cryptoasset is considered to be disposed of when the asset's owner transfers it out of their wallet so they are completely alienated from that cryptoasset, and no longer hold the private key. Often, they may receive another cryptoasset (such as a liquidity pool token) or a right to receive back equivalent cryptoassets in the future. Legally, this is not the same as continuing to own the original cryptoassets.[8] DeFi transactions usually involve what are essentially barter transactions, where cryptoassets are exchanged for other types of cryptoassets (or in some cases, rights to receive other cryptoassets in the future). These transactions usually require a disposal of cryptoassets in some way, because they require the cryptoassets to be transferred into smart contracts, liquidity pools or vaults from which other users can acquire the cryptoassets and deal with them. Rights of ownership are lost by the original holder and provided to the new user.

33. Even something that may be considered a temporary disposal of a cryptoasset, such as transferring it to a pool with a right to receive cryptoassets back in the future, is a disposal for tax purposes. This is because the asset is alienated from the transferor.

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[7] See comments made by the UK Law Commission in their final report on Digital Assets (Law Com no 412) at chapter 5 and 6.

[8] We consider this is consistent with statements made by Starke J in *Chapman Bros*, citing *South Australian Insurance Company v Randell* LR 3 P C. 101, that where an identical asset is not to be returned to the original owner, but instead a different asset of equal quantity and quality is to be returned, there has been a transfer of property with title to the original asset vesting in the transferee. See also *Wang v Darby* [2021] EWHC 3054 which considered a sale and re-purchase arrangement involving Tezos and Bitcoin.

Transferring cryptoassets into a liquidity pool involves the original holder losing ownership of their cryptoassets. The assets become intermingled with other assets contributed by other users in the pool, which are then acquired and used by other users. Those users have control over those cryptoassets and can transact with them. On exit, different cryptoassets of an equivalent type or value are returned to the original owner. Therefore, we consider there is a disposal for tax purposes when cryptoassets are transferred out of the user's wallet into a pool with other users' assets, where they can be acquired and used by others.

34. However, a disposal does not include the transfer of cryptoassets:

- between wallet addresses or accounts that belong to the same person;
- to a custodian that holds the assets on trust for the owner with the owner retaining a beneficial interest in those assets;[9] or
- to an individual vault or smart contract, where the cryptoassets are separately held and not pooled with other users' cryptoassets.

35. We consider when disposals of cryptoassets occur in particular DeFi transactions below.

What income tax rules could apply to a disposal of a cryptoasset?

36. The tax treatment of a transaction is determined by the legal rights and obligations actually entered into between the parties. The broad substance of the transaction measured by the overall economic consequence does not determine tax treatment.[10]

37. Our view in this issues paper is based on our understanding of how some common DeFi transactions work. Depending on the type of transaction and the protocol, DeFi transactions generally are likely to involve disposals of cryptoassets, sometimes several disposals in quick succession.

38. It could be argued that cryptoasset lending should be treated like share-lending with tax being imposed on qualifying transactions on the basis of their economic substance rather than their legal form. However, the share-lending rules are specific tax rules that do not apply to cryptoassets. There are also no equivalent provisions which apply to

[9] However, if the owner no longer has ownership of the cryptoasset (which could be indicated by the custodian being able to deal with those assets itself) or receives a different token in exchange for transferring their cryptoasset to a custodian, it is likely there is a disposal.

[10] *Marac Life Assurance Ltd v CIR* (1986) 8 NZTC 5,086 (CA) (at 5,098).

cryptoassets. Accordingly, tax outcomes must be determined under the ordinary income tax rules. Therefore, whether the disposal of cryptoassets in DeFi transactions is taxable depends on whether the following tax rules apply.

Section CA 1(2) – income under ordinary concepts

39. Section CA 1(2) provides that an amount is income of a person if it is their income under ordinary concepts. This was discussed in the context of rewards at [21]–[28], although s CA 1(2) can also apply to other amounts.

Section CB 1, s CB 2 or s CB 5 – business income

40. Sections CB 1, CB 2 and CB 5 apply where a person has a cryptoasset business. Amounts derived from a business are taxable income unless they are capital in nature.

41. Amounts received from the disposal of cryptoassets are taxable income of cryptoasset businesses as any disposal is likely to be the sale of trading stock in the ordinary course of that business or otherwise income from a business under s CB 1. When a business disposes of cryptoassets it holds as trading stock outside the ordinary course of the business or to put an end to the business, the disposal is taxable under s CB 2.

42. Alternatively, a cryptoasset dealer could be taxable under s CB 5, which includes as income amounts a person derives from disposing of personal property if their business is to deal in property of that kind.

43. Other businesses are unlikely to be taxable under these provisions unless disposing of cryptoassets is something that occurs in the ordinary course of the business.

Section CB 3 – income from profit-making undertaking or scheme

44. Disposals may be taxable under s CB 3 where the person is carrying on an undertaking or scheme with the dominant purpose of making a profit.

45. An undertaking or scheme is a series of steps directed to an end result. There needs to be a plan or purpose that is coherent and has some unity of conception.[11] The undertaking or scheme must be carried out for the dominant purpose of making a profit.

[11] *Investment & Merchant Finance v FCT* (1970) CLR 177 (HCA) at 189, *Vuleta v CIR* [1962] NZLR 325 (SC) at 329, *Duff v CIR* (1982) 5 NZTC 61,131 (CA) at 61,141 and *Case S86* (1996) 17 NZTC 7,538 (TRA) at 7,548.

Section CB 4 – property acquired for disposal

46. Income arises from a disposal of cryptoassets under s CB 4 where a person:

- disposes of a cryptoasset; and
- derives an amount or an amount in money's worth from the disposal; and
- acquired the cryptoasset for the dominant purpose of disposing of it.

47. A person can have a dominant purpose of disposal even if the cryptoassets are acquired, or received, and disposed of as part of a wider objective or as a means to an end.[12] For example, if a cryptoasset is acquired for use in a DeFi transaction that requires the cryptoasset to be disposed of in order to undertake the transaction. In that case, the person has acquired that cryptoasset with the dominant purpose of disposal and has immediately disposed of it (even though disposal is part of a wider objective of undertaking the DeFi transaction).

48. What is relevant is what was most important to the person at the time of acquisition of the particular cryptoasset. A person may have one purpose, several purposes, or no particular purpose for buying cryptoassets. The onus is on the person to show whether or not they had a dominant purpose of disposal for each cryptoasset.

49. A person must also have turned their mind to the acquisition. For example, where a person does something to acquire or take possession of cryptoassets, such as providing their wallet address for a smart contract, exchanging their cryptoassets for other cryptoassets in DeFi transactions or claiming additional cryptoassets, the person has turned their mind to acquiring the new cryptoassets.

50. The first step Inland Revenue takes when considering whether s CB 4 applies to a disposal is to consider what the person says their purpose was for acquiring the cryptoassets. Then, that statement is tested against the following objective factors identified by the courts:

- the nature of the asset;
- the length of time the cryptoassets are held;
- circumstances of the acquisition, use and disposal of cryptoassets; and
- the number of similar transactions.

[12] See *CIR v Hunter* [1970] NZLR 116 (CA), *Holden v CIR* [1974] 2 NZLR 52 (PC) and *CIR v National Distributors Ltd* [1989] 3 NZLR 661 (CA).

51. The nature of the asset refers to the particular assets that were acquired. This involves considering the type of asset and what rights the asset confers on the holder.

52. The length of time cryptoassets are held is also important. If a person routinely acquires cryptoassets and uses them in DeFi transactions, the cryptoassets are likely to be viewed as being acquired for disposal as part of undertaking the DeFi transactions. However, this may not always be the case; it depends on the facts.

53. The circumstances of acquisition, use and disposal of cryptoassets and the number of similar transactions involves considering what the person did and whether a pattern of activity exists. Again, this depends on the facts of each case.

54. Considering the factors at [50], it is likely that a person acquiring cryptoassets for use in DeFi transactions will generally have acquired cryptoassets for the purpose of disposal, given that disposals of those cryptoassets are an essential element of undertaking many DeFi transactions. It does not matter that a person has a wider objective in mind and the disposal is only a means to an end.[13]

55. There is no requirement that the person be in business or have a purpose of making a profit. One-off disposals are still taxable if the cryptoassets were bought for the dominant purpose of disposal.

Questions for submitters

Do you think the approach taken in this issues paper is technically correct and/or do you have suggestions for a more appropriate treatment?

It appears that many cryptoasset investors do not realise they have disposed of their cryptoassets in DeFi transactions. We would be interested to receive feedback on why you consider cryptoassets are, or are not, disposed of in these transactions and whether there are any arguments that cryptoassets in these transactions are not acquired for the purpose of disposal.

Subpart EW – financial arrangements rules

56. Some DeFi transactions are referred to as "lending" or "borrowing" transactions although, as discussed in more detail below, they may legally be seen more as a sale and re-purchase arrangement as they involve loss of ownership with a right to acquire or receive cryptoassets in the future. Lending or borrowing transactions may be subject to the financial arrangements rules in subpart EW. The financial arrangements

[13] *CIR v National Distributors Ltd* (1989) 3 NZLR 661 (CA).

rules generally apply to the receipt of money or money's worth in consideration for the provision of money or money's worth in the future.

57. An excepted financial arrangement is not a financial arrangement.[14] A cryptoasset is an excepted financial arrangement unless it meets specific requirements.[15] The requirements are that a consequence of ownership of the cryptoasset is that the owner receives or is entitled to receive, during the period of ownership, amounts that are determined:

- by reference to the quantity or value of the cryptocurrency; and
- on a basis that is known by the owner in advance; and
- not by reference to the profits of a business activity.[16]

58. These requirements need to be met for the period of ownership of the cryptoasset. Relevantly, the amounts must be received or receivable as a consequence of ownership of the cryptoasset. As discussed below in more detail, DeFi transactions generally involve disposals of the cryptoassets and amounts are received as the result of the relevant arrangement entered into (not as a consequence of ownership of a cryptoasset). Therefore, this exception does not generally apply to specific cryptoassets when cryptoassets are used in DeFi arrangements to generate rewards.[17]

59. However, the financial arrangements rules may still apply more broadly to arrangements that qualify as financial arrangements and involve the use of cryptoassets. Even where a financial arrangement exists, if all amounts paid or payable under the financial arrangement are excepted financial arrangements (such as cryptoassets), the financial arrangement rules may not require amounts to be spread or base price adjustments to be performed (as all amounts are likely to be solely attributable to excepted financial arrangements). In that situation, the personal property rules set out above will apply instead.

60. When the financial arrangements rules do apply, many individual cryptoasset investors are likely to be cash basis persons. A cash basis person does not need to spread amounts over the term of a financial arrangement (although they do need to perform a base price adjustment when the arrangement matures). For more information on the

[14] Section EW 4. Section EW 5 explains when there is an excepted financial arrangement.

[15] Section EW 5(3BA) provides that a cryptocurrency is an excepted financial arrangement unless it meets the requirements of subs (3BAB).

[16] Under s EW 5(3BAB).

[17] For more information, see Excluding cryptocurrency from the financial arrangements rules, *Tax Information Bulletin*, Vol 34, No 5 (June 2022): 7.

requirements for cash basis persons, see IS 22/05**: Cash basis persons under the financial arrangement rules.**

61. See Example | Tauira 1 for an example of a cryptoasset based financial arrangement.

Note for submitters: The financial arrangements rules are not the main focus of this issues paper, and we are currently considering whether detailed guidance is needed. We would be interested to know your thoughts on how these rules, and relevant spreading methods, could apply.

Example | Tauira 1 – Application of the financial arrangement rules

Wolfy is thinking about investing for her retirement and is looking for a long-term cryptoasset based investment. She discovers Crypt-Coin Bonds, a crypto-bond which is issued at a discounted price and is repaid in full when the investment matures in 20 years. The yield to maturity rate is set when the bond is purchased. The Crypt-Coin Bond Wolfy purchases has a yield to maturity rate of 5.67%.

The financial arrangements rules apply to the Crypt-Coin Bond.

The bond is not an excepted financial arrangement, as the amount that will be returned to Wolfy is calculated on the value of the Crypt-Coin Bond on a basis that is known to Wolfy when she buys the bond.

Whether or not Wolfy has to spread the income from the Crypt-Coin Bond depends on whether she is a cash-basis person. Wolfy considers the test in **IS 22/05: Cash basis persons under the financial arrangement rules** and considers she is not required to spread the income over the term of the arrangement. However, on maturity, Wolfy will need to calculate a base price adjustment.

Amount of taxable income under the personal property rules

62. When amounts from DeFi transactions are taxable under the above personal property rules, a person has an amount of income to return for tax purposes. The amount may be in money, other cryptoassets or other property. When the person receives another cryptoasset, the amount is the market value of that cryptoasset when it is received.

Returning the income

63. In terms of when to include income from DeFi transactions in a tax return, people who do not hold their cryptoassets as part of a business derive any amounts on receipt of

the cryptoassets (including rewards), that is, when the person can use the cryptoassets. Amounts then need to be converted into fiat (New Zealand dollars) to be included in a tax return.

64. Business owners who return income on a cash basis also return any income when cryptoassets are received. In a few cases, cryptoasset businesses may operate on an accruals basis so need to include amounts that have been earned, but not necessarily received, in their tax return.

Deductions available

65. When the disposal of a cryptoasset is taxable under the personal property rules above, a deduction is allowed for the cost of acquiring the cryptoasset as the cost of revenue account property under s DB 23.[18] The cost of a cryptoasset is the amount spent to acquire it, including any transaction fees. The cost is deducted from the amount of taxable income when the cryptoassets are disposed of. If disposals and acquisitions occur within a close period, there may be no (or a limited) net tax liability.

66. Some cryptoassets, like particular types of liquidity tokens, may be illiquid or not have an ascertainable market value. In these cases, an appropriate cost of the property for s DB 23 purposes could be the market value of the cryptoassets given up to secure the illiquid or non-tradeable token.

67. When the cost of a cryptoasset exceeds the amount of any income derived from disposal, a loss is available if the cryptoassets are held on revenue account; that is, as long as the cryptoassets were acquired for the purpose of disposal, or as part of a business or a profit-making undertaking or scheme.

68. Cryptoassets received as rewards have no cost on acquisition. Therefore, no deduction is available for the acquisition of those rewards.

69. However, given the nature of cryptoassets and DeFi transactions, there is potential for rewards to be taxable at two different points. First, on receipt of the rewards when they are income (see [21]-[28]). Second, on the increase in value of the rewards when they are disposed of (if the personal property rules apply). In these circumstances, our position is that, at the time of disposal, the person may claim the cost of acquiring the cryptoassets as a deduction. This cost is equivalent to the value of the cryptoassets at the time of receipt (on which an amount of tax was already paid). Allowing a cost for

[18] Other deductions may also be available if the person is in business. For more information see: https://www.ird.govt.nz/income-tax/income-tax-for-businesses-and-organisations/types-of-business-expenses.

this amount ensures the person is not effectively taxed twice on the same economic income (being the initial value of the cryptoasset at the time of receipt).[19] For more information, see **QB 21/07**: **Income tax - tax treatment of cryptoassets received from a hard fork.**

How do the tax rules apply to particular DeFi transactions?

70. We now set out how we consider the tax provisions above apply to our understanding of particular DeFi transactions.

Wrapping and bridging

71. Cryptoassets that are native to one blockchain can be wrapped or bridged so they can effectively be used on another blockchain. The original cryptoasset is locked on the source blockchain and a new token, representing the source asset, is created (also known as minted) on the target blockchain.

72. Locking the original cryptoasset generally involves sending the cryptoasset to a custodian address (for wrapping) or to a bridge contract (for bridging). When the transaction is confirmed, the original cryptoasset is no longer in the person's wallet and they are alienated from it. The person receives a new token to use on the target blockchain. The new token may be economically equivalent but it is a different asset to the original (locked) cryptoasset as it is on a different blockchain.

73. To unwrap or bridge back, the wrapped token on the target blockchain is burned, that is, the cryptoasset is permanently removed from circulation and is unrecoverable. Cryptoassets equivalent to the original cryptoassets that were wrapped or bridged are then unlocked by the custodian or bridging contract and transferred to the person's specified wallet.

74. Based on our understanding of the wrapping and bridging process, we consider there is:

- a disposal of the original cryptoasset when it is wrapped or bridged;
- an acquisition of a wrapped or bridged token (regardless of whether the cryptoassets are fungible or non-fungible tokens);

[19] This is consistent with comments made in *Tasman Forestry Ltd v CIR* (1999) 19 NZTC 15,147 (CA), *Sharkey v Wernher* [1956] AC 58 (HL), *Halliwell v CIR* (1991) 13 NZTC 8,197 (HC) and *Rangatira Ltd v CIR* (1996) 17 NZTC 12,727 (PC).

- a disposal of the token if it is transferred to another person or when it is burned; and
- an acquisition of an equivalent but different cryptoasset when the token is burned and the original cryptoasset is unlocked.

75. Determining whether these transactions are taxable, and which income tax provision applies, depends on the individual's circumstances, including whether they are in a cryptoasset business. However, we consider the most likely tax consequences of a wrapping or bridging transaction are as follows:

- The disposal of the original cryptoasset and the subsequent disposal of the token, whether through a transfer or burning, are most likely taxable under s CB 4. This section applies because in many cases cryptoassets acquired for use in DeFi transactions are acquired for the purpose of disposal (as disposals are essential elements of many DeFi transactions).
- For cryptoasset businesses, the amounts are instead taxable under s CB 1 or s CB 2 as amounts received from a business or the disposal of trading stock. Alternatively, the amounts may be income under s CB 5 if they are received by a cryptoasset dealer or under s CB 3 if the receipts are part of a profit-making undertaking or scheme.
- A deduction for the cost of the cryptoasset is allowed against any taxable income.

76. These tax consequences are illustrated in Example | Tauira 2.

Example | Tauira 2 – Wrapping and bridging

Dracs wants to increase his investment in cryptoassets. His best friend Wolfy tells him he can earn rewards using vault-based staking. Wolfy also tells Dracs that Crypt-coin on the Fangsalot blockchain is a trusted long-term store of value. However, the Fangsalot blockchain does not support vault-based staking protocols, which operate on the Crosses blockchain (which is newer and less trusted as a long-term store of value).

Dracs buys $1,000 of Crypt-coin with fiat so he can wrap it and use the wrapped Crypt-coin on the Crosses blockchain (wCrypt-coin). He immediately sends the Crypt-coin to a custodian, which locks it and mints a wCrypt-coin for Dracs to use on the Crosses blockchain for vault-based staking.

After a few months, Dracs unwinds his staking activity, unwraps the wCrypt-coin and receives Crypt-coin on the Fangsalot blockchain in return.

Drac's purpose for acquiring the original Crypt-coin was that it should immediately be swapped for a wCrypt-coin on the Crosses blockchain. Therefore, he acquired the Crypt-coin for the purpose of disposal under s CB 4. The amount of income is the value of the wCrypt-coin derived in the exchange for the original Crypt-coin, which was $1,000. The wCrypt-coin is pegged to the Crypt-coin, so is worth what that Crypt-coin is worth.

Dracs has a deduction under s DB 23 of $1,000 for the cost of acquiring the Crypt-coin he has disposed of. Because Dracs acquired the Crypt-coin and immediately swapped it for wCrypt-coin, Drac's income and deduction from the wrapping transaction match and there is no net tax liability.

Depending on Drac's purpose for acquiring the wCrypt-coin, he may also have income under s CB 4 and a corresponding deduction under s DB 23 when he unwraps the wCrypt-coin in exchange for a Crypt-coin.

Lending

77. Many DeFi protocols offer what is described as cryptoasset "lending". "Lending" in this context usually involves a person transferring their cryptoassets from their wallet to a liquidity pool, from which other users can acquire the cryptoassets with full ownership rights. The person may receive a right to acquire a cryptoasset in the future, or they may receive a corresponding amount of tokens from the liquidity pool (or other protocol used) equivalent to their interest in the liquidity pool.[20]

78. Legally, this is not the lending of an asset but could be more comparable to a sale and re-purchase arrangement. This is because at the time of transferring the cryptoassets to a pool, the person loses ownership of them and the person who receives the assets from the pool has control of them and may deal with them[21]

[20] The liquidity tokens may be created on the transfer of the assets to the pool and can usually be stored, transferred or traded, although not always.

[21] The court in *Wang v Darby* [2021] EWHC 3054 noted whether there has been a sale and re-purchase arrangement or whether cryptoassets are held on trust depends on the facts of the case. When cryptoassets are transferred to another person who is able to deal with them, and there is an agreement with the transferor to return cryptoassets in the future, there is not a trust relationship

79. The value of the cryptoasset transferred into the pool typically fluctuates with the market. The value of the liquidity tokens received in return may be pegged to the value of the transferred asset (or to other things such as the value of the person's interest in the pool).

80. If the liquidity token is pegged to the value of the cryptoasset, then when the value of the cryptoasset goes up or down, the value of the person's liquidity token also increases or decreases. However, in this situation the number of tokens held by the person who transferred their cryptoassets into the pool may increase, as other users pay fees into the pool (usually in cryptoassets).

81. Alternatively, liquidity tokens may be redeemable at an exchange rate relative to the transferred cryptoasset that constantly increases over time based on the rate of return earned by the transferred cryptoasset. In this scenario, the number of liquidity tokens held does not change but the value of those tokens instead increases over time.

82. Once cryptoassets are transferred into a pool, the person can withdraw an equivalent amount from the pool as long as there is sufficient unborrowed liquidity in the pool. To withdraw assets, a liquidity token holder usually burns their liquidity tokens by sending them to a particular address or smart contract. Tokens that are burned are taken out of circulation. The holder then receives cryptoassets from the pool (that may be equivalent to their original assets transferred in, plus additional cryptoassets representing fees or rewards).

83. Based on our understanding of lending transactions, we consider there will generally be:

- a disposal of the original cryptoasset when it is transferred to the lending protocol or liquidity pool;
- an acquisition of a liquidity token representing the person's interest in the pool;
- a disposal of the liquidity token if it is transferred to another person or burned;
- an acquisition of a cryptoasset when exiting the pool (eg, re-acquiring types of cryptoassets initially transferred); and
- an acquisition of cryptoassets as rewards (which may be incorporated into the acquisition above).

84. Determining whether these transactions are taxable, and which income tax provision applies, depends on the individual's circumstances, including whether they are in a

between the parties. Instead, there is a series of transactions between the parties involving full transfers of ownership.

cryptoasset business. Where a right to receive cryptoassets in the future is provided in exchange for the "lending" of cryptoassets, there may be a financial arrangement (see [56]–[60]). However, we consider the most likely tax consequences of these types of transactions are the same as for the wrapping and bridging transactions (at [75]). For the tax consequences of any rewards received, see [21]–[28].

85. How the relevant disposals are treated for tax purposes is illustrated in Example | Tauira 3 and Example | Tauira 4.

Example | Tauira 3 – Lending to a DeFi platform liquidity pool

Wolfy acquires Crypt-coin for $1,000 to lend to a DeFi platform, DeFang, on the Fangsalot blockchain. This requires Wolfy to transfer the Crypt-coin from her wallet to DeFang's liquidity pool. The liquidity pool also has Crypt-coins from other lenders which are lent out to third parties.

In exchange for the Crypt-coin, Wolfy receives a token that represents her share of the liquidity pool (the CC token). The CC token's value is pegged to the Crypt-coin.

The transfer of the Crypt-coin into the liquidity pool is a disposal for tax purposes. The value of the Crypt-coin at the time of its transfer to the liquidity pool is $1,100. As Wolfy's purpose in acquiring the original Crypt-coin was that it should be disposed of (by transferring it to DeFang's liquidity pool), Wolfy has income from the disposal under s CB 4. The amount of income is the value of the CC token received in exchange for the Crypt-coin.

As the value of the CC token is pegged to the value of the Crypt-coin, it is worth what the Crypt-coin was worth at the time of its transfer ($1,100). Wolfy has a deduction under s DB 23 for the cost of acquiring the Crypt-coin that she has disposed of ($1,000).

Because the value of the Crypt-coin increased by $100 between when it was acquired and when it was disposed of, Wolfy has net taxable income from this part of the transaction of $100.

Example | Tauira 4 – Redemption of cryptoassets lent to a DeFi platform liquidity pool

Wolfy decides to get back the Crypt-coin she lent to the DeFang liquidity pool in Example | Tauira 3.

As the pool accumulated a return, Wolfy's CC token balance increased. The CC tokens are to be redeemed 1:1 with the Crypt-coin.

At the time of redemption, Wolfy holds 1.05 CC tokens. The CC tokens are burnt and Wolfy receives 1.05 Crypt-coins. At the time of redemption, the value of a Crypt-coin was back down to $1,000.

Wolfy acquired the CC token with the purpose of disposal, as it needed to be disposed of (burnt) to get equivalent Crypt-coin and any rewards from the pool. Wolfy has income under s CB 4 for the value of the 1.05 Crypt-coins derived on the burning of the CC token. The market value of the Crypt-coins she receives at the time of redemption is $1,050.

Wolfy has a deduction under s DB 23 for the cost of acquiring the CC tokens disposed of. As discussed in Example | Tauira 3, the cost of the CC token to Wolfy was $1,100. There was no cost to her of the additional 0.05 CC tokens she received.

Wolfy has a net loss of $50 from the disposal of the 1.05 CC tokens.

Borrowing

86. "Borrowing" is another term used in many DeFi protocols. When a person is described as having borrowed cryptoassets, they have acquired cryptoassets from a protocol with an obligation to transfer a particular amount of cryptoassets back. As with lending, from a legal perspective these transactions are more comparable to sale and re-purchase transactions.

87. People who undertake these types of arrangements usually need to provide collateral to the lending protocol or platform to secure the transfer of assets to them. In the context of cryptoassets, "collateral" is the provision of other cryptoassets which may be greater in value than the amount of cryptoassets the person wishes to acquire. The collateral is usually locked in smart contracts or vaults until additional cryptoassets are returned into the pool (effectively repaying the "loan").

88. In some protocols, if the value of the collateral drops below a certain threshold, some or all of the collateral amount may be liquidated (sold) to repay the debt. When cryptoassets are liquidated in full, the loan is repaid and the debt is cleared. An amount equivalent to the amount of remaining collateral may be returned to the person after the deduction of penalties or fees. If the value of the collateral has dropped too much, the person may owe additional cryptoassets (or money) to the protocol.

89. While this issues paper focuses on DeFi transactions, these types of transactions can also occur through centralised lending platforms. Centralised lending platforms often use custodians to hold collateral, for either the person or the platform. There are different ways custodians can hold cryptoassets provided as collateral. If a custodian can deal with the assets and the transferor has only a right to get cryptoassets back, then the transferor has lost legal ownership of their assets to the custodian. There is no agency or trust relationship in this case. Where legal ownership is lost, the transferor has disposed of their assets to the custodian for tax purposes. In other cases, the collateral amounts may only be locked without the custodian having received a transfer of those assets – for example where the custodian cannot use and deal with the assets except in a liquidation scenario. In this situation, arguably there has not been a transfer of the assets until such liquidation event occurs.

90. In some DeFi transactions, the collateral is locked in the person's own wallet or a smart contract or vault that is not pooled with other users' cryptoassets, and the person retains the private keys. Ownership of the asset is not provided to another person in that scenario, and the person has not disposed of their collateral.

91. However, in many cases with both DeFi protocols and centralised lending platforms, ownership rights of the collateral are provided to the protocol or platform so it can deal with the collateral, or the collateral is transferred into a pool with other users' cryptoassets. In these cases, other users will acquire and use those cryptoassets, with the original holder only receiving a right to get an equivalent amount of cryptoassets back (unless liquidated).

92. Determining whether these transactions are taxable and which income tax provisions apply, depends on the individual's circumstances and the terms of the protocol. Terms and conditions, or an explanation of how the relevant transaction works, can usually be found on the protocol's webpage.

93. The provision of collateral could fall within the financial arrangements rules depending on the facts (see [56]-[60]). However, generally, we consider the most likely tax consequences are that the transfer of the collateral is a disposal (except in the situations discussed at [90]). A liquidation is also a disposal (if the collateral has not previously been disposed of). If the collateral was acquired for the purpose of disposal (such as for using it as collateral where control of the collateral is provided to the protocol or the collateral is transferred into a pool), there is a taxable disposal. The amount of income from the transaction depends on whether an amount is received for the provision of the collateral. Some protocols or platforms may give a person transferring a cryptoasset for use as collateral a re-acquisition right (a right to re-acquire the assets) as consideration for transferring it. The re-acquisition rights, in

many cases, may be transferred to other people and are money's worth. The value of the rights is generally income.

94. How the provision of collateral is treated for tax purposes is illustrated in Example | Tauira 5 for DeFi lending and Example | Tauira 6 for centralised lending.

Example | Tauira 5 – Borrower provides collateral to DeFi lending platform

Wolfy holds 10 Crypt-coins. She hears about a new Munsturs stablecoin and is keen to acquire some, but has no spare cash. Wolfy does not want to sell her Crypt-coins and decides to use the DeFang protocol to borrow Munsturs.

Under the DeFang protocol, Wolfy is required to provide collateral to borrow the Munsturs. The provision of 10 Crypt-coins as collateral will allow her to borrow 8 Munsturs. Wolfy's Crypt-coins are transferred to DeFang's liquidity pool that also has Crypt-coins provided by other lenders and borrowers.

The provision of Wolfy's 10 Crypt-coins into the liquidity pool as collateral is a disposal for tax purposes.

Example | Tauira 6 – Borrower provides collateral to centralised lending platform

Dracs needs to get hold of some Munsturs so he can purchase a new cape from an online store in Transylvania that only accepts Munsturs as payment. He holds Crypt-coins that he can use as collateral with centralised lending platform Lurchlends.

Lurchlends provides Dracs with a credit wallet. Dracs is the beneficial owner of this wallet. The collateral is locked in Dracs' credit wallet while his loan of Munsturs remains outstanding. It is not pooled with other users' collateral.

Lurchlends has the right to liquidate Dracs' wallet only if a loan-to-value ratio exceeds the maximum permitted threshold.

Once Dracs has repaid his loan and any borrowing fees, the collateral is unlocked and returned to Dracs. Dracs has not disposed of, or re-acquired, this collateral amount.

Staking

95. Staking involves cryptoassets being delegated to validators on some blockchains to act as a form of collateral (or a stake) in the validation process. For the purposes of this issues paper, we consider only general non-custodial staking in the DeFi context. We

do not consider other forms of staking such as solo staking. By solo staking, we mean validators who run their own nodes and use their own cryptoassets as the required collateral. In these cases, the validator does not lose ownership of their cryptoassets. For this reason, we do not consider there is a disposal of cryptoassets when a validator solo stakes. The following analysis does not consider solo staking further.

96. Delegated staking occurs when a person gives a validator the right to use their cryptoassets as collateral in return for payment of rewards. Validators cannot move, spend or control the staked cryptoassets, they just have a right to use the staked assets as a form of collateral for validating transactions on the blockchain.

97. The delegation of a cryptoasset can occur by transferring it to a:

- staking account within the person's wallet where it is locked until it is unstaked;
- staking pool where a group of people combine their cryptoassets to meet the minimum staking requirements for a blockchain; or
- staking service through a smart contract.

98. Where a cryptoasset remains in a staking account in a person's wallet while being staked, there is no disposal of the asset as the owner still has ownership of the cryptoasset. However, where a cryptoasset is transferred into a staking pool with other people's cryptoassets, there is a disposal because the person no longer has ownership of the cryptoasset, which may be acquired and used by another user, and a different cryptoasset will be returned to the original person.[22]

99. The same generally applies where a person uses a staking service. Usually, these services pool the cryptoassets of several people and lock them in a smart contract for a set period. The cryptoassets cannot be used, traded or otherwise transferred until they are unlocked. If the cryptoasset is locked in a smart contract by itself (that is, there are no other cryptoassets from anyone else also locked in the smart contract), there is not a disposal of the cryptoasset. However, if other cryptoassets are locked in the smart contract, there is a disposal because the smart contract has pooled the locked cryptoassets.

100. Another type of delegated staking that usually involves the use of a pool is liquid staking. Generally, liquid staking involves the person transferring their cryptoassets into a pooled smart contract and receiving a liquidity token in return. A liquidity token is a cryptoasset that the person can use instead of the staked cryptoassets.

[22] We consider an analogy could be drawn with the High Court of Australia's comments in *Chapman Bros.*

101. A person can earn staking rewards on their transferred cryptoassets while continuing to use the liquidity tokens in other transactions. Rewards may be paid at periodic intervals while the cryptoassets remain staked or when cryptoassets are unstaked. Rewards are usually paid in the same cryptoassets staked and may be paid automatically or may need to be claimed. The frequency of reward payments varies. The tax consequences of any rewards received is discussed at [21]–[28].

102. When cryptoassets are unstaked or undelegated, cryptoassets equivalent to the value of the staked cryptoassets plus any rewards earned are usually paid to the person.

103. Not all protocols provide additional cryptoassets as rewards for staking. In some cases, the proceeds of staking is an increase in the value of the transferred cryptoassets. This means that, upon unstaking, a person receives the same amount of cryptoassets they transferred but the cryptoassets are worth more. In this case, the gain in value is taxable.

104. A person who stakes or delegates their cryptoassets can also lose their staked cryptoassets through slashing. Slashing is a penalty imposed on a validator when they violate protocol rules, for example, when they are offline too often. A portion of the cryptoassets staked to the validator may be burned which reduces the amount of the stake available to be returned.

105. Whether there is a disposal of staked cryptoassets depends on how the staking protocol or service works. Based on our understanding of common staking protocols, we consider a disposal occurs where:

- a staked cryptoasset is transferred out of the person's wallet into a staking pool, staking account or a staking service such that the person has provided ownership of the cryptoassets to another person or the cryptoassets are pooled with other users' cryptoassets;
- a liquid staking token is burned to unstake the staked cryptoassets; and
- the staked cryptoassets are slashed (and no consideration is provided in return).

106. Determining whether these transactions are taxable and which income tax provision applies depends on the individual's circumstances. However, we consider the most likely tax consequences of any disposals occurring as part of a staking transaction are the same as for the wrapping and bridging transaction (at [75]). That is, the disposal of the original cryptoasset and any liquidity tokens are taxable disposals if the personal property rules apply. The amount of income is the value of any cryptoassets received in consideration.

107. If cryptoassets are slashed, there is technically a taxable disposal although one that would give rise to a loss given no consideration is received.

108. How the relevant disposals are treated for tax purposes is illustrated in Example | Tauira 7.

Example | Tauira 7 – Liquid Staking

Dracs discovers he can make a good return from staking Crypt-coins. He acquires 2 new Crypt-coins and transfers them into a staking pool. In return, he receives 20 liquidity tokens into his wallet.

Rewards are payable three times a day. The rewards are paid daily into Dracs' wallet.

After 6 months, Dracs burns the liquidity tokens to unstake the Crypt-coins. However, the Crypt-coins Dracs gets back are not the same ones he had transferred into the pool.

Overall, Dracs has:

- disposed of 2 Crypt-coins into the staking pool;
- acquired 20 liquidity tokens as consideration;
- disposed of 20 liquidity tokens by burning them;
- acquired 2 Crypt-coins; and
- acquired additional Crypt-coins as rewards.

Dracs has demonstrated that he has a dominant purpose of disposal by acquiring the Crypt-coins for the purpose of staking in a pool (which is a disposal). This disposal is taxable under s CB 4. Under s DB 23, the cost of the Crypt-coins can be offset against the amounts of income from the disposal. If these transactions occur in a short period, there may be no (or a limited) net tax liability.

Whether the liquidity tokens are also taxable on disposal depends on the purpose for which Dracs acquired them. If his purpose was always to burn the tokens in return for the staked Crypt-coins, he acquired the liquidity tokens for the purpose of disposal.

Dracs has also received rewards on a periodic basis so these amounts are taxable under s CA 1(1) as ordinary income at the time of receipt.

This issues paper does not address practical issues of complying with the personal property rules or the financial arrangement rules. After we have considered submissions on the tax issues raised in this issues paper, we will consider whether an operational statement is needed to provide more practical guidance on how to comply with these tax obligations. We are interested to know if you have any suggestions of practical ways that would assist with easing compliance difficulties.

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