



Crypto, NFT, Metaverse & Co. - financial administration gears up

12 | 2023

1 Background

The economic significance of cryptocurrencies is continuously gaining momentum due to constant technological progress and ever new blockchain-based business models. The issues here go far beyond the now familiar trading of cryptocurrencies. Non-fungible tokens (NFTs) and the "gifting" of tokens (airdrops) are increasingly being used by companies as a marketing tool. Transactions are no longer being validated by individuals, but more and more by so-called mining/staking pools. Meanwhile, the metaverse has become a billion-dollar market. While the German Federal Ministry of Finance's letter of 10.05.2022 was able to clarify some questions regarding the taxation of virtual currencies and other tokens in the area of income tax, the Ministry has, from the point of view of VAT law, only come to grips with Web 3.0 in a rudimentary way, at least so far. In order to compensate for this, the tax authorities are now reportedly upgrading internally, through targeted training and expert groups.

2 Publications of the tax authorities to date

In its letter of 10.05.2022, the German Federal Ministry of Finance commented extensively on the income tax treatment of cryptocurrencies. The corresponding publication on VAT already dates back some time. The Ministry's letter on VAT dated 27.02.2018 was issued following the ECJ decision in *Hedqvist* (KMLZ VAT Newsletter 11/2018). It is essentially limited to the validation of transactions through computing power (mining) and the exchange of conventional currencies (fiat money) into cryptocurrencies. Accordingly, a large number of application questions have, so far, remained unanswered in terms of VAT law. In some areas, the Ministry's statements on income tax and VAT even contradict each other. This suggests that the letter on VAT from 2018 is not only incomplete, but also already partially outdated.



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3 Current questions

In the case of blockchain-based business models, questions of VAT law arise at practically all levels of the test scheme - starting with the status as taxable person, determining the place of supply and the applicable VAT rate, and ending with the deduction of input VAT. The following list of practical questions are just some of the questions which currently remain unresolved:

- When is a validator/delegator/NFT creator/trader/liquidity provider a taxable person?
- Where is the place of supply if users only appear with wallet addresses?
- Does the NFT owner or the NFT marketplace supply to an NFT buyer?
- Is the reduced tax rate applicable for art NFTs?
- For which cryptocurrencies beyond Bitcoin does the VAT exemption for financial services under the ECJ *Hedqvist* decision apply?
- Is the VAT voucher regime applicable to NFTs and utility tokens?
- Which metaverse transactions lead to taxable transactions?
- How are the supply relationships in mining/staking pools between delegators, validators, blockchain network and transaction senders to be determined?
- Are transaction senders and the network identifiable recipients of supplies?
- Can validation services be VAT exempt as a transfer of money?
- Does the validator/delegator have a right to deduct input VAT?
- When is there taxable consideration in an airdrop?
- What are the supply relationships when providing liquidity on decentralised exchanges?
- Can a so-called Decentralised Autonomous Organisation (DAO) be a taxable person?

In 2022, the German Federal Fiscal Court ruled that the "rental" of virtual properties in the Metaverse does not fall within the scope of German VAT (KMLZ VAT Newsletter 13/2022). The "landlord" only receives remuneration when he exchanges the in-game currency generated by the "rental" for real money. This exchange constituted a taxable supply of service. It remains unclear to what extent the Court's statements can be generalised and applied to other Web 3.0 business models.

4 Consequences for the practice

Players in Web 3.0 face great legal uncertainty. The well-known VAT assessment scheme reaches its limits when applied to the new business models. However, this does not make the assessment under VAT law obsolete. On the contrary: those affected must assess their situations taking into account the characteristics of the respective blockchain network or token. In this context, the German Federal Fiscal Court's decision on the "rental" of virtual properties in the Metaverse must not be over-interpreted. Cryptocurrencies and other tokens as well as NFTs are not to be considered the same as in-game currencies. This applies equally to the blockchain and the Metaverse. In these areas, a proper separation and consideration of the individual case is indispensable.

In the past, for VAT purposes, crypto, NFT and metaverse transactions often flew under the radar of the tax authorities. In the future, the focus will no longer be solely on the income tax treatment. The tax authorities have laid the foundation for a VAT treatment of Web 3.0. A comprehensive guidance letter would be desirable to accompany this. This would not only benefit the companies, but ultimately also the tax authorities themselves.