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HOWARD COLLEGE

“Bitcoin and eSwatini Income Tax Order 1975 (King's Order in Council No. 21 of 1975)”

By

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‘This mini-dissertation is submitted in partial fulfilment of the requirements for the degree of Master of Laws in Business Law’.

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Abstract

Bitcoin usage and growth has gradually had an impact on the virtual world and financial markets of mostly South Africa, which has resulted in the Cryptocurrency being gradually adopted by eSwatini. The central bank of eSwatini has therefore noted that there have been reported cases of Bitcoin usage in the kingdom of eSwatini. However, with this growth the eSwatini Revenue Services has not made any statement or pronouncement on the possible tax treatment of the Cryptocurrency whilst on the other hand the central bank of eSwatini has begun the process of conducting research on how to regulate Cryptocurrencies in eSwatini. This situation in eSwatini has therefore presented us with a gap in literature and therefore an opportunity to conduct this study ensued on how Bitcoin can be treated for Income Tax purposes by the eSwatini Income Tax Order. This study has been conducted by focusing mainly on the direct tax consequences of the Cryptocurrency in eSwatini and South Africa, which may arise, and an examination of possible gaps in the eSwatini jurisdiction since there has been no pronouncement by the eSwatini Revenue Authority. Furthermore, brief lessons from the United Kingdom and the United States of America's position on the tax treatment and regulation of the Cryptocurrency have been explored. The UK and USA have been selected for this study because they have more advanced regulations in relation to Cryptocurrency and a higher prevalence of Cryptocurrency transactions than both eSwatini and South Africa. Furthermore, in conducting the study South Africa has been selected because the common law of both South Africa and eSwatini is relatively similar and has been adopted from both the Roman-Dutch and English common law. A further preferred feature about the South African jurisdiction is that it shares a border and a similar socio economic environment to that of eSwatini. Having identified the gaps in the eSwatini jurisdiction the study has therefore concluded that the findings on the gaps necessitate the application of tax on worldwide income, and the implementation of Capital Gains Tax to the Swati tax legislation. Furthermore, the study has uncovered that in order to achieve this the eSwatini Revenue Authority must seek to find a proper classification for Cryptocurrency which will aid in the application of tax on the new digital currencies.

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List of Abbreviations

CBE	Central Bank of Eswatini
ERA	Eswatini Revenue Authority
IFWG	Intergovernmental Financial Working Group
NT	National Treasury
SARB	South African Reserve Bank
FSCA	Financial Sector Conduct Authority
FIC	Financial Intelligence Centre
SARS	South African Reserve Bank
FATF	Her Majesties Revenue & Customs
IRS	Internal Revenue Services

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CHAPTER 1: BITCOIN AND THE ESWATINI INCOME TAX ORDER 1975

1.1 Background

The growth of Cryptocurrency usage and its general integration into financial markets has caused a huge challenge for financial regulators and tax collecting bodies. This is because these Cryptocurrencies do not have a central governing body or authority that governs their existence and as a result, a number of illicit activities have been associated with digital currencies.¹ This has caused a legal international concern regarding Cryptocurrencies. Developing countries such as the Kingdom of eSwatini² and South Africa are now therefore faced with the challenge of how to legally address Cryptocurrencies such as Bitcoin, because of their growing adoption.³

In South Africa, Bitcoin has had a significantly high impact and adoption. High Bitcoin usage and growth has been experienced, which has been growing gradually since the Cryptocurrency's introduction in 2009.⁴ Bitcoin growth and usage in South Africa is at the forefront in the Southern African region. Furthermore, South Africa houses Cryptocurrency development teams in exchange centres like Luno, BitX and Bithub in Cape Town.⁵ These centres have been largely used for both the processing of Cryptocurrency transactions and their development.⁶ Moreover, with South Africa sharing a border and a relatively similar socio economic environment with the Kingdom of eSwatini, these countries have both recorded the use of Cryptocurrencies such as Bitcoin on platforms such as Bitstamp, where fiat currency (real money) has been bartered for this Cryptocurrency.⁷ Although eSwatini has not had much activity with regard to Bitcoin transactions, many Bitcoin investors have fallen prey to Bitcoin

¹M K-Meng Ly 'Coining Bitcoin's 'Legal-bits': Examining the Regulatory Framework for Bitcoin and Virtual Currencies' (2014) 27 *Harvard Law & Technology Journal* 588, 608 available at <http://www.woodlump.com/Media/Press/pdf/Coining.pdf> accessed 14 March 2019.

² It must be noted that Swaziland had its name changed officially to the Kingdom of eSwatini on the 5th of September 2018 and is still in a transition phase with regard to the names of entities and titles given to statutes, therefore a variation of the name of the country will be encountered throughout the research.

³Op cit note 1 at 608.

⁴C Greeff, 'An investigation into the output tax consequences of bitcoin transactions for a South African value-added tax vendor', (2019) 22, *South African Journal of Economic and Management Sciences* 1, 1 available at <http://www.scielo.org.za/pdf/sajems/v22n1/16.pdf> accessed 15 April 2019. "Bitcoin as a means of payment for goods and services has grown substantially over the past few years with more than 100 South African merchandizers accepting Bitcoin as a means of payment. In addition, Bitcoins traded in South Africa on Luno has increased from 1000 Bitcoins per week in 2016 to between 4000 and 7000 Bitcoins per week as of 9 November 2017".

⁵LL Berger 'Bitcoin exchange transactions: Income tax Implications to consider within the South African environment (unpublished mini dissertation, Northwest University 2016) 2.

⁶Ibid 2.

⁷Ibid 2.

investment scams.⁸ In March of 2018, an estimated 15000 Emaswati (Swati's) were swindled out of over R200 million in a scam known as the Bitcaw Trading Company scam.⁹ Moreover, in South Africa, the same happened two months later when 28 unsuspecting South African investors were swindled out of over R 1 billion in the same scam as that of eSwatini.¹⁰

This high level of criminal activity associated with this digital currency is due to the anonymous nature of Bitcoin, which bars third parties from each transaction's information, when transferring Bitcoin amongst its users using computer-powered technology.¹¹ Moreover, this anonymous feature only allows interested persons to see the transaction movements, and no record of who has processed such a transaction is given.¹² The Kingdom of eSwatini and other countries thus face a big challenge in alleviating a large amount of criminal activity associated with Cryptocurrency transactions, and this has to be done by creating an appropriate legal framework that will adapt to the fast growing world of Cryptocurrencies.¹³

Moreover, the growth of Cryptocurrency users in the region raises the concern that if there are no law or policy developments to address the question of Cryptocurrency, then illicit activities associated with Bitcoin will gradually escalate in eSwatini.¹⁴ In addition, this is made evident by the fact that, since the active usage of Bitcoin began in 2013, there have been no published tax tribunal rulings, government publications, consultation papers, and interpretation notes addressing the question of regulation and tax treatment of Cryptocurrency in eSwatini.

The Central Bank of eSwatini (CBE), in a recent official statement on virtual currencies, stated:

“The eSwatini, Central Bank Order of 1974 (As Amended) stipulates that only notes and coins issued by the Central bank shall be legal tender.¹⁵ The bank noted that due to its nature as a Cryptocurrency there are no restrictions, disclosures or regulatory compliance mechanisms,

⁸T Dlamini 'Swazi's lose Over E200M in Bitcoin scam' Swazi observer 3 March 2019 available at new.observer.org.sz/details.php?id=3932 accessed 23 March 2019.

⁹Ibid.

¹⁰Ibid.

¹¹A Bal 'Bitcoin Transactions: Recent Tax Developments and Regulatory Responses' (2015) 17 *Derivatives & Financial Instruments* available at https://www.ibfd.org/sites/ibfd.org/files/content/pdf/dfi_2015_05_int_2.pdf accessed 26 March 2019.

¹²Grindberg R 'An Innovative Alternative Digital Currency' (2011) 4 *Hastings Science & Technology Law Journal* 159, 164.

¹³M.S Wicht 'The Tax Implications of Bitcoin in South Africa' (Unpublished Mini Dissertation University of Pretoria 2016) 10.

¹⁴Ibid.

¹⁵Central Bank of Swaziland 'Public Statement on Virtual Currencies Bitcoin' 25 August, 2017 available at <http://www.centralbank.org.sz/media/releases/cbsbitcoin.jpg> accessed 23 march 2019.

applicable to transactions executed using bitcoin and yet like any other currency it can be used for illegal purposes or to facilitate fraudulent activity.”¹⁶

The Bank further noted

“In line with its mandate to issue and redeem currency as well as to promote safe and accessible payment systems it continues to closely monitor developments in the financial services industry with a view to ensuring that the regulatory framework remains relevant and appropriate.¹⁷ The bank acknowledged its role in supporting innovation and the adoption of new technologies in the industry. The bank stated that together with many other regulatory institutions worldwide it will adopt an optimistic but cautious view and that the financial services will certainly benefit from these technologies, but that their development and deployment must be done in a manner that sufficiently safeguards the interests of the users”.¹⁸

The official statement by the CBE therefore highlights a gap that the bank is now in the process of filling by adopting a proper financial regulatory framework for Cryptocurrency in eSwatini. However, we first consider the definition of ‘financial regulation’, which has been defined as “rules and laws regulating firms operating in the financial industry, such as banks, credit unions, insurance companies, financial brokers and asset managers.”¹⁹ Therefore, Bitcoin, being a currency, falls within the monitoring purview of the CBE which raises the duty to protect the integrity of financial transactions within eSwatini.

The eSwatini Revenue Authority (ERA), on the other hand, has not made any official statement yet on the application of tax on Cryptocurrencies such as Bitcoin, and has maintained a conservative stance towards Cryptocurrencies.²⁰ In a recent press statement, the eSwatini Revenue Authority Director of Communications, Vusi Dlamini, expressed the local tax authority’s scepticism around Bitcoin, and cautioned people against being easily carried away by the phenomenon. He stated that many technicalities about the Bitcoin phenomenon should be ascertained and clarified first before taxation can be considered.²¹

However, the legal aspects on the taxation and regulation of Bitcoin in South Africa, on the other side of the border, is at an advanced stage. The year 2016 saw the establishment of the

¹⁶Central Bank of Swaziland op cit note 15.

¹⁷Ibid.

¹⁸Ibid.

¹⁹Central Bank of Ireland ‘What is financial regulation and why does it matter?’ available at <https://www.centralbank.ie/consumer-hub/explainers/what-is-financial-regulation-and-why-does-it-matter> accessed 30 November 2020.

²⁰H Ndlovu ‘SRA Wary of taxing Bitcoin earnings’ Swazi observer 5 February 2018 available at new.observer.org.sz/details.php?id=3932 accessed 23 March 2019.

²¹Ibid.

Intergovernmental Fintech Working Group (IFWG). The group included the National Treasury (NT), South African Reserve Bank (SARB), Financial Sector Conduct Authority (FSCA) and the Financial Intelligence Centre (FIC).²² The aim of the IFWG has been to share ideas and knowledge on the regulatory and policymaking aspect of Financial Technology (FinTech).²³

Tasked with the mandate to “review the position on Crypto assets” a working group was formed in early 2018, as a subsidiary of the IFWG. This group is made up of personnel from both the IFWG and the “South African Revenue Service (SARS)” collectively known as the Crypto Assets Regulatory Working Group.²⁴ The IFWG has also been working hand in hand with SARS which has also recently issued a media release on the 6th of April 2018, stating SARS’ stance on the Tax Treatment of Cryptocurrencies. It stated,

“SARS will continue to apply normal Income Tax rules on Cryptocurrencies and will expect affected taxpayers to declare Cryptocurrency gains or losses as part of their taxable income..... SARS for Income Tax purposes classifies Cryptocurrencies as assets of an intangible nature.²⁵Whilst not constituting cash, Cryptocurrencies can be valued to ascertain an amount received or accrued as envisaged in the definition of “gross income” in the Act. Following normal income tax rules, income received or accrued from Cryptocurrency transactions can be taxed on revenue account under “gross income”. Alternatively, such gains may be regarded as capital in nature as spelt out in the Eighth Schedule of the Income Tax Act for Taxation under Capital Gains.”²⁶

In essence, from the media release we see that the existing tax laws on normal tax still apply to Cryptocurrencies in South Africa. In addition, SARS has also taken the initiative to classify Cryptocurrencies such as Bitcoin for tax purposes which has been applauded by the IFWG as a positive step.

Therefore, it must be noted that in conducting this research Bitcoin will be used as a reference point to analyse the question of regulation of Cryptocurrency. Bitcoin is used because it is of high value compared to other Cryptocurrencies in the financial market. Furthermore, in its

²²South African Department of the National Treasury: *Consultation Paper on Policy Proposals For Crypto Assets* (2018) 4,1 available at http://www.treasury.gov.za/comm_media/press/2019/CAR%20WG%20Consultation%20paper%20on%20crypto%20assets_final.pdf accessed 12 July 2019.

²³Ibid.

²⁴Ibid.

²⁵South African Revenue Services: ‘SARS Stance on the taxation of crypto currencies 6 April 2018 available at <http://www.sars.gov.za/Media/MediaReleases/Pages/6-April-2018---SARS-stance-on-the-taxation-of-cryptocurrencies.aspx> accessed 19 April 2019.

²⁶Ibid.

media release SARS refers to Bitcoin as an example of the most widely used Cryptocurrency in the virtual world, which can also be exchanged for fiat currency. Therefore, Bitcoin is the digital Cryptocurrency most likely to be encountered by taxpayers for disclosure to the relevant tax authority in eSwatini.²⁷ Having discussed the background we now move on to discuss the research problem question of this study.

1.2 Research Problem/Question

The advent of Bitcoin into the Southern African region, and the Cryptocurrency's rapid development have created a problem for the central bank of eSwatini, in terms of how to classify these assets for regulation purposes and the eSwatini Revenue Authority, with regard to the application of tax on Bitcoin in the kingdom of eSwatini. The cause of this problem is the anonymous nature of Bitcoin, which also contributes to the promotion of criminal activity and tax evasion through Bitcoin transactions. Furthermore, the rapidly evolving technology around Cryptocurrency has made it difficult for financial regulators in eSwatini to apply regulations to govern Cryptocurrencies and to develop a suitable classification for the tax treatment of Cryptocurrencies and this has created a gap in the literature, which this study seeks to address. This study seeks to address this gap by seeking lessons from the South African perspective on how to treat Bitcoin transactions for tax purposes. The goal will be to explore how Bitcoin transactions can be treated for tax purposes in eSwatini. Furthermore, an examination of the United Kingdom and the United States of America will be briefly undertaken to acquire lessons on how tax may be applied in these cases, in an effort to explore solutions for the tax treatment of Cryptocurrencies (mainly Bitcoin) in eSwatini. It must be noted further that this research will cover the regulatory development of this Cryptocurrency and its taxation in the various abovementioned jurisdictions up to the end of the year 2019 in finding solutions for the eSwatini. This stance emanates from the fact that the law regarding this subject is developing at a fast pace as studies and questions regarding Cryptocurrencies such as Bitcoin are being answered at a frequent and fast moving rate.

1.3 The Rationale of the Study

In the past decade, the eSwatini Government has revised its revenue collection legislation and structure to improve "revenue collection including rationalising the tax structure and rates,

²⁷Dr F Moosa *The income tax treatment of Bitcoin and other cryptocurrencies* (unpublished thesis, University of the Western Cape 2019)18.

https://www.academia.edu/37325492/Income_tax_treatment_of_Bitcoin_and_other_cryptocurrencies_in_South_Africa?auto=download accessed 14 July 2019.

replacing the sales tax with value-added tax, introducing a source based tax system and modernisation of the tax administration system”.²⁸ Since its reformation the eSwatini tax system does not apply tax on amounts that are received or accrued outside eSwatini, but only assesses income that is received or accrued within eSwatini. As a result, the system does not cover worldwide income like its counterpart South Africa.²⁹

The idea to conduct this research stems from the notion that most developing countries, particularly in the Southern African region, including South Africa and eSwatini, face a major challenge on the regulation and imposition of tax on Bitcoin because of the Cryptocurrency’s anonymous nature. As a result, this has left eSwatini in a vulnerable position because the anonymity when conducting transactions using Bitcoin, opens up the potential to the escalation of illicit activities.

1.4 Research questions

The study seeks to address the following questions:

1. What is the conceptual formulation of Bitcoin?
2. How can the current, tax and regulatory position in eSwatini possibly classify and apply tax on Bitcoin?
3. How the South African government currently regulates Cryptocurrencies and the application of tax on Bitcoin by SARS, in South Africa?
4. What lessons can be derived by eSwatini from other jurisdictions on the regulation and the taxation of Cryptocurrencies such as Bitcoin.

1.5 Research Objectives

To address the questions posed and the problem statement of the study the following objectives will be used;

1. The study will investigate the background of regulations on Bitcoin use in eSwatini and South Africa.
2. The study will then explore the nature of Bitcoin, and how it operates in the digital space.

²⁸Institute of policy research and analysis working paper 58 (2017) on ‘The Reform of the Tax System in Swaziland’ I, I available at <https://mpira.ub.uni.muenchen.de/84739/> accessed 24 March 2019.

²⁹N Musviba; South African Tax Guide, ‘Taxation made easy; Swaziland Personal Income Tax; Swaziland Taxes Overview’ available at <https://www.sataxguide.co.za/swaziland-taxes-overview/> accessed 5 April 2019.

3. An exploration of the need to address the application of tax on, and regulation of Bitcoin.
4. An investigation into how Swati legislation can possibly address and apply to Bitcoin.
5. An investigation into the developments of how South Africa has addressed the regulation of Cryptocurrencies and their regulation.
6. The study will undertake a brief investigation into how the United Kingdom and the United States has applied tax on Cryptocurrencies.
7. The study will then highlight possible recommendations by making an analytical comparison of the Swati legislation to that of South Africa.

1.6 Research Methodology

In conducting this study for purposes of obtaining data, desktop research is used where data is collected from existing sources. This kind of research can be put to use in two ways which include “internal desk top research” where existing resources of data are used. Another form of desktop research is “external desk research”, and this kind of research is conducted “outside organizational structures”. This type of research also exists in two forms, which are firstly, the use of the internet to collect information that already exists in the worldwide web. Secondly, government published data, which involves collecting useful information from government publications.³⁰

To make recommendations and acquire lessons to get solutions, Secondary data will be collected in support of the desktop research and this is data that is readily available from other sources and these sources will include journal articles, case law, academic dissertations, published reports, Interpretation notes and policy papers will be assessed. To draw lessons for eSwatini, the UK and the USA have been selected, mainly because they have a large number of transactions involving the use of Bitcoin. The UK and the USA have further developed regulatory measures and tax treatment of Bitcoin, which can be useful for brief lessons for the kingdom of eSwatini. South Africa has also been selected in this study because eSwatini and South Africa have a similar social and economic environment making a study of South Africa’s jurisdiction more favourable and more appealing to derive lessons for eSwatini.

³⁰ P Juneja ‘Desk Research Methodology and Techniques’ available at <https://www.managementstudyguide.com/desk-research.html> accessed 16 April 2019.

Selection of the countries is based on the following criteria:

- (i) Firstly, Bitcoin-related financial activity is highly prevalent to these countries in varying degrees compared to eSwatini.
- (ii) Secondly, advanced legal frameworks pertaining to regulations and collection of revenue by the tax authorities of these countries have reached advanced levels.
- (iii) Thirdly, Swaziland depends mainly on South Africa for socioeconomic and legal guidance.

1.7 Structure of the Dissertation

The research will be presented in the form of chapters which make part of the format of the mini-dissertation.

1.7.1 Chapter 1: Introduction

Introduction and a background will form the introductory parts of this chapter and they will briefly outline the history of Bitcoin, and the regulatory and tax treatment developments of Bitcoin. The research problem of the study, which also sets out the purpose statement, will also be presented in this chapter. The chapter then goes on to present the rationale of the study, research methodology and the structure of the dissertation.

1.7.2 Chapter 2: Bitcoin and its general nature

This chapter will explore the concept of Bitcoin as a Cryptocurrency and the impact of Bitcoin as a virtual currency. The chapter will then go on to explore how the Bitcoin system operates in the digital space, how Bitcoin is used in commerce, tax evasion, and criminal activity associated with Bitcoin, the OECD and BEPS action plan and how to own a Bitcoin. The chapter will also briefly discuss the need to determine the tax treatment of Bitcoin in eSwatini and then a conclusion will end the chapter.

1.7.3 Chapter 3: Bitcoin and the Income Tax Order of 1975 of eSwatini

This chapter provides an investigation into the current developments in the regulatory framework on Cryptocurrencies in eSwatini. The chapter assesses the current tax legislative framework in eSwatini and how Bitcoin would fit into the current tax legislative framework. The chapter will then address the need for the regulation and tax treatment of

Bitcoin in eSwatini by assessing briefly the vulnerability to illicit activities if the Cryptocurrency is ignored. The chapter will then end with a conclusion.

1.7.4 Chapter 4: South Africa's current legal regulatory framework and Tax treatment of Bitcoin and brief lessons from other jurisdictions

This chapter provides a brief description of the current South African regulatory framework on virtual assets, in particular Bitcoin. The main aim of this chapter is to understand how South Africa has classified Bitcoin in its regulatory framework, and further explore how South Africa addresses the question of imposing tax on Bitcoin transactions. The chapter will then briefly assess other international jurisdictions to draw lessons for eSwatini and end with a conclusion.

1.7.5 Chapter 5: Lessons from the International jurisdictions Recommendations For eSwatini and Conclusion

This chapter provides an analysis of the current financial regulatory framework in eSwatini in relation to that of South Africa, further absorbing lessons from international jurisdictions to find ways on how best tax can be applied on Bitcoin transactions within eSwatini. The study will also explore additional taxation methods or types that can be injected to the tax legislative system of eSwatini to efficiently apply tax on virtual assets in eSwatini. The chapter will then conclude the research, a conclusive summary of the discussions from all the chapters will be made, The chapter will then explain the contributions, and also give ideas to conduct research on the subject in the future.

CHAPTER 2: BITCOIN AND ITS GENERAL NATURE

2.1 Introduction

Cryptocurrencies are a highly advanced technological innovation of digital Cryptocurrency, which has the potential to contribute immensely to the way we conduct transactions in the financial sector across the globe. This technological innovation, although having potential also presents a number of challenges that are associated with its nature, mainly around addressing the legal challenges the innovation presents. In light of these attributes, as a point of departure and before exploring the legal aspects regarding the regulation and tax treatment of Cryptocurrencies, the study first examines the different attributes that make up and are associated with Bitcoin.

2.2 The Concept of Bitcoin

Bitcoin was invented by a person or persons using the pseudonym Satoshi Nakamoto, a decade ago. In light of this invention, KPMG has defined Bitcoin as “digital units of account in which cryptographic techniques are used to regulate the generation and distribution of units on a blockchain”.³¹ A feature about this Cryptocurrency is that it uses ‘block chain technology’³² to operate and to maintain a high level of anonymity and privacy.³³ Moreover, this currency is a form of digital electronic money, “a decentralised digital currency”, with no central governing body to monitor its transactions. Bitcoin is shared amongst its users on what is called a “peer-to-peer Bitcoin network” without a need for third party intervention.³⁴ Bitcoin, is not backed by any financial governing authoritative body, or government.³⁵ Instead, using, “heavily encrypted hash codes across a peer-to-peer network” many online traders and merchants accept

³¹The ‘Institutionalization of Crypto assets Cryptoassets have arrived. Are you ready for Institutionalization’ (published in NDPPS 775054 of November 2018) available at <https://assets.kpmg/content/dam/kpmg/us/pdf/2018/11/institutionalization-cryptoassets.pdf>; accessed on 26 March 2019.

³² E Reddy, V Lawack ‘An Overview of the Regulatory Developments in South Africa Regarding the Use of Cryptocurrencies’ (2019) 31 South African Merchantile Law Journal, 12 available at <https://journals.co.za/content/journal/10520/EJC-1a76e8f6e1> accessed 2 December 2020. Defines blockchain as “a public transaction ledger built into the Bitcoin Protocol. Once a transaction is conducted and subsequently validated by a *miner*, a block containing the transaction details of the sender and recipient is generated and added sequentially on the network, forming a chain of transactions.”

³³ Institutionalization of Crypto assets opcit note 30 at 19.

³⁴The ‘Statement of Jennifer Shasky Calvery, Director Financial Crimes Enforcement Network United States Department of the Treasury before the United States Senate Committee on Homeland Security and Government Affairs’ (published on November 18 2013) available at <https://www.fincen.gov/sites/default/files/2016-08/20131118.pdf> accessed 15 April 2019.

³⁵M Rouse ‘Bitcoin’ available at <https://whatistechtarget.com/definition/bitcoin> accessed 5 April 2019.

the Cryptocurrency as payment for goods and services.³⁶ There are now a number of Cryptocurrency dealers, which exchange Bitcoin for real money. Examples include Luno, AnycoinDirect and Coinbase.

The use of this Cryptocurrency has been promoted largely because its transaction costs are cheap and the anonymity of users is preserved.³⁷ This Cryptocurrency provides a more efficient method of sending and receiving money worldwide through internet use, and transactions can be completed with anyone in the world without knowing their identities.³⁸ The anonymous nature of Bitcoin has therefore placed a significant challenge for financial regulators and tax regulating bodies worldwide. In addition, Cryptocurrency has experienced considerable growth within the unregulated virtual financial markets worldwide.³⁹ As a recent development, Bitcoin has also attracted the interest of a number of large companies and internet traders that use this Cryptocurrency when concluding transactions.⁴⁰

The growing phenomenon of Bitcoin has attracted the interest of many writers on this topic who are still studying and understanding the nature of this fast-growing Cryptocurrency. Consequently, there are few publications to provide guidance on the tax and regulatory aspects of Bitcoin.⁴¹ The void in the literature is a cause of concern because Bitcoin is making significant inroads into the Southern African unregulated virtual financial markets, especially in South Africa and eSwatini. In both these countries, Bitcoin has the potential to become a preferred investment instrument like gold, substituting long-established forms of currency and investment with those based in the digital space.⁴² In exploring the potential presented by

³⁶Ibid.

³⁷B Atkins et al. 'A Whole New World: Income Tax Considerations of the Bitcoin Economy' (2014) 12 Pittsburgh Tax Review 25, 25 available at <https://taxreview.law.pitt.edu/ojs/index.php/taxreview/article/view/32/48> accessed 25 April 2019.

³⁸M Rouse op cit note 35.

³⁹Yellin T, Aratan D, Pagliery J 'What is bitcoin?' available at <https://money.cnn.com/infographic/technology/what-is-bitcoin/index.html> accessed 15 April 2019.

⁴⁰The Working Party on Financial Statistics 'How to deal with Bitcoin and other cryptocurrencies in the System of National Accounts?' (published in COM/SDD/DAF(2018)1 of 29 October 2018) available at [http://www.oecd.org/officialdocuments/publicdisplaydocumentpdf/?cote=COM/SDD/DAF\(2018\)1&docLanguage=En](http://www.oecd.org/officialdocuments/publicdisplaydocumentpdf/?cote=COM/SDD/DAF(2018)1&docLanguage=En) accessed 24 April 2019.

⁴¹B Atkins et al. op cit note 37 at 25.

⁴²Institutionalization of Crypto assets op cit note 31.

Bitcoin we take a much closer look into the Cryptocurrency and the impact it has made on the financial and tax arenas.

2.3 The Impact of bitcoin

Fiat currency (real money), has traditionally been governed and administered by central governing bodies. These governing bodies have historically used strenuous systems of money transfer, often not concluding transactions in some instances.⁴³ Examples of this are central banks. However, in Cryptocurrency usage, blockchain technology has empowered Bitcoin to process transactions faster, and in a more cost-effective and efficient manner for its users, superseding the traditional methods of payment.⁴⁴

This technological phenomenon has further facilitated transacting between ‘person-to-person (‘P2P’) and or person to business (‘P2B’)’ in essence functioning in the same manner as the normal methods of concluding transactions.⁴⁵ Transacting using this Cryptocurrency further relies on the exchange of Cryptocurrency to fiat currency (Bitcoin to real money), through instant exchange platforms allowing for the receipt of real money in exchange for Bitcoin, anywhere in the world.⁴⁶ A known example is Coinbase, a Bitcoin exchange that also has a presence in South Africa.⁴⁷ Through this service, users are able to enjoy same time money transfers to anywhere in the world, without identifying themselves, and paying only two percent of the amount they are sending for the service.⁴⁸

Blockchain technology has provided a solution for sending money electronically, by not only facilitating money transfers through this technology but also ‘integrating several components of the trade-clearing settlement value chain in an elegant, efficient and digital way’.⁴⁹ Users advocating for the use of Bitcoin have contended that financial service providers need to integrate Bitcoin into their systems in order to increase its legitimacy in society, because its characteristics make it a suitable form of alternative payment instrument.⁵⁰

⁴³Institutionalization of Crypto assets op cit note 31.

⁴⁴Institutionalization of Crypto assets op cit note 31.

⁴⁵ E Reddy, V Lawack Op cit note 32 at 12.

⁴⁶T, I Kiviat ‘Beyond bitcoin: Issues in Regulating Blockchain Transactions’ 2015 (65) *Duke Law journal* 569, 587 available at <https://scholarship.law.duke.edu/cgi/viewcontent.cgi?article=3827&context=dlj> accessed 21 June 2019.

⁴⁷Ibid.

⁴⁸Ibid.

⁴⁹Ibid.

⁵⁰Ibid.

Bitcoin's easily attainable and secure nature, without any third party interference, would make it a preferred investment for investors in the financial markets.⁵¹ If adopted, the Cryptocurrency can provide solutions to many challenges that fiat currency currently imposes on the financial services markets.⁵² However, an impediment to the solutions presented by Bitcoin is the anonymous nature of Bitcoin. A brief examination of the scientific digital nature of Bitcoin will aid in understanding how the anonymous characteristic of the currency poses a significant challenge for regulatory and tax purposes.

2.4 Bitcoin as a Virtual Currency

Bitcoin is a form of virtual asset, defined by the Financial Action Task Force (FATF)⁵³ as:

“A digital representation of value digitally traded or transferred and can be used for payment or investment purposes, including digital representations of value that function as a medium of exchange, of account, and or store of value.⁵⁴ The FATF emphasises that virtual assets are distinct from fiat currency (a.k.a. “real currency,” “real money,” or “national currency”), which is the money of a country that is designated as its legal tender.”⁵⁵

In addition, Bitcoin is a Cryptocurrency and Cryptocurrencies are Virtual Currencies,⁵⁶ which are types of virtual assets. They are distinguished from the real money used every day,⁵⁷ examples of which are the Swati lilangeni and the South African Rand. Virtual Currencies are digital currencies because they only need the use of the internet to operate, requiring multiple

⁵¹Ibid.

⁵²Institutionalization of Crypto assets op cit note 31.

⁵³Financial Action Task Force ‘Regulation of Virtual Assets’ available at <http://www.fatf-gafi.org/publications/fatfrecommendations/documents/regulation-virtual-assets.html> accessed on 28 March 2019. ‘The FATF is an intergovernmental organization founded in 1989 on the initiative of the G7 to develop policies to combat money laundering, terrorism financing and also monitors progress in implementing the FATF recommendations through ‘peer reviews’ mutual evaluations of member countries housed at the OECD headquarters in paris.’

⁵⁴Ibid.

⁵⁵Ibid.

⁵⁶Financial Action Task Force ‘Virtual Currencies Key Definitions and Potential AML/CFT Risks’ available at <https://www.fatf-gafi.org/media/fatf/documents/reports/Virtual-currency-key-definitions-and-potential-aml-cft-risks.pdf> accessed 31 October 2019. “Virtual currency is a digital representation of value that can be digitally traded and functions as (1) a medium of exchange; and/or (2) a unit of account; and/or (3) a store of value, but does not have legal tender status. (i.e., when tendered to a creditor, is a valid and legal offer of payment) in any jurisdiction. It is not issued nor guaranteed by any jurisdiction, and fulfils the above functions only by agreement within the community of users of the virtual currency.”

⁵⁷Ibid.

participation to work efficiently, in the virtual space,⁵⁸ through interaction.⁵⁹ Therefore, Bitcoin, a Cryptocurrency, as abovementioned⁶⁰ is a Virtual Currency in nature and its functioning involves the producing of ciphers⁶¹ that allow the currency's information to be kept private.⁶² The umbrella term for classifying Bitcoin is “digital currency” a term used to define money that only exists on the internet.⁶³

Virtual Currencies are not supplied by any governing body, nor does any governing body give assurance to its users, in addition, when using these currencies users complete their transactions through consensus amongst themselves online.⁶⁴ The European Central Bank points out that Virtual currencies are divided into three commonly recognised virtual currency schemes, which are:

“Closed virtual currency schemes,”⁶⁵ - refer to systems where the virtual currency has no link to the real economy and are connected with computer games and they can only be spent within the virtual environment and cannot be used to purchase goods or services outside of that environment. The most common use of closed-flow currency is within video gaming environments, such as World of Warcraft.⁶⁶

Virtual currencies with unidirectional flow- can be purchased directly using real currency at a specific exchange rate, but they cannot be exchanged back to the original currency. The scheme owner establishes the conversion conditions. These schemes allow the currency to be used to purchase online goods and services. Examples of virtual currency schemes with unidirectional flow include Facebook advertising credits, Nintendo points, and airlines' frequent flyer miles.⁶⁷

Virtual currencies with bidirectional flow- can be bought and sold according to the exchange rates to real currency. The virtual currency seems to be similar to any other

⁵⁸W Erlank 'Introduction To Virtual Property: Lex Virtualis Ipsa Loquitur' (2015) 18 Potchefstroom Electronic Law Journal, 2531 available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2753716 accessed 3 December 2020.

⁵⁹Ibid.

⁶⁰Financial Action Task Force op cit note 56.

⁶¹Cambridge Dictionary 'Cipher' available at <https://dictionary.cambridge.org/dictionary/english/cipher> accessed 13 November 2019. 'a system of writing that prevents most people from understanding the message.'

⁶²Yessi Bello Perez 'The differences between cryptocurrencies, virtual and digital currencies' available at <https://thenextweb.com/hardfork/2019/02/19/the-differences-between-cryptocurrencies-virtual-and-digital-currencies/> accessed 18 May 2019.

⁶³ Ibid.

⁶⁴Financial Action Task Force op cit note 56.

⁶⁵OS Belomytseva 'Conceptual Framework for the Definition and Regulation of Virtual Currencies: International and Russian practices' 2015 (61) *De Gruyter Open Review Paper* 32, 34 available at <https://www.degruyter.com/downloadpdf/j/ngoe.2015.61.issue-5/ngoe-2015-0020/ngoe-2015-0020.pdf> accessed 23 July 2019.

⁶⁶ Ibid.

⁶⁷ Ibid.

convertible currency with regard to its interoperability with the real world. Virtual currency schemes with bidirectional flow allow for the purchase of both virtual and real goods and services. One example of virtual currency schemes with bidirectional flow is Bitcoin.⁶⁸

In addition, Virtual Currencies are also classifiable as “centralised or decentralised”, and “convertible or non-convertible”.⁶⁹ “Convertible” virtual currencies are those that have a value that is equivalent to real currency, to which they may be exchanged. Virtual Currencies exist in two constant⁷⁰ and server controlled⁷¹ subsets, which include centralised convertible and decentralised convertible Virtual Currencies. “Centralised convertible virtual currencies” rely on an intermediary that exercises control and distributes the Virtual Currency, initiates directives for usage among principals in transactions, ‘maintains a central payment ledger’ for the currency and possesses the requisite control for retrieving it.

“Decentralised convertible virtual currencies” are on the other hand root based, issued, scientific, user-to-user virtual currencies with no intermediary governing body, and no intermediate supervision. These currencies are typified by Bitcoin, Litecoin and Ripple. These currencies are considered Cryptocurrency, math-based and protected by cryptography.⁷² For purposes of this research, we concentrate on the functioning of Bitcoin as a Cryptocurrency that uses blockchain technology in the digital space of the financial markets.

2.5 How the bitcoin system operates in the digital space

The functioning of Bitcoin relies on a user-to-user network that is free from oversight and financial service provider intermediaries. The network further manages verification, distribution and the processing of numerous Bitcoin transactions all at the same time.⁷³ This Cryptocurrency relies on the encryption of its transactions, protecting its operation and transaction information from being viewed by other parties, mainly to validate transactions and manage the generation of the Cryptocurrency.⁷⁴ In completing Bitcoin transactions, Bitcoin

⁶⁸Ibid.

⁶⁹Dr F Moosa op cit note 27 at 3.

⁷⁰W Erlank op cit note 58 at 2528.

⁷¹Ibid.

⁷²Financial Action Task Force op cit note 56.

⁷³Her Majesties Revenue and Customs ‘Revenue and Customs Brief 9 (2014): Bitcoin and other cryptocurrencies’ available at

<https://www.gov.uk/government/publications/revenue-and-customs-brief-9-2014-bitcoin-and-other-cryptocurrencies/revenue-and-customs-brief-9-2014-bitcoin-and-other-cryptocurrencies> accessed 29 April 2019.

⁷⁴M.S Wicht op cit note 13 at 21.

users are assigned secret cryptographic identities, which is an essential feature of this Cryptocurrency.⁷⁵

When conducting a transaction, a user must, in the encrypted communication, during a transaction, endorse Bitcoins from him or herself to another user ‘essentially putting a lock and a key on each Bitcoin.’ A set of encrypted symbols, numbers, and letters, then make up the identity of a person that uses Bitcoin.⁷⁶ When sending the Cryptocurrency to a particular inscription the transferor of the Bitcoin transfers the Bitcoins to an exclusive and exposed matching identical key upon linking it with his key, through a communication informing the transferee of the number of Bitcoins he is receiving. The last stage involves the transferor completing the transaction by allowing his private key to be known by the public as a signature. Thereafter the transferor then transmits the transaction nodes to the receiver of the Bitcoin.⁷⁷

2.5.1 Blockchain technology and Bitcoin

To issue new Bitcoins into the virtual community, an activity called ‘mining’ takes place. Any person using a highly technologically advanced computer system that is able to go online can do this process resulting in the issuance of new Bitcoins.⁷⁸ Users that conduct this activity are called ‘miners’.⁷⁹ During the mining process, a new Bitcoin is produced when a newly created block links with the chain, the link takes place when, after a user solves a particular puzzle, they get to link the block to the chain, extending the blockchain and making the user eligible to claim rewards. As rewards, the user receives new Bitcoins and fees that are connected to the Bitcoin transactions that the user has completed.⁸⁰ A blockchain has been defined as a distinctive sub element of “distributed ledger technology (DLT)’ that serves as a pathway that records, carries and distributes coded information “ across multiple data stores (also known as ledgers) in the virtual space, which each have the exact same data records and are collectively maintained and controlled by a distributed network of computer servers, which are called nodes.”⁸¹ The Bitcoin blockchain has been designed in such a manner that it is able to record

⁷⁵Ibid at 21.

⁷⁶S Gruber ‘Trust, identity and disclosure: Are Bitcoin Exchanges the next virtual havens for money laundering and tax evasion note’ (2013) 32 *Quinnipiac Law Review* 144, 146.

⁷⁷Ibid.

⁷⁸E Reddy, V Lawack op cit note 32 at 12 (See paragraph 2.2).

⁷⁹Ibid at 12.

⁸⁰Ibid at 12.

⁸¹Cryptocurrencies and blockchain ‘Legal Context and Implications for Financial Crime, Money Laundering and Tax Evasion’ (published in B-1047 Brussels of June 2018) available at <http://www.europarl.europa.eu/supporting-analyses> accessed 27 November 2020.

and carry all data during Bitcoin transactions.⁸² In addition, newly created Bitcoins are also recorded on the blockchain, which has led to users often referring to the blockchain as a ‘ledger of the Bitcoin system’ where all the Bitcoin transactions are recorded.⁸³ As the transactions take place, the database shared to the public records them and they are then called a ‘blockchain’. The blockchain is made up of blocks that form a chain, these blocks have newly recorded information on the transactions, which has not been recorded on any previous blocks. All the blocks in the chain will then individually confirm the authenticity of all the previous blocks up to the first created block through encrypted proof.⁸⁴

To facilitate the receiving, storing and sending of Bitcoins in unit form the user must download what is called a Bitcoin wallet. To use the wallet to send, receive or store Bitcoin, users would have to download a phone or computer application to facilitate the completion of transactions, which is similar to online banking. Digital wallets enable users to store Bitcoin. The wallet exists in an internet cloud, which can be accessed by a phone or computer application that must be downloaded. The wallet is essentially an online bank account without the interference of any intermediary, which allows the user to send, receive and store Bitcoin value. The only disadvantage about a digital wallet is that it cannot be insured.⁸⁵

In addition, wallets have individual encrypted keys, that the general public has access to, which are not tied to anyone’s personal identity and a user may use this key as an inscription to send and receive Bitcoins.⁸⁶ When processing transactions, information on the user’s identity is always kept private by the key, keeping transactions anonymous.⁸⁷ Moreover, the key enables the user to process the transaction and when it has been processed, the transaction will then be generated to the whole community of Bitcoin users.⁸⁸

Once the funds have been transferred, the receiving user may then trade the Bitcoin for real currency.⁸⁹ To facilitate the exchange in commerce, Bitcoin users may use the many available Bitcoin exchange platforms that trade in Cryptocurrency, where they are allowed to open

⁸²A Berensten F Schar ‘A short introduction to the world of Cryptocurrencies’ (2018) 100 *Federal Reserve Bank of St Louis Review*, first Quarter 4-5, 1 available at <https://files.stlouisfed.org/files/htdocs/publications/review/2018/01/10/a-short-introduction-to-the-world-of-cryptocurrencies.pdf> accessed 13 July 2019.

⁸³Ibid.

⁸⁴S Gruber op cit note 76 at 146.

⁸⁵GBBIT ‘About Bitcoin’ available at <https://www.gbbbit.com/pages/aboutbitcoin/> accessed 23 July 2019.

⁸⁶M.S Wicht op cit 13 at 21.

⁸⁷Ibid at 21.

⁸⁸Ibid at 21.

⁸⁹A Berensten; F Schar op cit note 82 at 5.

accounts to facilitate exchange, or alternatively the user may opt to invest the Bitcoins and withdraw real money at a later date.⁹⁰ The scientific nature of Bitcoin presents a more efficient way to conduct transactions using the Cryptocurrency in a quick and cost effective manner as the Cryptocurrency integrates into the commerce of both eSwatini and South Africa. Therefore, an exploration into the ways in which the Cryptocurrency can be used in commerce is essential in understanding the nature of the Cryptocurrency.

2.6 Using Bitcoin in Commerce

Bitcoin presents users with a number of ways that they can use to access services in commerce. Users can invest by storing monetary value in Bitcoin. Users can also buy goods and acquire certain services and thirdly users can exchange Bitcoin for real money.⁹¹ These transactions can be completed in the many virtual currency exchange platforms available like Anycoin Direct.⁹² To facilitate Cryptocurrency use, service providers such as “financial firms ranging from hedge funds to large asset managers” make it possible for users to complete Cryptocurrency transactions.

In addition, educational institutions are beginning to allow the use of Cryptocurrencies to facilitate fee payment.⁹³ The use of Cryptocurrencies to facilitate fee payment is, according to the website Futurism.com,⁹⁴ practiced by some European Universities, which include universities situated in Germany and Switzerland, and some universities in the United States, which have all been reported to accept Bitcoin as payment for fees. Moreover, in the beginning of 2013, according to the website cheap air.com,⁹⁵ a company that facilitates travelling services, including the buying of flight tickets, hotel bookings, car rentals and the booking of cruise ship tours, these amenities can now be purchased using Cryptocurrency.⁹⁶

Furthermore, to fund service provision, new business start-ups and the production of goods, beginner entrepreneurs without the use of conventional ways of raising capital such as the use of internet sites to raise money have resorted to Cryptocurrency as a method to raise funds.⁹⁷ Therefore, in light of the above developments it is evident that many business establishments

⁹⁰Ibid at 5.

⁹¹The Working Party on Financial Statistics op cit note 40 (See paragraph 2.2)

⁹²Ibid.

⁹³Ibid.

⁹⁴K Leary ‘Schools Are officially Accepting Bitcoin for Tuition’ available at <https://futurism.com/schools-accepting-bitcoin-tuition> accessed 28 November 2019.

⁹⁵Cheapair.com ‘Bitcoin cool ways to spend your cryptocurrency on vacation’ available at <https://www.cheapair.com/blog/category/bitcoin/> accessed 28 November 2019.

⁹⁶Ibid.

⁹⁷Ibid

and institutions are starting to adopt the use of Cryptocurrencies. Thus drawing from this context it is evident that in the near future Cryptocurrencies will attract a number of users who may wish to acquire ownership of Bitcoin.

2.7 Bitcoin Ownership Acquisition

To obtain Bitcoin, persons or traders may in the process of trading, barter goods or services for payment in Bitcoin, instead of real money, although this may not be the case in many countries such as the kingdom of eSwatini, which still does not yet have Bitcoin exchange platforms like its counterpart South Africa to facilitate the exchange of Bitcoin.⁹⁸ Bitcoin users may also acquire bitcoins through ‘mining’ which demands the usage of highly powered technology as discussed above.⁹⁹

In addition, another common way among users of acquiring Bitcoin is when a user pays an exchange platform or kiosk, like Coinbase or Bitstamp, which are web market Cryptocurrency exchanges where users can complete Bitcoin transactions by exchanging real money for Cryptocurrency.¹⁰⁰ People may also acquire Bitcoins through marketing or advertising campaigns and in this instance, the receivers of the Bitcoins are randomly selected as part of the campaign and this method of acquiring Bitcoin is called an Airdrop.¹⁰¹ The acquisition of Bitcoin is available to users in a number of ways and this aspect about Bitcoin creates a gap in the Cryptocurrency, which has created room for exploitation by criminals to facilitate illicit activities since the Cryptocurrency is not yet regulated in many jurisdictions.

2.8 Tax Evasion and Criminal Activity

Bitcoin technology has introduced new and efficient ways of transferring money worldwide but in as much as transactions can be available on the Bitcoin log for everyone to see, the users’ identities are never revealed, barring Bitcoin wallets to be exposed for third party view.¹⁰² The anonymity of these transactions as a consequence allows users with criminal intent to purchase and distribute whatever they want, with no way of tracing the transactions back to them. This

⁹⁸Her Majesties Revenue & Customs ‘Policy paper for individuals’ available at <https://www.gov.uk/government/publications/tax-on-cryptoassets/cryptoassets-for-individuals> accessed 23 July 2019.

⁹⁹S Gruber op cit note 76 at 147.

¹⁰⁰A M Antonopoulos *Mastering bitcoin unlocking digital Crypto-currencies* 1st ed (2010) 10 available at <https://unglueit-files.s3.amazonaws.com/ebf/05db7df4f31840f0a873d6ea14dcc28d.pdf> accessed 18 May 2019.

¹⁰¹Her Majesties Revenue & Customs op cit note98. “An airdrop is where someone receives an allocation of tokens or other cryptoassets, for example as part of a marketing or advertising campaign in which people are selected to receive them. Other examples of airdrops may involve tokens being provided automatically due to other tokens being held or where an individual has registered to become eligible to take part in the airdrop.”

¹⁰²Yellin T, Aratari D, Pagliery J op cit note 39.

has led to Bitcoin being a favourable currency to use in the conduct of unlawful activities using the internet.¹⁰³

In addition, Bitcoin has, through its technology, developed the characteristic of instant money transfer to any country worldwide, providing relief for criminals from processes that limit the speed of money transfer which require clearance from banks when using electronic funds transfers.¹⁰⁴ In addition, the absence of a central governing body such as a bank or central bank, its anonymous nature and the ability to be transferred instantly worldwide exposes Bitcoin to the wider unregulated virtual financial markets allowing a high degree of criminal activity.¹⁰⁵

Therefore, while the Bitcoin phenomenon presents a new, highly efficient and innovative technology for conducting financial transactions online, its anonymity strongly suggests that there is a gap that needs to be covered by developing countries such as the kingdom of eSwatini, in terms of tax and financial regulation. This can be done by introducing new and stricter measures to safeguard against the potential rise of illicit criminal activities that are associated with the Cryptocurrency, further facilitating a smooth integration and advancement of Bitcoin into the financial market of eSwatini. This need to address the gap posed by Cryptocurrency as noted above by developing countries has also been recognized by international organizations such as the Organisation for Economic Cooperation and Development. The organization has therefore formulated a Base Erosion and Profit Shifting Action Plan to address the formulation of regulations and tax rules for Cryptocurrencies.

2.8 OECD and Basic Erosion and Profit Shifting Action Plan

The rising need for developing countries to develop their regulatory measures and tax rules has also been emphasised by global organisations such as the Organisation for Economic Cooperation and Development (OECD).¹⁰⁶ This has been done in conjunction with the G20 countries, through a Base Erosion and Profit Shifting Plan (BEPS), which was developed emphasising the need for group efforts to upgrade tax rules.¹⁰⁷ The purpose for this is to strengthen supervision of Multinational Enterprises (MNE's), which Bitcoin exchange

¹⁰³Ibid.

¹⁰⁴The 'European parliament study requested by the tax 3 committee Cryptocurrencies and blockchain. Legal context and Implications for financial crime, money laundering and tax evasion.' (published in PE 619.024 of July 2018) 1, 53 available at http://www.europarl.europa.eu/cmsdata/TAX3_Study_on_cryptocurrencies_and_blockchain.pdf accessed 10 May 2019.

¹⁰⁵Ibid.

¹⁰⁶Organization for Economic Co-operation and Development 'Taxing Multi-national Enterprises Base erosion and profit shifting' (2015) *Policy Brief* available at <https://www.oecd.org/ctp/policy-brief-beps-2015.pdf> accessed 22 May 2019. 'South Africa is one of the non-member economies with which the OECD has work relationships.'

¹⁰⁷Ibid.

platforms can be classified under, to disclose profits and value that is created in the course of conducting economic activity.¹⁰⁸

Globalisation has also promoted the necessity for cooperation amongst countries globally, to be aware of and updated on the fast-evolving digital world economy.¹⁰⁹ In a bid to promote this kind of cooperation, the OECD/BEPS project through joint action with the G20 nations, sets out a plan of action with fifteen set actions to aid governments with domestic and international instruments. These instruments are to be used to equip member countries to target economically active areas of the economy, where profits and value are created in a bid to combat tax avoidance and maximise the taxation of profits.¹¹⁰ The recent developments in the financial markets with the integration into the market of digital currencies was identified as being at the forefront of issues that need to be addressed by the BEPS action plan.¹¹¹

The countries proposed the development of two pillars, which formed the essence of the agreements between the countries.¹¹² Under the ‘first pillar’, the countries viewed the challenges that have been brought about by the digitalisation of the global economy.¹¹³ The countries proposed the improvement of the current rules by taking into account factors such as the division in the traditional methods of applying tax on multinational corporations among members.¹¹⁴ This took into account the issue that ‘traditional transfer pricing rules and the arm’s length principles’ were in need of some modification to adapt to the new technologies of the financial markets.¹¹⁵ Under the “second pillar” the consensus between the countries was to find ways to solve BEPS action plan issues focusing on ways to provide solutions in cases where no or very low taxation is applied on income.¹¹⁶

Moreover, in 2013, the OECD, as part of the action plan responding to the growing use of virtual currencies highlighted in a workpaper issues that needed attention.¹¹⁷ These included

¹⁰⁸Ibid.

¹⁰⁹Ibid.

¹¹⁰BEPS Actions ‘Base Erosion and Profit shifting’ available at <https://www.oecd.org/tax/beps-actions.htm> accessed 22 May 2019.

¹¹¹OECD/G20 Base Erosion and Profit Shifting Project ‘Addressing the Tax Challenges of the Digitalisation of the Economy’ 2019 available at <https://www.oecd.org/tax/beps/policy-note-beps-inclusive-framework-addressing-tax-challenges-digitalisation.pdf> accessed 23 May 2019.

¹¹²Ibid.

¹¹³Organization Economic Corporation and Development ‘International community makes important progress on the tax challenges of digitalisation’ available at <https://www.oecd.org/tax/beps/international-community-makes-important-progress-on-the-tax-challenges-of-digitalisation.htm> accessed 23 May 2019.

¹¹⁴Ibid.

¹¹⁵Ibid.

¹¹⁶Ibid.

¹¹⁷C Greeff op cit note 4 at 2.

the issue of capital gains and losses in Cryptocurrency transactions and the use of the Cryptocurrency's anonymity to avoid taxes when using virtual currencies.¹¹⁸ The plan presented by the OECD is in line with its mission to stimulate progress and world trade in the economies of developing countries that are part of the OECD/G20 inclusive framework on BEPS, which includes both South Africa and eSwatini.¹¹⁹ This approach by the OECD will in essence aid in guiding the kingdom of eSwatini to address the tax treatment of Cryptocurrency and the formulation of financial regulations.

2.9 The Need for the Tax Treatment of Bitcoin in eSwatini.

The growth and integration of digitalised currencies in the global financial markets has had a ripple effect on the less developed financial markets like eSwatini. Therefore, the call for the modification of regulations to meet the standards of the new age strongly suggests that governments understand the need for clarifying the tax treatment of Bitcoin globally. Thus, developing countries need to review their tax rules, with a view to modifying them to aid domestic enterprises that may wish to trade using Bitcoin as a currency.¹²⁰

The need for prompt action in applying taxes to, and the regulation of, Bitcoin is necessitated by Bitcoin's traditional characteristics, making it favourable to criminals as a means of tax avoidance or evasion because its functioning does not depend on any intermediaries. Furthermore, earnings from Bitcoin cannot be easily subjected to taxation because the taxpayer's anonymity is maintained by its pseudonymous nature.¹²¹ Moreover, since financial markets are now technologically advanced and the economy is becoming more digitalised, ignoring the growing adoption of Cryptocurrency would be detrimental to the existing forms of payment systems because of the efficiency in conducting financial transactions offered by Cryptocurrency.¹²²

In addition, since governments depend highly on the collection of taxes as a source of income to function efficiently, effective regulation is an important means of ensuring tax compliance

¹¹⁸Ibid.

¹¹⁹Organization for Economic Corporation and Development 'Members of the OECD/G20 Inclusive Framework on BEPS' available at <http://www.oecd.org/tax/beps/inclusive-framework-on-beps-composition.pdf> accessed 31 October 2019.

¹²⁰Ibid.

¹²¹O Marian, 'Are Cryptocurrencies Super Tax Havens?' (2013) 112 *Michigan Law Review First Impressions* 38, 38

available at: http://repository.law.umich.edu/mlr_fi/vol112/iss1/2 accessed 23 July 2019.

¹²²Organisation for Economic Co-operation and Development 'Tax Challenges of Digitalisation the Request for Input - Part II' available at <https://www.oecd.org/tax/beps/tax-challenges-digitalisation-part-2-comments-on-request-for-input-2017.pdf> accessed 23 July 2019.

within any tax system.¹²³ Therefore, if the government of eSwatini continues, to allow, unregulated Cryptocurrencies to operate concurrent to regulated fiat currency this will place a threat to the sustenance of the existing tax system¹²⁴ in the long term. Therefore, the imposition of timeous regulation by the eSwatini Revenue Authority is an important consideration.¹²⁵

2.10 Conclusion

In the wake of the development of virtual assets such as Bitcoin, it is essential for regulators to seek ways to address regulating and taxing Bitcoin, considering the level of anonymity that this Cryptocurrency possesses. In addition, a strengthening aspect of the need for regulations is that Bitcoin does not have a third party regulating body that monitors transactions conducted using this Cryptocurrency. This vulnerability opens up the innovation to a lot of criminal activity which includes tax evasion, international money laundering and drug trafficking.

The application of such regulations should be done in a manner that will seek to welcome innovation in the financial technology market, and to help developing countries like the kingdom of eSwatini to be able to implement favourable regulatory measures to the latest developments in the current evolving global financial markets.

This process will be eased by organizations such as the OECD, which have a mission to aid developing countries in formulating regulations and updating their tax rules to address the adverse effects of the introduction of Cryptocurrency into the virtual financial market. Therefore, to examine the possible reforms that eSwatini can implement to its current tax rules system in relation to virtual currencies, the next chapter will examine the current rules that may possibly apply, should there be a need to tax income that is derived from Cryptocurrency in eSwatini.

¹²³J cook, S Parsons and T Sebeela 'The Regulation of Bitcoin to Address Tax Compliance: International Experience and South African Application' 236, 244 available at https://www.researchgate.net/publication/320245135_The_Regulation_of_Bitcoin_to_Address_Tax_Compliance_International_Experience_and_South_African_Application/link/5c74f8f1458515831f6ffe7c/download accessed 23 July 2019.

¹²⁴Ibid.

¹²⁵Ibid.

CHAPTER 3 ESWATINI TAX IMPLICATIONS

3.1 Introduction

The global spread of Bitcoin in the virtual world and unregulated financial markets has attracted attention in even the less developed countries like the Kingdom of eSwatini, where regardless of the risks associated with Bitcoin, users are fascinated by the efficiency of Bitcoin transactions and the Cryptocurrency's potential to yield high profits.¹²⁶ This growing adoption of Cryptocurrency has left governments and global financial service governing authorities with a dilemma. On the one hand, there is a clear need to embrace the efficiency and innovation associated with the new Cryptocurrency, while on the other hand, Cryptocurrency is posing a threat to fiat currency, a currency that has been traditionally viewed globally as the only usable and legal currency.¹²⁷

Moreover, the Kingdom of eSwatini is also trying to find answers through the CBE on how to regulate this ever-evolving Cryptocurrency, but the ERA is finding it difficult to formulate possible solutions to apply taxes to Cryptocurrency. Therefore, this chapter will briefly explore the reported progress that has been made by the CBE on Cryptocurrency regulations, and we then proceed to explore the tax implications that the current tax regulations would possibly have on Bitcoin in eSwatini.

3.2 Regulation of Bitcoin in ESwatini

In 2018, the CBE made an official statement alerting virtual currency users that only money in note and coin form, issued by the CBE, will be recognised as official legal tender in eSwatini.¹²⁸ The bank further stated that, "there are no restrictions, disclosures or regulatory compliance measures applicable to transactions executed using Bitcoin."¹²⁹ In addition, the bank alerted users that at the present moment, "there is no protection or legal recourse available from any

¹²⁶K Mothokoa *Regulating Crypto-Currencies in South Africa: The need for an effective legal framework to mitigate the associated risks* (Unpublished LLM thesis, University of Pretoria, 2017) 4.

¹²⁷J Hun, Oh K Nguyen 'The Growing Role of Cryptocurrency: What Does It Mean for Central Banks and Governments?' (2018) 25 *International Telecommunications Policy Review* 33, 34 available at https://www.researchgate.net/publication/329023530_The_Growing_Role_of_Cryptocurrency_What_Does_It_Mean_for_Central_Banks_and_Governments/link/5bf0d33c4585150b2bbef9bc/download accessed 6 August 2019.

¹²⁸Central Bank Of Swaziland op cit note 15.

¹²⁹Ibid.

institution, including the Central Bank, in the event that the user suffers financial loss from the use of Bitcoin or any other Cryptocurrency.”¹³⁰

Moreover, the CBE has actively commenced the process of seeking ways to regulate financial technology developments, by monitoring both nationally and internationally emerging technologies. These technologies include Cryptoassets, and to achieve this the bank has established a Financial Technology (FinTech) Unit, to promote the active monitoring of FinTech innovation locally and around the world.¹³¹ This new development follows the recent developments that have been brought about by virtual currencies in neighbouring South Africa, which have not gone unnoticed by users in eSwatini creating the potential growth of Bitcoin transaction activity in eSwatini.

3.3 Bitcoin Activity in eSwatini

There have been no reported Cryptocurrency exchange platforms in the kingdom of eSwatini. This has, however not stifled any remote Cryptocurrency activity transactions. The CBE noted in an alert to users that, “the Bank is aware that Bitcoin is one of the leading Cryptocurrencies globally, and that the bank has been advised of instances where this currency is being marketed and traded in Swaziland.”¹³² This activity noted by the CBE therefore necessitates a closer look at the current laws that may guide the regulation and taxation of Cryptocurrency in the kingdom. Therefore, in examining the laws in eSwatini, it must be noted that the universal characteristics of Bitcoin transactions allow these transactions to occur in eSwatini just like in any other jurisdiction. Therefore, since there are no reported exchange platforms in eSwatini, transactions in Bitcoin in eSwatini have the potential to be conducted in the following ways,

- (i) “Mining through the use of highly sophisticated computer machinery,
- (ii) Acquiring Bitcoin through the exchange of or payment for goods and services rendered,
- (iii) Investors can exchange local currency for a Cryptocurrency (or vice versa) by using Cryptocurrency exchanges.”¹³³

Therefore, having considered that Bitcoin transactions do occur in eSwatini as confirmed by the CBE, the bank has however not confirmed the ways in which the reported transactions noted in the public statement occur. The study now therefore considers using the above three types of transactions as a reference point on the possible tax implications on Bitcoin, with

¹³⁰Central Bank of Swaziland op cit note 15.

¹³¹Central Bank of Swaziland ‘Financial Technology (FINTECH) Unit’ available at <https://www.centralbank.org.sz/fintech/> accessed 7 August 2019.

¹³²Central Bank Of Swaziland op cit note 15.

¹³³Dr F Moosa op cit note 27 at 9.

regard to the current tax legislation in eSwatini, since there has been no pronouncement by the ERA on its position on Cryptocurrency. Furthermore, no case law or tax tribunal ruling has been issued, which makes this study an important contribution to policy.

3.4 Eswatini Revenue Authority and Bitcoin.

The tax collecting body in the kingdom of eSwatini is the ERA,¹³⁴ which recently undertook a major reform of its tax system, motivated by South Africa's improvement of its business tax system.¹³⁵ The reforms have included broadening the tax base to collect more revenue including consumption and Income Taxes through the ERA and further, the standardisation of the revenue service to facilitate more efficiency in collecting taxes.¹³⁶ The changes brought about by eSwatini have seen a major growth in revenue collection, boosting the economy and simplifying the conduct of business in eSwatini for international corporations.¹³⁷

The improvements of the Swati¹³⁸ tax system introduced by the ERA have come with a positive impact, however the continued development of the financial markets in light of emerging financial technologies such as Bitcoin presents the need for further review of the tax legislation within eSwatini. In doing so, it must be noted that eSwatini uses a source based tax system, which means that ERA cannot tax income that is sourced outside the kingdom of eSwatini, unless the income is deemed to be from a source within eSwatini.¹³⁹ Secondly, in collecting tax revenue ERA applies both direct and indirect taxes on revenue collection. Therefore, Collecting Income Tax, which is a direct tax, collected from individual taxpayers and businesses on the profit they make during the year of assessment.¹⁴⁰

Moreover, Value Added Tax is also collected in eSwatini. This is an indirect tax applied on the consumption and the importation of goods, collected by the government at a rate of 15%, enabling the facilitation of a number of services to the Swati nation.¹⁴¹ Therefore, as a point of departure before we examine the Swati tax legislation, it must be noted that to conduct this

¹³⁴Central Bank of Ireland op cit note 19.

¹³⁵M Ayoki 'The Reform of the tax system in Swaziland' (2017) 58 *Institute of Policy Research and Analysis* 1, 2.

¹³⁶Ibid 2.

¹³⁷Ibid 5.

¹³⁸Just an Ordinary Lady 'Speak Siswati like a true Swati' available at <http://lincayam.blogspot.com/p/speak-siswati-like-true-swazi.html> accessed 7 December 2020.

¹³⁹Ibid 5.

¹⁴⁰Eswatini Revenue Authority 'Swaziland VAT' available at <http://www.sra.org.sz/vat/pageview.php?id=79&name=Swaziland%20VAT> accessed 25 September 2019.

¹⁴¹Ibid.

study we will focus only on the direct tax consequences to determine the position of Tax law on Bitcoin as a Cryptocurrency in eSwatini.

This study emanates from the fact that in light of the technological advancements and the nature of Cryptocurrency, and the relative inability of the eSwatini revenue authority to levy taxes on worldwide income, a need arises to shed light on the possible tax consequences on Bitcoin in the kingdom of eSwatini. This will enable us to identify the weaknesses of the eSwatini tax system and then make recommendations to add to policy. This will be done by examining the provisions of the Income Tax Order, King's Order in Council No. 21 of 1975¹⁴² (as amended), which is the official Swati legislation that governs the taxation of income obtained from a source or a source deemed to be within the kingdom of eSwatini.¹⁴³

3.5 Bitcoin and the ESwatini Income Tax Order of 1975.

The collection of Income Tax in eSwatini is conducted in five main ways. The first is pay as you earn tax (PAYE) where deductions are made from employees' salaries by employers who then make a monthly remittance to the ERA.¹⁴⁴ In addition to this, provisional and corporate Income Tax is collected from businesses and companies annually. This includes self-employed individual Income Tax payers. These may be suitable taxes which may be applied to Bitcoin merchants.¹⁴⁵ In addition, the revenue service also collects withholding taxes, which are taxes applied at the source, where a third party may be tasked with the responsibility of making deductions on taxes from specific forms of payments and making a remittance to ERA.

Lastly, tax may be collected through graded tax, a levy payable only by adults in eSwatini.¹⁴⁶ However, it must be noted that the eSwatini tax system does not have Capital Gains Tax (CGT) legislation, and as a result, there is no CGT.¹⁴⁷ This therefore, leaves a gap with regard to the disposal of capital assets where gains or losses have occurred which may be through investments that are made using Bitcoin. In addition, with the different methods of applying taxes in eSwatini there have been very few reported disputes for determination by the courts of

¹⁴²Income Tax Order 1975 Kings Order in Council Act No. 21 of 1975.

¹⁴³Swaziland Tax Guide 2016/17 'PKF World Wide Tax Guide 2016/17' 1, 4 available at <https://www.pkf.com/media/10028478/swaziland-tax-guide-2016-17.pdf> accessed 8 August 2019.

¹⁴⁴Eswatini Revenue Authority 'Swaziland Income Tax' available at <http://www.sra.org.sz/incometax/pageview.php?id=68&name=Swaziland%20Income%20Tax> accessed 26 September 2019.

¹⁴⁵Ibid.

¹⁴⁶Ibid.

¹⁴⁷KPMG Swaziland fiscal Guide 2017/18 'Tax' 1,1 available at https://home.kpmg/content/dam/kpmg/za/pdf/2017/12/Swaziland%20Fiscal%20Guide%202017_18.pdf accessed 16 July 2019.

eSwatini, resulting in many provisions of the tax legislation in the kingdom of eSwatini remaining uninterpreted by case law. However, an exploration of the historical perspective of the development of laws in eSwatini will be useful in establishing ways of interpreting the provisions of the Income Tax Order of 1975 in relation to Bitcoin.

3.6 Interpretation of the ESwatini Income Tax Order of 1975.

A legal system known as the Roman-Dutch Law was integrated into some parts of Africa during the beginning of the colonisation period commonly known as the scramble for Africa.¹⁴⁸ During this time, the Dutch settlers used their native Roman-Dutch law in the Cape Colony, which spread from the Cape to the inner parts of Southern Africa. These laws ‘took the form of Ordinances, Orders in Council, Edicts and proclamations’.¹⁴⁹ An example of an Order in Council that is relevant to this research is the Income Tax Order Kings Order in Council No. 21 of 1975 of eSwatini. Administration of these laws was conducted under the Afrikaner regime in the Transvaal in South Africa, extending to eSwatini, formerly known as Swaziland, as well as Lesotho and Botswana during the colonial era.¹⁵⁰

In 1903, the position changed after the British won the Anglo-Boer war, and took over the Transvaal, with eSwatini remaining ‘under the Transvaal administration but only with a shift from the upper hand of the Afrikaner to the lesser grip of the British’.¹⁵¹ The British in addition passed the General Law and Administration Proclamation No. 4 of 1907 section 3, which read:

“(1) The Roman Dutch common law, save in so far as the same has been here before or may from time to time hereafter be modified by statute, shall be the law in Swaziland;

(2) Save and except in so far the same have been repealed or amended the statutes in force in the Transvaal on the fifteenth day of October 1904 and the statutory regulations thereunder shall **mutatis mutandis** and as far as they may be applicable be in force in Swaziland...”¹⁵²

A significant highlight from the above provisions is that since their promulgation the above provisions have continued to apply up to the present time not only in eSwatini, but also in the Southern African region including Lesotho, Botswana and South Africa, following the British

¹⁴⁸*Umcebo Mining (Pty) Limited v USA Distillers (Pty) Limited* (1890/2012) [2017] SZHC 202 (6th October 2017) par 8.

¹⁴⁹*Ibid* par 8.

¹⁵⁰*Ibid* par 8.

¹⁵¹*Ibid* par 9.

¹⁵²*Ibid* par 9.

expansion in the region. More recently, the Constitution of the Kingdom of Swaziland Act, 2005¹⁵³ section 252 (1) recognised the provisions, stating:

“Subject to the provisions of this Constitution or any other written law, the principles and rules that formed, immediately before the 6th September, 1968 (Independence Day), the principles and rules of the Roman Dutch Common Law as applicable to Swaziland since 22nd February 1907 are confirmed and shall be applied and enforced as the common law of Swaziland.....”

The above provisions provide a sense of clarity that the development of the law in the Southern African region has been largely influenced by the Roman-Dutch and English common law in Botswana, South Africa, Lesotho and eSwatini.¹⁵⁴ In addition, the continued reception of these laws, as evident from the constitution of eSwatini explains why the courts in eSwatini have been habitually following the decisions of the courts in South Africa.¹⁵⁵ Moreover, since the gaining of independence and the repealing of the 1973 constitution in eSwatini there have been no laws, which would suggest that eSwatini abolished the usage of Roman-Dutch and English common law.¹⁵⁶ This strengthens the view that the common law is still applicable in eSwatini where current legislation and decided cases fall short.

Therefore, having explored the historical perspective and the development of laws in eSwatini it must be noted that many writers and courts in eSwatini espouse the view that South African case law is of a strong persuasive value to the Swati court’s interpretation of legislative provisions, in a case where there is no interpretative case law in eSwatini. Therefore, in interpreting the application of the provisions of the Income Tax Order on Bitcoin the use of South African tax law precedent will be used as a persuasive source for the eSwatini Income Tax Order 1975.

3.7 Income tax in eSwatini.

In eSwatini Income Tax is levied on both natural persons and juristic persons on income generated from a source within or deemed to be within the kingdom of eSwatini.¹⁵⁷ Therefore, for the collection of revenue, reference is made to section 6 (1) of the Income Tax Order of

¹⁵³Constitution of the Kingdom of Swaziland Act 2005 (2005 Constitution).

¹⁵⁴JH pain ‘The reception of English and Roman Dutch law in Africa with reference to Botswana, Lesotho and Swaziland’ (1978) 11 *The Comparative and International Law Journal of Southern Africa* 137, 167 available at https://www.jstor.org/stable/23245418?seq=1#metadata_info_tab_contents accessed 30 September 2019.

¹⁵⁵Ibid.

¹⁵⁶Ibid.

¹⁵⁷KPMG op cit 147.

1975 which states that “an amount shall be levied and paid as Income Tax also known as normal tax, received by or accrued to or in favour of any person in a year of assessment.”¹⁵⁸ Income Tax is thus payable by a person after all allowable deductions have been made from the said amount, which then leaves the taxpayer with what is known as ‘Taxable Income.’¹⁵⁹

Therefore, to determine the Income Tax payable by a taxpayer we refer to the Gross Income definition, which is defined by section 7 of the Income Tax Order 1975 as

“ the total amount whether in cash or otherwise received by or accrued to or in favour of any person, excluding such receipts or accruals of a capital nature in any year or period assessable under this Part from any source within Swaziland or deemed to be within Swaziland.” ¹⁶⁰

In assessing the applicability of the components of the Gross Income definition to Bitcoin, we will consider them separately as follows.

3.7.1 The Total amount

In determining whether Bitcoin may be regarded as an amount to fit into the gross income definition for the payment of taxes reference is made to the case of *WH Lategan v Commissioner for Inland Revenue*,¹⁶¹ where the court held that an amount does not need only to include money in the form of hard cash, “but the value of every form of property earned by the taxpayer, whether corporeal or incorporeal, which has a money value”. The term incorporeal implies an intangible asset such as a right.¹⁶² An example of an incorporeal form of property in our case is Bitcoin since it exists only on the internet and attracts ownership rights to property such as Bitcoin which can be valued as an amount. Therefore, intangible assets such as Bitcoin attract rights known as rights *in rem* or *jus in rem* which shields an individual’s assets from interference by anyone, either juristic or natural person.¹⁶³ In the case of *Commissioner for Inland Revenue v People’s Stores (Walvis Bay) (Pty) Ltd* ¹⁶⁴ the court stated that what was “required for an accrual in terms of the definition of ‘gross income’ was that the person concerned must have become entitled to the amount in question, or to a right

¹⁵⁸Income Tax Order 1975.

¹⁵⁹Income Tax Order 1975.

¹⁶⁰Income Tax Order 1975.

¹⁶¹*WH Lategan v Commissioner for Inland Revenue* (1926), CPD 203; 2 SATC 16, 19.

¹⁶²CFI ‘What are intangible Assets’ available at

<https://corporatefinanceinstitute.com/resources/knowledge/accounting/intangible-assets/> accessed 7 December 2020.

¹⁶³Toppr ‘Rights available to parties’ available at <https://www.toppr.com/guides/business-laws-cs/indian-contract-act-1872/rights-available-to-parties/> accessed 4 December 2019.

¹⁶⁴*Commissioner for Inland Revenue v People’s Stores (Walvis Bay) (Pty) Ltd* 52 SATC 9, 20.

capable of being valued in money.” Therefore, in this case Bitcoin being an intangible asset, a type of asset existing online, it is argued that the right of ownership to this property can be categorized as an amount that can be valued in monetary terms. This amount may then fit into the gross income definition for Income Tax purposes in eSwatini. Having settled that Bitcoin is an amount in terms of the gross income definition, we move on to the next component which is the amount must be in cash or otherwise.

3.7.2 In cash or otherwise

Bitcoin in eSwatini will be taxable in the event the requirement that the ‘total amount must be in cash or otherwise’¹⁶⁵ is met, which essentially entails that there must be an amount that must be in cash or some other consideration such as an ‘in kind’ payment.¹⁶⁶ This means that the term in ‘cash or otherwise’ does not only imply payment in monetary terms but also other valuable forms of payment can be made.¹⁶⁷ Examples of such may be the use of Bitcoin to conclude a payment transaction. Therefore, if Bitcoin is paid to the taxpayer, since it is not regarded as a legal tender in eSwatini for the payment of taxes, the currency may therefore be considered an ‘otherwise’ form of payment that has an equal value to real money.¹⁶⁸

Furthermore, to determine whether Bitcoin can be regarded as an otherwise amount, the study refers to the principle set out in the South African case of *Commissioner for Inland Revenue v Delfos*¹⁶⁹ where the court held that “tax is to be assessed in money on all receipts or accruals having money value. Thus if it is something which is not money’s worth or cannot be turned into money, it is not regarded as income.” It is therefore clear that the characteristics of Bitcoin meet the requirements of this component and Bitcoin has money value and can be turned into cash in line with the meaning of gross income. Bitcoin is therefore an amount not in cash but an “otherwise” amount.

It must further be noted that while Bitcoin only exists in the virtual world and can be regarded as an otherwise amount, one Bitcoin is far more valuable than one Lilangeni.¹⁷⁰ In terms of the Coinbase price index, on the 20th of August 2019 at 12:30 GMT +2 one Bitcoin was valued at R164, 892, 06, South African Rands,¹⁷¹ an amount that is equivalent to the Swati Lilangeni.

¹⁶⁵M Stighlingh et al *Silke: South African Income Tax* (2018) 35.

¹⁶⁶*Commissioner for Inland Revenue v Butcher Bros (Pty) Ltd* 13 SATC 21, 34.

¹⁶⁷M Stighlingh et al op cit note 165.

¹⁶⁸*Butcher Bros (Pty) Ltd Supra* note 166 at 34.

¹⁶⁹*Commissioner for Inland Revenue v Delfos* 1933 AD 242; 6 SATC 92, 99.

¹⁷⁰OS Belomytseva op cit note 65 at 34.

¹⁷¹CoinDesk ‘Bitcoin Price (BTC)’ available at <https://www.coindesk.com/price/bitcoin> accessed 20 August 2019.

The value of the amount attached to Bitcoin by Coinbase can therefore be classified as its ‘in kind’ or ‘otherwise’ value, which enables the Bitcoin amount to fit into the gross income definition as explained above. Furthermore, the ‘otherwise’ Bitcoin amount must be “received by or accrued to” the taxpayer in order to fall in the gross income definition.

3.7.3 Received or Accrued

The amount “in cash or otherwise” which in this case is an ‘otherwise’ amount in the form of Bitcoin must have been “received by or accrued to” the taxpayer or Bitcoin user “during the year of assessment” to be regarded as part of a user’s gross income in that year of assessment.¹⁷² This essentially means that the amount received in Bitcoin must be received or accrued on the user’s behalf for the user’s own benefit.¹⁷³ In addition, what must be noted is that the individual must not necessarily have been entitled to the Bitcoin amount, however once they receive or have the amount accrue to them, the amount is as a result acquired by the user and duly taxable.¹⁷⁴ The receiving or accrual of the Bitcoin as discussed in chapter two will occur when an unidentified sender sends a Bitcoin amount, on the Blockchain, to an unidentified receiver,¹⁷⁵ resulting in the intangible asset being Bitcoin accruing to them for a future payment.

In addition, a highlight about Bitcoin is that the Cryptocurrency’s nature, that of being an intangible asset will most likely result in accruals because it does not exist in physical form for it to be received but accrues online on the user’s wallet and is later converted into money by a Bitcoin User. Therefore, in line with the Income Tax order the Bitcoin amount can accrue to the user by vesting in him a right to a future payment.¹⁷⁶ It is essential to point out that in including the accrued Bitcoin amount in the gross income in the year of assessment, the amount does not need to be due and payable to the Bitcoin user, but can be assessed from a right that has been vested in the user for a future payment in Bitcoin.¹⁷⁷ Therefore, since Bitcoin users can send Bitcoin amounts to other users in the virtual world, this then means they can accrue to a user on their own behalf for their own benefit online, resulting in the Cryptocurrency meeting this requirement. Furthermore, the receipts or accruals must not be of a capital nature which is the next component of the gross income definition that we examine.

¹⁷²M Stighlingh et al op cit note 165 at 35.

¹⁷³*Geldenhuis v Commissioner for Inland Revenue* 1947(3) SA 256 (C); 14 SATC 419, 431.

¹⁷⁴*MP Finance Group CC v Commissioner, SARS* [2007] JOL 20011 (SCA), 6 par 12.

¹⁷⁵Note 76 (See paragraph 2.5)

¹⁷⁶*People’s Stores (Walvis Bay) (Pty) Ltd* supra note 164 at 32.

¹⁷⁷*Ibid* 37.

3.7.4 Excluding Receipts or Accruals of a Capital Nature

In order to fit into the gross income definition, the receipts or accruals from Bitcoin earnings must not be of a capital nature. This essentially entails that the receipts or accruals may either be categorised as capital or revenue in nature and may not be half of either. This principle was confirmed in the South African case of *Pyott Ltd v Commissioner for Inland Revenue*.¹⁷⁸ Therefore, in making a determination of whether the Bitcoin earnings are revenue or capital in nature it is vital to note that “Income is the product or fruit of a person’s labour or capital or both, furthermore it is the proceeds that one receives from the conduct of a business or trade”.¹⁷⁹ Thus, in a case where a person renders services or provides goods in exchange for payment in Bitcoin these amounts will be considered as revenue and may consequently attract Income Tax consequences.¹⁸⁰ The position will be different however in the event that the receipt or accrual is capital in nature. Thus, when an asset is said to be of a capital nature, ‘it is of an enduring benefit to the taxpayer which is used to produce income, and is not consumed in that process, save for normal wear and tear, or is a personal use asset’.¹⁸¹ Receipts or accruals that may be classified as being capital in nature from Bitcoin transactions can include Bitcoin capital that is invested to produce interest from online Bitcoin investments.

Therefore, to properly classify whether Bitcoin receipts or accruals are capital in nature this will depend on the intention¹⁸² of the Bitcoin user when they acquire and dispose of their intangible assets in the form of Bitcoin. Thus if a Bitcoin merchant acquires Bitcoin with the motive of making a profit, the proceeds will be revenue in nature.¹⁸³ The position alters if the Bitcoin user or taxpayer receives the Bitcoin and keeps it not to re sell it at a profit but to use it in producing more income, an example being the gaining of interest through the investing of such Bitcoin.¹⁸⁴ The eventual disposal of such Bitcoin will then be regarded as being capital in nature and may consequently not be included in the gross income definition.¹⁸⁵ However, it

¹⁷⁸*Pyott Ltd v Commissioner for Inland Revenue* 1945 AD 128 13 SATC 121 (A), 126.

¹⁷⁹*Butcher Bros (Pty) Ltd Supra* note 166 at 34.

¹⁸⁰TLC Maliti *An analysis of the approach of the courts in determining the capital and revenue nature of income and expenditure* (unpublished Mcom thesis, University of Durban-Westville 2002) 11.

¹⁸¹*Butcher Bros (Pty) Ltd Supra* note 166 at 34.

¹⁸²*Commissioner for Inland Revenue v Visser* 1937 TPD 77; 8 SATC 271, 276. “The most important test used by the courts in deciding whether a receipt in respect of the disposal of an asset is income or capital in nature is the intention of the taxpayer. Generally, the proceeds will be income in nature if the asset was acquired with the purpose of selling it at a profit. However, if the asset itself was acquired and held, not for the purpose of resale at a profit, but to produce income from that asset such as rent, interest or dividends, then the proceeds on the disposal of the asset will be capital in nature.”

¹⁸³*Ibid.*

¹⁸⁴*Ibid.*

¹⁸⁵*Ibid.*

must further be noted that eSwatini does not have capital gains tax,¹⁸⁶ therefore gains or losses that are made from the disposal of capital assets in eSwatini cannot attract capital gains tax consequences. Furthermore, the Bitcoin amount must be from a source within the kingdom of eSwatini in order to fit into the gross income definition and be subject to Income Tax.

3.7.5 From a Source within eSwatini

Bitcoin amounts that have been received or have accrued to the user must be sourced from within eSwatini or deemed to be sourced within eSwatini.¹⁸⁷ This requirement must be fulfilled because eSwatini has a ‘source’ based tax regime. Source based income essentially entails that the user will be taxed where the income originates from a source within the territorial boundaries of eSwatini, regardless of the physical or legal residence of the user who receives the income.¹⁸⁸ There are no decided cases in the determination of source in eSwatini. Therefore to get a clear understanding of the word ‘source’, we rely on the South African case of *Commissioner for Inland Revenue v Lever Bros & Unilever Limited*.¹⁸⁹ In this case, Watermeyer CJ, finding it difficult to interpret the meaning of the word source within the Republic of South Africa stated that “source in relation to receipts and accruals means not the quarter whence they come, but the originating cause of their being received as income.” *Commissioner for Inland Revenue v First National Bank of South Africa Limited*¹⁹⁰ also affirmed this principle.

In essence what must be noted is “that the originating cause is the work which the taxpayer does to earn the income, in our case the work done by the user to obtain Bitcoin earnings. The work may be a business or enterprise or an activity in which the taxpayer engages, whether involving mental or physical exertion, it may also be in the form of employment of capital.”¹⁹¹ In considering the taxability of Bitcoin with regard to the source element, it is important to point out that Bitcoin does not have any central authority and since its release by a person or group of persons into the virtual world as open source software in 2009, using the pseudonym Satoshi Nakamoto, the Cryptocurrency remains with an unknown jurisdiction.¹⁹² Therefore the

¹⁸⁶KPMG op cit note 147 at 1.

¹⁸⁷Income Tax Order 1975.

¹⁸⁸The ‘5th Report – Basing the South African Income Tax System on the Source or Residence Principle - Options and Recommendations’ par 1.2 available at <http://www.treasury.gov.za/publications/other/katz/5.pdf> accessed 10 August 2019.

¹⁸⁹*Commissioner for Inland Revenue v Lever Bros & Unilever Ltd* 1946 AD 441 14 SATC 1, 12.

¹⁹⁰*Commissioner for Inland Revenue v First National Bank of South Africa Limited* (2000) 62 SATC 253, 260.

¹⁹¹RC Williams *Income Tax in South Africa Law and Practice* 4 ed (2006) at 43 and 44.

¹⁹²M Najib, M Imam ‘Bitcoin’ (2019) *Lebanese International University* 1, 3 available at https://www.researchgate.net/publication/332705840_The_history_of_Bitcoin_pdf accessed 13 August 2019.

transactions involving the use of Bitcoin may further help in determining the source of the income from Bitcoin earnings, these may include mining and the earning of Bitcoin in exchange for goods and services.

3.7.5.1 Mining

In determining the source of Bitcoin during the process of mining for Bitcoin in the virtual world, where a user or taxpayer has purchased highly advanced computer software, the location of the mining activity is important in eSwatini.¹⁹³ Therefore, the location of the activity during the mining of Bitcoin where the user is involved in the activity of solving highly complex mathematical puzzles, for which he is awarded with Bitcoins as a reward, is essentially the source according to the eSwatini Income Tax Order.¹⁹⁴ Therefore, the whole process of investing capital and conducting the activity of Bitcoin mining is the originating cause of the Bitcoin that is subsequently paid into the Bitcoin wallet of the user or taxpayer and is as a result taxable. Thus, if such an activity is conducted within the territorial boundaries of eSwatini, then the source becomes eSwatini.

3.7.5.2 Receiving Bitcoin in exchange for goods and services

Moreover, in the event a Bitcoin user receives payment by Bitcoin for goods and services rendered from a user in eSwatini, source in this case may also be established. This is because once mined, and awarded to a user, that user then becomes the rightful owner of Bitcoin, which essentially results in them being liable to pay Income Tax. Thus, in the event a user offers their services in exchange for payment in Bitcoin in eSwatini, reference is made to South African tax court decisions which have followed the view that “the source of income from employment and the rendering of services is the services themselves and that the location of the source is the place where the services were rendered.”¹⁹⁵ Therefore source in the case of rendering services in exchange for Bitcoin is the location where the services were rendered in eSwatini.

There may also be transactions where payment in Bitcoin results from the supply of **moveable goods** in the form of moveable property. In this regard, we consider two requirements, which are:

- i) The employment of the taxpayer’s capital, and

¹⁹³The white paper on ‘How to deal with Bitcoin and other cryptocurrencies in the System of National Accounts?’ (published on COM/SDD/DAF (2018)1 of 9 October 2018) 1, 7 available at [http://www.oecd.org/officialdocuments/publicdisplaydocumentpdf/?cote=COM/SDD/DAF\(2018\)1&docLanguage=En](http://www.oecd.org/officialdocuments/publicdisplaydocumentpdf/?cote=COM/SDD/DAF(2018)1&docLanguage=En) accessed 29 April 2019.

¹⁹⁴Ibid 7.

¹⁹⁵*Income Tax Case 1104* (1967) 29 SATC 46, 50.

ii) The carrying out of his trade.

To establish source both these requirements must be met.¹⁹⁶ Therefore, if a trader employs his capital for the purchase of goods in order to carry out a trade by reselling them for payment in Bitcoin in eSwatini these two requirements must be met to establish source.

In the South African case of *Transvaal Associated Trade and Skin Merchants' v Collector of Income Tax, Botswana*¹⁹⁷ the court held that “when all activities giving rise to the income consist of buying and selling, the country where the sales were made is generally held to be the source of the trading profit”. Therefore, in the case where moveable goods are sold for Bitcoin in eSwatini, then eSwatini may become the source of the Bitcoin earnings for Income Tax purposes. However, the position differs in the case of a sale of immoveable property where the payment during the sale is made using Bitcoin. The principle set out in *Rhodesian Metals Ltd (in liquidation) v Commissioner of Taxes, Southern Rhodesia*¹⁹⁸ suggests that “the place where the capital was employed is regarded as the source, when a sale of immoveable property is made”. This suggests that if the immoveable property is purchased in eSwatini using Bitcoin, then the source of the Bitcoin is from eSwatini. However, the situation differs if the immoveable property is purchased outside eSwatini. Then the source of the Bitcoin will be regarded as being from a location outside eSwatini therefore not taxable. The discussion then leads us to deemed source with regard to some transactions conducted outside of eSwatini which may be deemed to have been conducted within eSwatini.

3.7.6 From a source deemed to be within eSwatini

Eswatini, with a source based tax system, has elected to treat certain amounts from a foreign jurisdiction to be deemed to have been sourced from within the territorial boundaries of eSwatini.¹⁹⁹ The deeming provisions apply not where the service is rendered within eSwatini in carrying on any trade, but where the service is rendered in carrying on in eSwatini of any trade. This essentially implies that the service itself must be from outside eSwatini.²⁰⁰ For example if a Bitcoin trading exchange company ordinarily conducts business in eSwatini, but renders services in Lesotho or Botswana, any Bitcoin amount that is paid for such services will in terms of section 11(1) be deemed to be from eSwatini.

¹⁹⁶RC Williams op cit note 191 at 45.

¹⁹⁷*Transvaal Associated Hide and Skin Merchants v Collector of Income Tax Botswana* 29 SATC 97 1967(BCA), 104.

¹⁹⁸*Rhodesian Metals Ltd (in liquidation) v Commissioner of Taxes, Southern Rhodesia* 9 SATC 363, 371.

¹⁹⁹Dr F Moosa op cit note 27 at 11.

²⁰⁰RC Williams *Income Tax in South Africa Law and Practice* 2nd ed (1996), 39.

Section 11(1) of the eSwatini Income Tax Order of 1975 states that

‘An amount shall be deemed to have accrued to any person from a source in Swaziland notwithstanding that it may have been recovered or recouped outside Swaziland whenever it has been received by or has accrued to or in favour of such person’²⁰¹

Section 11 in subparagraph (a) and (b) of subsection (1) provides for the payment for goods²⁰² and services²⁰³ that have been supplied in or outside eSwatini and payment accrues from a source outside eSwatini, if the payment is made using Bitcoin then the user will attract Income Tax consequences in the Kingdom of eSwatini. The principle in this provision is derived from the common law principle that if a taxpayer carries on business in a particular jurisdiction²⁰⁴ the income derived from the transactions in the course of that business irrespective of whether the work was done within or outside, in our case eSwatini, is deemed to be from a source within eSwatini.²⁰⁵

To determine the link between the payment and services rendered reference is made to the South African *Income Tax Case 749*.²⁰⁶ In this case, the court held that

“There must be some close link between the work done outside the union and the carrying on of a trade within the union. A link closer than the mere fact that the taxpayer is carrying on a trade in the union and that the work done outside the union is in the way of such trade or of the same nature as the work done by the a taxpayer in the union.”

An example of the principle illustrated in *Income Tax Case 749* is that if an individual carries on a trade in eSwatini the fees or payment earned in the form of Bitcoin must be because of the individual’s carrying on of a trade in eSwatini that he has earned the fees.²⁰⁷ Therefore, in illustrating this point, if for example **company A** from eSwatini offers construction services in Zimbabwe and is paid using Bitcoin, the payment from Zimbabwe will be deemed to be from eSwatini. This is because **company A** is in the business of carrying on the trade of construction in eSwatini and which has had the result of attracting business to which services had to be rendered in Zimbabwe which then results in the earning of fees in the form of Bitcoin by **company A** in Zimbabwe.

²⁰¹Income Tax Order 1975.

²⁰²Income Tax Order 1975.

²⁰³Ibid.

²⁰⁴RC Williams op cit note 191 at 42.

²⁰⁵Ibid.

²⁰⁶*Income Tax Case No 749* (1952) 18 SATC 319 (T), 322.

²⁰⁷RC Williams op cit note 191 at 43.

The above point was further illustrated in *Income Tax Case 56*²⁰⁸ where the court held that fees that were paid for a project done in Lourenco Marques in Maputo were deemed to have their source within the South African Republic. This was because although the work was done and paid for outside South Africa, the taxpayer had been approached because he was an accountant of high standing in Johannesburg. In other words it was in respect of his carrying on of the business of an accountant in Johannesburg that the fees were earned. It must however be noted that a different conclusion is arrived at in the event a business has establishments in two different jurisdictions and has received payment by Bitcoin. This contention is supported by Silke²⁰⁹ who is of the view that if the business of the company is conducted in more than one town with different branches then the position will be different.

The difference in the position emanates from the fact that if a country carries on business in another country, this results in that country having branches in different countries commonly referred to as permanent establishments.²¹⁰ The branches attract tax payer status in the foreign countries and may thus be required to pay their Income Tax earned from Bitcoin taxable income in that country which gives rise to double taxation²¹¹ consequences.²¹² This may occur where **company A** may attract Income Tax consequences on its income from its branch in **country B** on income that it has derived **country B**. However this problem may be neutralised by the use of double tax treaties where most likely taxing rights may be allocated to the country where the business is conducted by the branch in this case **country B**.²¹³ In addition where the two jurisdictions have a right to apply taxes to the branch on its taxable income, “the country of residence will likely grant a foreign tax credit to eliminate any potential double taxation.”²¹⁴

A highlight that has been noted from the Income Tax Order is that the order does not provide for Capital Gains Tax therefore amounts that have been earned through the disposal of capital assets may not be taxable. This then implies that gains that have been accumulated or losses that have been incurred through interest gained from investments through Bitcoin may not be

²⁰⁸*Income Tax Case No 56* (1926) 2 SATC 178 (U), 180.

²⁰⁹RC Williams *Income Tax in South Africa Law and Practice* 2nd ed (1996). See also M Stighlingh et al *Silke: South African Income Tax* (1989) 40.

²¹⁰PKF South Africa ‘Tax Implications for International Branches’ available at <http://www.pkf.co.za/news/2016/tax-implications-for-international-branches/> accessed 22 November 2019.

²¹¹“Double taxation is a tax principle referring to income taxes paid twice on the same source of income. It can occur when income is taxed at both the corporate level and personal level. Double taxation also occurs in international trade or investment when the same income is taxed in two different countries”.Source Julia Kagan ‘Double Taxation’ available at https://www.investopedia.com/terms/d/double_taxation.asp accessed 23 November 2019.

²¹²PKF South Africa op cit note 210.

²¹³*Ibid.*

²¹⁴*Ibid.*

taxable in eSwatini. Therefore, in determining Taxable Income and having considered the Income tax consequences in eSwatini that Bitcoin transactions may incur the study now considers the deductions when determining taxable income.

From the above discussion it is therefore clear that Bitcoin is taxable in the Kingdom of eSwatini and is therefore an amount. Furthermore, in as much as it exists in the virtual world the amount possesses the features of an intangible, incorporeal asset that can be valued in money which tends to attract Income Tax consequences. In addition, it has been uncovered that just like money Bitcoin transactions can be conducted in various ways that may either render the Bitcoin as being of a capital nature or of a revenue nature, to which, to fit into the gross income definition only Bitcoin amounts, of a revenue nature may qualify. A further characteristic that must be noted is that like any other form of income the Bitcoin amount must be from a source within or deemed to be within the kingdom of eSwatini in order to fit into the gross income definition. Lastly, in the event Bitcoin attracts normal tax consequences, these must be done in the year of assessment, which is the year or period in which tax may be charged by the tax authority in our case eSwatini revenue authority. Moreover, in order to determine taxable income, allowable deductions of expenditure and losses will have to be determined which is the next section we examine.

3.8 Deductions

In the determination of taxable income of a taxpayer or Bitcoin user in eSwatini the taxable amount will be the amount that remains after deducting all allowable deductions and deductions from the Bitcoin value earnings.²¹⁵ The Income Tax Order makes provision for the deduction of certain amounts that are incurred by a taxpayer when producing income, in terms of section 14 (1) (a) of the Income Tax Order of 1975,²¹⁶ which provides that

‘For ascertaining the taxable income of any person there shall be deducted from the income of such person –

expenditure and losses actually incurred in Swaziland by the taxpayer in the production of his income, including such expenses incurred outside Swaziland in the production of the taxable income as the Commissioner may allow, provided that such expenditure or losses are not of a capital nature’²¹⁷

²¹⁵M Stighlingh et al *Silke: South African Income Tax* (2017) 114.

²¹⁶Income Tax Order 1975.

²¹⁷*Ibid.*

A significant highlight about the Order is that it makes provision for deductions of expenditure and losses incurred in the ‘production of income’. It must further be noted that the Income Tax Order, unlike the South African Income Tax Act, does not stipulate that the production of income must be in the carrying on of a trade but merely states that it must be in the production of income. Thus, for Bitcoin users this may be expenses or losses incurred in conducting activities related to the provision of goods or services in and outside the kingdom of eSwatini. This may include actions which are causally connected to the payment that is consequently made via Bitcoin.²¹⁸ This may also include expenditure and losses that are incurred in the mining of Bitcoin.

3.8.1 In the production of income

During the production of income, income that is derived from Bitcoin earnings through mining may be regarded as being from a source within the kingdom of eSwatini and may be deductible. In addition, the expenditure or losses that are incurred when producing such income in order to be deductible must be of a ‘recurring nature.’²¹⁹ These may include internet charges and electricity payments. However, the purchase of expensive computer systems to facilitate Bitcoin mining may therefore not be deductible when determining Taxable Income from Bitcoin earnings because it is ‘final expenditure’ and is of a capital nature.²²⁰ Furthermore, in the event that a Bitcoin user or individual renders services or provides goods in exchange for Bitcoin, losses and expenditure incurred by the individual during such a transaction may be deducted in determining taxable income because they are causally connected to the income earning activity.²²¹

3.8.2 Not of a Capital Nature.

The expenses or losses that are incurred by the taxpayer using Bitcoin in the production of income must furthermore not be of a capital nature. In essence, the deductions must not be for wealth that has been used by the Bitcoin merchant for the purpose of producing fresh wealth.²²² This includes wealth used for the purchasing of highly advanced computer systems in order to facilitate the production of new Bitcoins through mining. An illustration of expenditure incurred when producing income is found in the case of *Commissioner for Inland Revenue*

²¹⁸*Port Elizabeth Electric Tramway Company Ltd v Commissioner for Inland Revenue*, 1936 CPD 241, 8 SATC 13, 20.

²¹⁹*Commissioner for Inland Revenue v Jacobsohn* (1923) CPD 221, 232.

²²⁰*Ibid.*

²²¹*Income Tax Case 1104* supra note 195.

²²²*Commissioner of Taxes v Booysen* 1918 AD, 582.

*Appellant v George Forest Timber Co.*²²³ where the court held that, “money spent in creating or acquiring an income-producing concern must be capital expenditure, it is invested to yield future profit and while the outlay does not recur the income does. Stating that, there is a great difference between money spent in creating or acquiring a source of profit and money spent in working it. Thus the former is capital and the latter is not.” This principle therefore illustrates that there is a difference between the expenses or losses that may be incurred in setting up the Bitcoin trading activity and expenses or loss that are incurred whilst running the operations of a Bitcoin trading activity.

Therefore, having considered the deductions that are determined in determining taxable income a significant highlight is that the provisions of the eSwatini Income Tax Order do not provide for deductions made in the carrying on of any trade but simply state that the income must be in the production of income. This position differs from that of the South African Income Tax Act which we will consider in the next chapter which provides that the taxpayer must have been carrying on a trade.

3.9 Conclusion

From this chapter we have determined that the CBE has not made a final determination on the regulatory implications of Bitcoin in eSwatini, and as such, the bank has kept a very cautious approach on the development of regulations that may best suit Cryptocurrencies such as Bitcoin in eSwatini. Furthermore, the eSwatini revenue authority has not made a determination or pronouncement on the application of tax on Bitcoin and other Cryptocurrencies. However, the revenue authority is still monitoring the development of the Cryptocurrency in order to make laws that will best suit the developing nature of Bitcoin.

Furthermore, it is important to highlight that in conducting this study we have used South African case law in determining the provisions of the Income Tax Order 1975 of eSwatini, which is to a greater extent similarly worded to that of the South African Income Tax Act. Moreover, in determining the taxability of Bitcoin in light of the Income Tax Order it is evident from the interpretation of the gross income definition components, that Bitcoin is taxable in the Kingdom of eSwatini. This is the case regardless of the factors such as that eSwatini has a tax regime that is source based and the fact that Bitcoin has no jurisdiction governing it as a currency.

²²³*Commissioner for Inland Revenue Appellant v George Forest Timber Co Ltd Respondent* 1924 AD 516, 526.

However, it must be noted that there is still a gap that still needs to be addressed by the eSwatini revenue authority in terms of assessing worldwide income. This is because in as much as eSwatini can tax income that is from a source deemed to be from eSwatini some transactions that are conducted outside eSwatini cannot be taxed. This may include transactions where there may be no link of any carrying on of any trade in eSwatini, with transactions that are conducted outside of eSwatini. However, in the South African jurisdiction the case is different and the South African Income Tax Act provides for the taxing of amounts that are conducted from anywhere in the world. Furthermore, the Income Tax Order in eSwatini does not provide for Capital Gains Tax which also leaves a gap in the taxing of gains or losses from the disposal of capital assets thus Bitcoin investments may not be taxable under the Income Tax Order. We therefore in the next chapter consider the South African jurisdiction on the regulation and the tax implications of Bitcoin in a bid to fill the gaps that are in the Income Tax Order.

CHAPTER 4 GUIDANCE FROM SOUTH AFRICA'S POSITION ON THE REGULATION AND TAX TREATMENT OF CRYPTOASSETS.

4.1 Introduction

Since the first release of Bitcoin into the virtual, open market through open source software by Satoshi Nakamoto in 2009, South Africans did not have much of an interest in the Cryptocurrency and focused on other forms of less popular financial technologies to earn profits.²²⁴ However, the rapid adoption and growth of Bitcoin globally attracted a significant growth of interest amongst the locals for Cryptocurrency during 2017. During that year internet search engines like Google recorded an all-time high of search inquiries about Bitcoin compared to any other country.²²⁵ This popularity attracted by the Cryptocurrency proves that an integration and injection of Bitcoin has the potential to greatly improve financial technology amongst banking institutions “including financial inclusion and enhancing the value of financial services to society.”²²⁶

Moreover, the financial environment fostering the growth of the Cryptocurrency in South Africa has also been very lively and has had rapid growth.²²⁷ The Bitcoin support system has been classified into three parts that help foster the growth of the Cryptocurrency and these include:

- i) Vendors that accept Bitcoin payments for goods and services.
- ii) Bitcoin Miners
- iii) Bitcoin exchange Platforms.²²⁸

Bitcoin transactions rely mainly on these activities for their growth in South Africa and other jurisdictions mainly because of the Cryptocurrency's universal attribute. The growth of

²²⁴I Ventures N Bekker 'South Africans, Cryptocurrencies and Taxation' *Research Report May 2018* 1, 4 available at <http://blockchainacademy.co.za/wp-content/uploads/2018/09/SA-Cryptocurrencies-Research-Report.pdf> accessed 18 June 2019.

²²⁵Ibid 4.

²²⁶National Treasury Department, Financial Sector Conduct Authority 'Matrix: Comments submitted on the South African Retail banking diagnostic' (2018) 1, 38 available at <http://www.treasury.gov.za/publications/other/Comments%20matrix%20for%20retail%20banking%20diagnostic%20Final.pdf> accessed 16 September 2019.

²²⁷R Grinberg 'Bitcoin: An Innovative Alternative Digital Currency' (2012) 4 *Hastings Science & Technology Law Journal* 151, 165.

²²⁸M K-Meng Ly op cit note 1 at 591.

Bitcoin's use and its adoption has also seen the need for financial regulations and tax regulations, which SARB and SARS are actively in the process of addressing.

4.2 Bitcoin and financial regulation in South Africa

In the Republic of South Africa, the SARB “defines Cryptocurrencies, typified by Bitcoin, as an internet-based digital currency that exists almost wholly in the virtual realm.”²²⁹ The SARB has not proclaimed any ‘secondary or primary legislation’ pertaining to the regulation of Bitcoin.²³⁰ This position by the SARB therefore renders Cryptocurrencies such as Bitcoin immune from consumer protection laws and unregulated.²³¹ In 2014 with the support of the SARB, the FIC, the SARS and the FSB, the NT warned Bitcoin and other Cryptocurrency users by issuing an alert pertaining the non-regulation of the Cryptocurrency.²³² This user alert warned the public that “there are no specific laws or regulations that address the use of virtual currencies, and therefore users would have no remedy in law, to aid them in cases where there would be unfair trading practices.”²³³ In essence making it clear that “people who transact with Cryptocurrencies do so at their own risk with no recourse to the SARB”.²³⁴

The SARB later issued a position paper stating

“That given the current landscape and information available, virtual currencies pose no significant risk to financial stability and price stability on the National payment systems.²³⁵ However, individuals or businesses involved in the virtual currencies ecosystem are cautioned that any activities, performed or undertaken with virtual currencies are at their sole and independent risk.²³⁶ The South African Reserve Bank reiterated its position stating that regulation should follow innovation, but that it continues monitoring developments in this regard and reserves the right to change its position should the landscape warrant regulatory intervention.”²³⁷

²²⁹South African Revenue Services op cit note 25.

²³⁰A Nieman ‘A South African cents worth on Bitcoin’ (2015) 18 *Potchefstroom Electronic Law Journal* 1979, 1988.

²³¹E Reddy, V Lawack op cit note 32 at 18.

²³²South African Department of National Treasury ‘User Alert: Monitoring of Virtual Currencies’ available at http://www.treasury.gov.za/comm_media/press/2014/2014091801%20-%20User%20Alert%20Virtual%20currencies.pdf accessed 15 July 2019.

²³³Ibid.

²³⁴E Reddy, V Lawack op cit note 32 at 18.

²³⁵The *Position Paper on Electronic Money* (published on Position Paper number 02/2014 of 3 December 2014) available at [https://www.resbank.co.za/RegulationAndSupervision/NationalPaymentSystem\(NPS\)/Legal/Documents/Position%20Paper/Virtual%20Currencies%20Position%20Paper%20%20Final_02of2014.pdf](https://www.resbank.co.za/RegulationAndSupervision/NationalPaymentSystem(NPS)/Legal/Documents/Position%20Paper/Virtual%20Currencies%20Position%20Paper%20%20Final_02of2014.pdf) accessed 15 July 2019.

²³⁶Ibid.

²³⁷Ibid.

The South African government, in a bid to find solutions on how to regulate Bitcoin and other Cryptoassets formed the IFWG, made up of the NT, SARB, SARS, FSCA and FIC. The group has been tasked with the mission of fostering knowledge amongst the stakeholders placing them in line with the developments of Fintech, examples being Cryptocurrency developments. This group is meant to better guide the formulation of policy and regulation of new and developing Fintech instruments.²³⁸

Therefore, in conjunction with SARS, the IFWG formed a joint working group under its auspices to focus on Cryptocurrencies and their development in 2018 known as the Cryptoassets Regulatory Working Group.²³⁹ However, on the regulation of Cryptocurrency, the representatives have frowned upon assigning new ‘definitions and regulations’ on the technology as it is still developing. They noted that making regulations at an early stage poses the risk of regulations becoming outdated due to the evolving nature of Cryptocurrencies.²⁴⁰ However in 2019 the IFWG through a Consultation Paper on Policy Proposals for Crypto Assets suggested a three phased proposal with which Cryptocurrencies can be regulated, which include:

1. “Phase one: Registration process for crypto asset service providers.
2. Phase two: Review of existing regulatory frameworks followed by new regulatory requirements or amendments to existing regulations.
3. Phase three: Assessment of regulatory actions implemented.”²⁴¹

Therefore when registering, Cryptocurrency service providers will be listed as “accountable institutions under the FIC.”²⁴² In addition, during the workshops to find possible answers on how to regulate Cryptocurrency, the delegates noted that two options were at their disposal in terms of how to formulate the regulations for Cryptocurrencies, which include:

²³⁸The ‘Crypto Assets Regulatory Working Group’ *Consultation Paper on Policy Proposals for Crypto Assets* (2018) 1, 4 available at http://www.treasury.gov.za/comm_media/press/2019/CAR%20WG%20Consultation%20paper%20on%20crypto%20assets_final.pdf accessed 12 July 2019.

²³⁹*Ibid.*

²⁴⁰Intergovernmental Fintech Working Group ‘Fintech Workshop 19-20 April 2019’ 1, 4 available at <https://www.genesis-analytics.com/uploads/Note-%E2%80%93-Intergovernmental-Fintech-Working-Group-Workshop.pdf> accessed 12 July 2019.

²⁴¹The ‘Crypto Assets Regulatory Working Group’ *Consultation Paper on Policy Proposals for Crypto Assets* (2019) 6 available at <https://www.masthead.co.za/wp-content/uploads/2019/01/CAR-WG-Consultation-paper-on-crypto-assets.pdf> accessed 7 December 2020

²⁴²E Reddy, V Lawack op cit note 32 at 23.

- (1) “To amend existing legislation by changing current definitions to cater for emerging innovation.”²⁴³
- (2) Ensuring that regulation is proportional and appropriate to the risk of the innovation or instrument and that the activity and not the entity is regulated and that regulation is as far as possible technology neutral.”²⁴⁴

Regulation of Cryptocurrencies therefore has many implications, which entail the fact that the laws that are implemented in the regulation of these currencies have to cater for developing technological advancements. An obvious feature about Bitcoin and other Cryptocurrencies is that they exist as an electronic virtual technology, and as technological advancements happen regularly, it is difficult for laws to be made to correctly regulate these currencies. Having considered the regulation of Cryptocurrency, the study will now consider the position adopted by SARS regarding the tax treatment of Bitcoin. Furthermore, an investigation on how SARS has gone about in developing tax legislation for Bitcoin in the South African jurisdiction will be conducted.

4.3 SARS Direct Tax treatment of Bitcoin in South Africa

SARS has taken active steps towards finding effective and comprehensive ways to apply tax on Cryptocurrency transactions in South Africa. These are contained in a media release by SARS dated 6 April 2018. This media release serves as a guide for taxpayers, and has gained recognition from the IFWG “as a positive and effective example of communicating a regulatory position to taxpayers.”²⁴⁵ The SARS media release stated

“The South African Revenue Services (SARS) will continue to apply normal income tax rules to Cryptocurrencies and will expect affected taxpayers to declare Cryptocurrency gains or losses as part of their taxable income. However, as indicated in this media statement, there is an existing tax framework that can guide SARS and affected taxpayers on the tax implications of Cryptocurrencies, making a separate interpretation note unnecessary for now. Cryptocurrencies are not regarded by SARS as a currency for Income Tax purposes or Capital Gains Tax (CGT). Instead, Cryptocurrencies are regarded by SARS as assets of an intangible nature.”²⁴⁶

The important aspect to note from the SARS media release is that it only focuses or gives a guide on the application of tax on Cryptocurrency transactions with a reference point as Bitcoin

²⁴³Ibid.

²⁴⁴Ibid.

²⁴⁵Ibid.

²⁴⁶South African Revenue Services op cit note 25.

and it does not refer to virtual currencies in general.²⁴⁷ Therefore, in determining the taxability of Bitcoin in South Africa it must be pointed out that, the South African tax regime applies tax on a residence basis which also assesses worldwide income, with source-based tax applied on individuals not originally from South Africa but who have their source of income in the territorial boundaries of South Africa.²⁴⁸ This position differs from that of eSwatini where the tax regime is source based, applying tax on income that is acquired from within the territorial boundaries of eSwatini, or which is deemed to be from eSwatini on all residents whether from eSwatini or not.²⁴⁹

Moreover, it must be noted that SARS has decided to use the phrase ‘assets of an intangible nature’ to categorize Cryptocurrencies when implementing taxes. This decision has its basis on two points as pointed out by SARS which are

1. “Cryptocurrencies are not official South African tender; and
2. Cryptocurrencies are not widely used and accepted in South Africa as a medium of payment or exchange.”²⁵⁰

On the media release, SARS further makes provision for gains or losses arising from Cryptocurrency transactions stating that their categorisation can be best arranged according to these three different classes of transactions which have different tax outcomes.²⁵¹

1. “A Cryptocurrency can be acquired through the so-called ‘mining’. The ‘miner’ is rewarded with Cryptocurrency; this gives rise to an accrual or receipt on successful mining of the Cryptocurrency. This means that until the newly acquired Cryptocurrency is sold or exchanged for cash, it is held as trading stock, which can subsequently be realised through either a normal cash transaction or a barter transaction.”²⁵²

²⁴⁷Dr Fareed Moosa op cit note 27 at 5.

²⁴⁸South African Revenue Services ‘Non-Residents’ available at <https://www.sataxguide.co.za/swaziland-taxes-overview/#targetText=Swaziland%20corporate%20tax%20rate%20is%20a%20flat%2030%25.&targetText=The%20Kingdom%20of%20Swaziland%20income,will%20be%20subject%20to%20taxation> accessed 3 October 2019.

²⁴⁹South African Tax Guide ‘Swaziland Taxes Overview’ available at <https://www.sataxguide.co.za/swaziland-taxesoverview/#targetText=Swaziland%20corporate%20tax%20rate%20is%20a%20flat%2030%25.&targetText=The%20Kingdom%20of%20Swaziland%20income,will%20be%20subject%20to%20taxation> accessed 3 October 2019.

²⁵⁰South African Revenue Services op cit note 25.

²⁵¹Ibid.

²⁵²A Straude, A Greef ‘Cryptocurrencies and SARS’ available at <http://www.wylie.co.za/articles/cryptocurrencies-and-sars/> accessed on 15 July 2019.

2. Investors can exchange local currency for a Cryptocurrency (or vice versa) by using Cryptocurrency exchanges, which are essentially markets for Cryptocurrencies or through private transactions.²⁵³
3. Goods or services can be exchanged for Cryptocurrencies. This transaction is regarded as a barter transaction. Therefore, the normal barter transaction rules apply.”²⁵⁴

Therefore, to get a clear understanding of how the SARS media release affects the implementation of tax regulations on Cryptocurrency in the South African jurisdiction, the focus of the study will be based on the three above scenarios that have been highlighted by SARS.

4.4 Direct Income Tax consequences of Bitcoin in South Africa

Income Tax, also referred to as normal tax in the South African jurisdiction, is the tax which an individual taxpayer has to pay on his taxable income during any year of assessment.²⁵⁵ To apply Income Tax on Cryptocurrencies, SARS pointed out in a media release dated 6 April 2018 that it intends to ‘apply normal tax rules’²⁵⁶ to the virtual currency. Therefore in examining the normal tax rules we examine the Gross Income definition entrenched in section 1 of the Income Tax Act 58 of 1962, which states that ²⁵⁷

“In relation to any year or period of assessment,

- (i) In the case of any resident, the total amount, in cash or otherwise, received by or accrued to or in favour of such resident; or,
- (ii) In the case of any person other than a resident, the total amount, in cash or otherwise, received by or accrued to or in favour of such person from a source within or deemed to be within the Republic.”²⁵⁸

SARS’s media release revealed an intention to ‘include every Cryptocurrency received or accrued, of a non-capital nature in the ‘taxable income’²⁵⁹ of a ‘resident’²⁶⁰ and ‘non-resident’

²⁵³Ibid.

²⁵⁴Ibid.

²⁵⁵South African Revenue Services ‘Personal income tax’ available at <https://www.sars.gov.za/TaxTypes/PIT/Pages/default.aspx> accessed 22 August 2019.

²⁵⁶South African Revenue Services op cit note 25.

²⁵⁷Income Tax Act 1962.

²⁵⁸Income Tax Act 1962.

²⁵⁹Ibid.

²⁶⁰Ibid.

taxpayer for any ‘year of assessment,’²⁶¹ based on the fact that it is non-cash property with an objectively determinable monetised value. It must further be noted that like a SARS interpretation note, this media release is not a binding ruling or statement of law.²⁶² Thus, a taxpayer may, under the Tax Administration Act 28 of 2011 (TAA), object to SARS decision to tax a Cryptocurrency as a receipt or accrual. In this way, a dispute may arise for adjudication.

It must further be noted that SARS’ classification of “Cryptocurrencies as assets of an intangible nature” for tax purposes, is in line with Bitcoin’s digital virtual nature of being a currency that is not tied to any jurisdiction, therefore possessing the qualities of being termed a universal currency. Furthermore, since the currency is intangible and not legal tender, this does not preclude it from being valued, and according to SARS, Bitcoin’s value can be ‘received or accrued’ in line with the definition of gross income for Income Tax purposes.²⁶³ Therefore, to gain an understanding of the South African direct Income Tax implications on Bitcoin we briefly consider the components of the gross income definition separately.

4.4.1 Residence

A residence based tax system is practiced in South Africa, “which means residents are, subject to certain exclusions, taxed on their worldwide income irrespective of where the income was earned.”²⁶⁴ This essentially means that with the three scenarios that have been outlined by SARS above,²⁶⁵ income on Bitcoin earnings that a taxpayer receives or which accrues to them, regardless of its source, will attract normal tax consequences. Furthermore, this implies that no matter where the source of the Bitcoin income is located in the world, this income will attract Income Tax consequences in South Africa for a South African resident. Thus, if a Bitcoin miner mines Bitcoin and receives income from the United States or provides goods and services and receives income from the United States, this amount will be subject to Income Tax in South Africa. Furthermore, any other activity that will result in Bitcoin income with the originating cause of such income being from outside South Africa, this amount may also be subject to Income Tax consequences in South Africa. However, the position is different with regard to persons not resident in South Africa, such persons are assessed for normal tax purposes on

²⁶¹Ibid.

²⁶²*Marshall v Commissioner for South African Revenue Services* 2018 ZACC 11 par 4-10.

²⁶³M Stighlingh et al op cit note 165 at 35.

²⁶⁴South African Revenue Services op cit note 244.

²⁶⁵Note 247,248 and 249 (See paragraph 4.3).

income that is acquired from a source within South Africa.²⁶⁶ In addition, for Bitcoin income to be subject to Income Tax in the determination of taxable income it must be an amount which is the next component of the definition that we discuss.

4.4.2 The Total Amount

SARS' guidance and classification of the Cryptocurrency is therefore acceptable as being in line with the South African courts' interpretation of the component, an "amount in cash or otherwise" affirming that when determining an amount, that amount can either be 'money or money's worth'²⁶⁷ which in our case is Bitcoin in the form of an intangible asset. Furthermore, the courts have also stated that "for an amount to be included in the gross income definition it does not need only to include money, but the value of every form of property earned by the taxpayer whether corporeal or incorporeal."²⁶⁸ This principle therefore falls in line with the characteristics of Bitcoin because as classified by SARS Bitcoin has been classified as an asset of an intangible nature that can also be recognized as an incorporeal asset with a monetary worth. Therefore, the Cryptocurrency can thus be regarded as an 'otherwise' amount falling into the gross income definition for Income Tax purposes.

4.4.3 In cash or Otherwise

On the media release issued by SARS, Cryptocurrencies typified by Bitcoin have been classified as "Assets of an Intangible Nature."²⁶⁹ This essentially entails that bitcoin is a form of property that cannot be touched and does not have a physical existence. This form of intangible asset however can be valued in money and does have money's worth which is in line with the *Delfos* case.²⁷⁰ Furthermore, as an incorporeal form of property the *Lategan* case²⁷¹ clearly states that property even if it is not cash does fit into the gross income definition. Therefore, the features of Bitcoin essentially align the Cryptocurrency as fitting into the gross income definition and are thus an 'otherwise' amount other than cash. This 'otherwise' amount in fitting into the gross income definition must further be received or must accrue to the taxpayer for Income Tax to be levied during the year of assessment. However, as noted in chapter 3 and by the SARS media release Bitcoin is an intangible asset that only exists in the internet therefore payments made by Bitcoin may not exist in physical form like fiat currency.

²⁶⁶Ibid.

²⁶⁷*Delfos* supra note 169 at 99.

²⁶⁸*WH Lategan* supra note 161 at 19.

²⁶⁹South African Revenue Services op cit note 25.

²⁷⁰*Delfos* supra note 169 at 99.

²⁷¹*WH Lategan* supra note 161 at 19.

This as a result implies that when a sender sends a Bitcoin amount instead of being received by an individual in physical form like fiat currency the Bitcoin amount accrues to the individual online making the individual entitled to a future payment.

4.4.4 Received by or Accrued to or in favour of

In order to fit into the gross income definition the Bitcoin amount must further be received or accrued on behalf and for the users own benefit.²⁷² Therefore, in essence it does not matter whether the individual was entitled to the receipt in question, but what matters is that when they take the Bitcoin amount it is received and duly taxable.²⁷³ As highlighted above, Bitcoin amounts are most likely to accrue than being received because of the Cryptocurrency's intangible nature. Instead of being received physically just like fiat currency, a Bitcoin amount will accrue online entitling the individual to a future payment. Therefore as held in the case of *Golden Dumps (Pty) Ltd v Commissioner for Inland Revenue*²⁷⁴ "an accrual occurs when a taxpayer is unconditionally entitled to an amount, although it may only be payable at a future date." Thus a future payment in Bitcoin amounts that accrues to an individual may therefore attract Income Tax consequences under the gross income definition.

4.4.5 From a Source within or deemed to be within South Africa for Non-South African citizens.

In determining the tax consequences for Non-South African residents, a source based tax system is applicable in determining the taxable income for income tax purposes. Therefore, should a dispute arise with regard to Bitcoin earnings from a source within South Africa for non-South African residents the courts will have to determine whether the originating cause of the income is from a source within South Africa. "Source in relation to receipts and accruals means not the quarter whence they come, but the originating cause of their being received as income."²⁷⁵ Therefore, in essence, Bitcoin taxpayers who are not South African residents will be taxed on income from Cryptocurrency that has its originating cause within South Africa.

In conclusion, it is therefore clear that SARS guidance on the tax treatment on Cryptocurrency typified by Bitcoin is sufficient for the application of normal tax consequences on the Cryptocurrency in South Africa. In the application of normal tax consequences on Bitcoin, the study has uncovered that Bitcoin as an intangible asset possesses the characteristics to being classified as an amount for Income Tax purposes. In addition, according to SARS guidance,

²⁷²*Geldenhuys* supra note 173 at 431.

²⁷³MP Finance supra note 174 at 6 par 12.

²⁷⁴*Golden dumps Pty Ltd v Commissioner for Inland Revenue* 1993 4 SA 110 (A) 117-118.

²⁷⁵*Lever Bros & Unilever Ltd* supra note 189 at 12.

the nature of Bitcoin renders it an otherwise amount that can be received or accrued by a taxpayer through the transfer of the Cryptocurrency on a Blockchain from user to user. Furthermore, just like the position in eSwatini in the gross income definition, the Bitcoin amount received must not be of a capital nature.

In essence, the Bitcoin must not be of an enduring benefit to the taxpayer that is used to produce income and is not consumed in the process save for normal wear and tear. However, the Bitcoin amount must be the product or fruit of the taxpayers labour or capital or both during the year of assessment.²⁷⁶ A further point to note is that unlike eSwatini, South Africa does have Capital Gains Tax where gains or losses from the disposal of capital assets can be included when determining Income Tax consequences of such amounts. In the next section we consider the capital gains consequences on Bitcoin amounts in South Africa.

4.5 Capital gains Tax and Bitcoin in South Africa

SARS has furthermore classified Bitcoin and other Cryptocurrencies as “assets of an intangible nature.”²⁷⁷ A significant point is that Bitcoin, just like money, is an asset. However unlike real money, which is an asset that can be touched physically, Bitcoin is an intangible asset that exists only in the virtual world. Therefore, gains or losses from the disposal of such assets are considered as being of a capital nature.²⁷⁸ Furthermore, the term ‘Financial Instrument’²⁷⁹ under Section 1 of the Income Tax Act 58 of 1962 has been amended by the Taxation Laws Amendment Act 23 of 2018²⁸⁰ to include Cryptocurrency. Section 1 (c) of the Act²⁸¹ states

“Section 1 of the Income Tax Act, 1962, is hereby amended—

by the deletion in subsection (1) in the definition of “financial instrument” of the word “and” at the end of paragraph (d), the insertion of the word “and” at the end of paragraph (e) and the addition of the following paragraph:
“(f) any cryptocurrency;”;

The explanatory memorandum on the Taxation Laws Amendment Bill 2018²⁸² provides clarification on the amendment by stating that “Cryptocurrency is a financial instrument and

²⁷⁶*Butcher Bros (Pty) Ltd Supra* note 166 at 34.

²⁷⁷South African Revenue Services op cit note 25.

²⁷⁸A Straude, A Greef op cit note 247.

²⁷⁹T Clendon “SA TECHNICAL ACCA: What is a Financial Instrument” available at <http://www.chinaacc.com/upload/html/2013/06/26/lixingcun7989928cf2cb4d69970e269efac8b12e.pdf> accessed 4 December 2020. Defines financial Instrument as: “Financial instrument is a contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity.”

²⁸⁰Taxation Laws Amendment Act 23 of 2018.

²⁸¹*Ibid.*

²⁸²The “Explanatory Memorandum on the Taxation Laws Amendment Bill, 2018 available at <https://www.sars.gov.za/AllDocs/LegalDoclib/ExplMemo/LAPD-LPrep-EM-2018> accessed 3 December 2020.

would therefore not be a personal use asset for capital gains tax purposes.”²⁸³ The insertion of Cryptocurrency under the definition of financial instrument in Section 1(1) of the Income Tax Act is therefore a measure by the National Treasury preventing Taxpayers from overlooking gains or losses from Cryptocurrencies on the basis that they are personal use assets.²⁸⁴ This emanates from the fact that when a taxpayer disposes of a Cryptocurrency held as a capital asset this may give rise to a capital gain or loss.²⁸⁵ The amendment therefore aides in that the non-consideration of Cryptocurrencies as personal use assets prevents the avoidance of Capital Gains Tax by taxpayers on the grounds that the Cryptocurrencies are personal use assets.

Therefore, in calculating the capital gains on Bitcoin for tax purposes, a determination of whether the intangible assets are of a capital or revenue nature is made. In making a determination, four building blocks need to be present. These are “(i) there must be an asset whether tangible or intangible, (ii) which must be disposed of during the year of assessment, (iii) there must be a base cost of the asset and (iv) proceeds on the disposal of such assets which may accumulate either a gain or a loss.”²⁸⁶

Furthermore, the Bitcoin disposed of must be of a capital nature. In determining the nature of the Bitcoin, reference is made to the case of *Commissioner for Inland Revenue v Stott*. This case suggests that in determining whether assets are capital or revenue in nature, the “method of acquisition, the purpose for its possession and ultimate disposal are important indicators that are considered when determining whether the asset is capital or revenue in nature.”²⁸⁷ Therefore, in the event a Bitcoin miner mines Bitcoin and goes for a number of years without disposing of them intentionally, and keeps them to sell at a later date for more profit, a gain or loss from such a transaction will therefore create Capital Gains Tax consequences.²⁸⁸ In addition, if in the determination, Bitcoins are declared to be capital in nature, then this will result in gains or losses that are acquired upon the disposal of such Bitcoins making up the user’s taxable income if they are gains or carried forward to the next year of assessment if they are losses²⁸⁹ “at the prescribed inclusion rate for Capital Gains Tax.”²⁹⁰

²⁸³Ibid.

²⁸⁴R Basson “An analysis of issues relating to the taxation of cryptocurrencies as financial instruments” (2020) 13 Journal of Economic and Financial Sciences. available at <https://jefjournal.org.za/index.php/jef/article/view/487/897> accessed 4 December 2020.

²⁸⁵Ibid.

²⁸⁶M Stighlingh et al Silke: *South African Income Tax* (2019) 565.

²⁸⁷*Commissioner for Inland Revenue v Stott* 1928 AD 252; 3 SATC 253, 261 and 262.

²⁸⁸A Straude, A Greef op cit note 247.

²⁸⁹M Stighlingh et al op cit note 215 at 595.

²⁹⁰A Straude, A Greef op cit note 247.

An important consideration to note is that when SARS makes a tax assessment, Capital Gains Tax is not assessed separately but is added to taxable income and is subject to normal tax.²⁹¹ A capital gain is the fruit of the alienation of an asset, in our case an intangible asset such as Bitcoin, where the disposal proceeds surpass the original “value of the asset, (Bitcoin) known as the base cost of the asset,²⁹² thus creating a profit known as a capital gain.”²⁹³ Therefore, a disposal of Bitcoins by a user at a price higher than its normal price results in a profit, otherwise known as a ‘taxable capital gain.’²⁹⁴ This may then be added to the user’s taxable income and consequently attracting normal tax consequences.

In addition, ‘paragraph 4 of the Eighth Schedule to the Act’²⁹⁵ states that “a person’s capital loss for a year of assessment in respect of the disposal of an asset during the year is equal to the amount by which the base cost of that asset exceeds the proceeds received or accrued in respect of that disposal.”²⁹⁶ Therefore, in the event there is a disposal of Bitcoin at a price lower than its normal price which is the base cost resulting in a loss then the loss is carried on to the following year of assessment. Therefore having discussed the Income Tax consequences and Tax on Capital Gains the study then moves to discuss deductions which are deducted in the process of determining a taxpayer’s taxable income.

4.6 Deductions

In determining taxable income, users may claim expenditure and losses linked with the Cryptocurrency. The courts have therefore stated that in determining expenditure and losses for deductions, the general deduction formula is ascertained by reading section 11(a) together with section 23(g) of the Income Tax Act 58 of 1962,²⁹⁷ to ascertain whether a deduction may occur.²⁹⁸ Section 11 (a) of the Act states

“For the purpose of determining the taxable income derived by any person from carrying on any trade, there shall be allowed as deductions from the income of such person so derived-

²⁹¹Income Tax Act Eighth schedule Paragraph 3.

²⁹²Paragraph three of the Eighth Schedule to the Income Tax Act states that “capital gains tax that will arise during that year of assessment, will be equal to the amount by which the proceeds received or accrued in respect of that disposal exceed the base cost of the asset.”

²⁹³Ibid.

²⁹⁴M Stighlingh et al op cit note 215 at 595.

²⁹⁵Income Tax Act 1962.

²⁹⁶South African Revenue Services “Capital Gains Tax” available at <https://www.sars.gov.za/TaxTypes/CGT/Pages/default.aspx> accessed 16 July 2019.

²⁹⁷Income Tax Act 1962.

²⁹⁸*Port Elizabeth Electric Tramway Co Ltd* supra note 218 at 20.

- (a) Expenditure and losses actually incurred in the production of the income, provided such expenditure and losses are not of a capital nature.²⁹⁹

Section 23 (g) of the Act³⁰⁰ states that

“No deductions shall in any case be made in respect of the following matters, namely-

- (g) Any moneys claimed as a deduction from income derived from trade, to the extent to which such moneys were not laid out or expended for the purposes of trade.”³⁰¹

Essentially the components making up the general deduction formula are set out in the following manner. All the components need to be proven for a deduction to take place.

1. “Expenditure and Losses
2. Actually incurred
3. During the year of assessment
4. In the production of income
5. Not of a capital nature
6. Either in part or in full laid out or expended for the purposes of trade (s23(g))”³⁰²

4.6.1 Carrying on of a Trade

In order for the elements set out in the deduction formula to apply in determining deductions, an individual must have been “carrying on a trade.” This component, as set out in section 11 of the act has two requirements which are a trade and the trade must have been carried on as an active step.³⁰³ Therefore, the essential features of carrying on a trade include the purchase of items for re sale, with the requisite intent to make a profit.³⁰⁴ This in our case may include the purchase of Bitcoin for re sale in order to make a profit at a later date. It is imperative that the Bitcoin user proves that he was carrying on a trade and if he is unable to discharge that onus, which is, he was “carrying on a trade, as an active step” then the Bitcoin user will not successfully claim deductions. In essence the Bitcoin user must have set up the Bitcoin trade activity for the purposes of making a profit.³⁰⁵

Although “the general implication is that expenditure incurred prior to the commencement of that trade is not deductible in terms of section 11”,³⁰⁶ certain pre-trade expenditure may be

²⁹⁹Income Tax Act 1962.

³⁰⁰Income Tax Act 1962.

³⁰¹Ibid.

³⁰²Ibid.

³⁰³*Income Tax Case 1476* (1989) 52 SATC 141 (T), 148.

³⁰⁴South African Revenue Services ‘Interpretation note 33 (Issue 3),’ 2 12 July 2014.

³⁰⁵*Income Tax Case 1404* (1985) 48 SATC 1 (N), 4.

³⁰⁶M Stighlingh et al op cit note 215.

deductible. Such pre-trade expenditure includes assets bought and salaries or rent paid. These may be allowed as deductions in terms of section 11A, which reads as follows,³⁰⁷

“(1) For purposes of determining the taxable income derived during any year of assessment by a person from carrying on any trade, there shall be allowed as a deduction from the income so derived, any expenditure and losses-

(a) Actually incurred by that person prior to the commencement of and in preparation for carrying on that trade.”³⁰⁸

In understanding the term ‘trade’ section 1 of the Act defines the term as³⁰⁹

“every profession, trade, business, employment, calling, occupation or venture, including the letting of any property and the use of or the grant of permission to use any patent as defined in the patents Act, or any design as defined in the Designs Act, 1993 (Act 195 of 1993), or any trade mark as defined in the Trade Marks Act, 1993 (Act 194 of 1993), or any copyright as defined in the Copyright Act, 1978 (Act 98 of 1978) or any other property which is of a similar nature.”³¹⁰

It must be noted that the term trade in this section has not necessarily been set out exhaustively, therefore the term is meant to include every form of ‘profitable activity’ and this in our case includes Bitcoin profits that may be derived from the carrying on of an income producing Bitcoin trading activity according to SARS media release.³¹¹ Having considered the first component of Section 11 which is the carrying on of a trade the study will now consider the component ‘in the production of income’.

4.6.2 In the production of income

The amount must have been expended for the purpose of producing income when trading in Bitcoin. The key requirement for Section 11 (a) is there must be a sufficient link between the expenditure or loss and the production of income.³¹² Therefore it must be established that the expenses incurred in producing Bitcoin profits are closely connected with the Bitcoin income producing activity.³¹³ Furthermore in examining the requirement in the production of income reference is made to the case of *Commissioner for Inland Revenue v Genn & Co Pty (Ltd)*.³¹⁴

³⁰⁷Ibid.

³⁰⁸Income Tax Act 1962.

³⁰⁹M Stighlingh et al op cit note 215.

³¹⁰Income Tax Act 1962.

³¹¹*Burgess v Commissioner for Inland Revenue* 1993 (4) SA 161 (AD) 55 SATC 185, 196.

³¹²*Port Elizabeth Electric Tramway Co Ltd* supra note 218 at 20.

³¹³Ibid.

³¹⁴*Commissioner for Inland Revenue v Genn & Co Pty (Ltd)* 20 SATC 113 (1955) All SA 382 (A), 120.

In this case the court held “that it must be proper, natural and reasonable to regard the expense as being part of performing the activity in question.” This case in essence illustrates that the expenses incurred during the Bitcoin income producing activity must be closely linked to each other in order to be deductible. In addition, to regard the expenses as part of the cost of performing the Bitcoin income earning operation the expenses must proper, natural and reasonable to be regarded as being part of the Bitcoin trading activity. Therefore, when running a Bitcoin income earning trading activity, proper, natural and reasonable expenses would include the servicing of highly powered computer machinery, losses incurred in the event there is a loss of internet connection during crucial Bitcoin trade. The last component to be considered is that the expenses incurred must not be of a capital nature.

4.6.3 Not of a capital nature

The expenses that are incurred in the producing of income through Bitcoin must not be of a capital nature. Section 11 (a) does not provide for deductions for expenses or losses incurred which are of a capital nature. Therefore, in determining expenses or losses of a capital nature, “money spent in creating or acquiring an income-producing concern is a capital expenditure, it is invested to yield a future profit and while the outlay does not recur the income does.”³¹⁵ Therefore, there is a great difference between money spent in creating or acquiring a source of profit and money spent in working it. Thus the former is capital and the latter is not.”³¹⁶ Essentially items that would be of a capital nature when trading in Bitcoin are non-recurring items, meaning they would have to be bought once-off to produce the income and this would include computer hardware. On the other hand, examples of expenses not of a capital nature being money spent on working a source of profit would be the costs of a reliable internet connection and expenses incurred in maintaining the computer hardware.

The discussion then brings us to section 23 (g) which is the negative part of the general deduction formula. In terms of this section the Bitcoin trader cannot claim expenses to the extent that these were not laid out for the purposes of trade. This provision in essence implies that if a Bitcoin trader earns a Bitcoin amount, the Bitcoin trader cannot claim for deductions if the Bitcoin amount was not earned in the carrying on of a trade or in the production of income. Therefore, in order to claim for deductions, the above requirements must all be met by the Bitcoin trader in order to claim for deductions. Having considered the direct tax

³¹⁵*George Forest Timber* supra note 223 at 526.

³¹⁶*Ibid.*

implications in the South African jurisdiction the chapter then goes on to consider lessons from international jurisdictions namely the UK and the USA.

4.7 Lessons from the United Kingdom and the United States of America

Having considered the implementation of tax regulations on Bitcoin in South Africa, the study as mentioned in chapter one now moves on to other international jurisdictions to ascertain the tax treatment of Cryptocurrencies with Bitcoin as a reference point. The study will conduct a brief investigation of the treatment of Bitcoin in terms of tax law in the UK and USA.

4.7.1 Regulation and Taxation of Crypto assets in the United Kingdom

The United Kingdom (UK), of which eSwatini is a former colony and from which the Kingdom has absorbed to a large extent its legal system which is now regarded as the common law in eSwatini, has been at the frontlines of developing regulations and the formulation of ways to apply tax on Cryptocurrency globally. The UK, through the Financial Conduct Authority (FCA) issued a Guidance Paper on Cryptoassets,³¹⁷ pointing out that

“While cryptoassets can be used as a means of exchange they are not considered to be a currency or money, as both the Bank of England and the G20 Finance Ministers and Central Bank Governors have previously set out.”³¹⁸

The Guidance paper further highlights that the Cryptoasset Taskforce Report (CATF) identified three forms of uses for Cryptoassets, which aid in their classification. These are:

1. “Exchange Tokens which are intended to be used as a method of payment and encompass ‘cryptocurrencies’ like bitcoin.
2. Utility Tokens, which provide the holder with access to particular goods or services on a platform usually using Distributed Ledger Technology.
3. Security Tokens which provide the holder with particular interests in a business, for example in the nature of debt due by the business or a share of profits in the business.”³¹⁹

As set out in the provisions, the policy paper essentially implies that if an individual buys, sells or transfers bitcoin they do so free from any regulations of the FCA in the UK.³²⁰ In addition, a significant point to highlight is that the current position in the UK regarding the regulatory classification of Bitcoin has not been finalised. Furthermore, as set out by the Bank of England

³¹⁷The white paper on the *Guidance on Cryptoassets Consultation Paper* (published in CP19 of 3 January 2019) 9 available at <https://www.fca.org.uk/publication/consultation/cp19-03.pdf> accessed 17 March 2019.

³¹⁸Ibid.

³¹⁹United Kingdom Financial Conduct Authority op cit note 312 at 9.

³²⁰Ibid 8.

and the FCA, the UK does not at the current moment consider Cryptocurrencies to be currency or money. However, Her Majesty's Revenue and Customs (HMRC), through a policy paper,³²¹ provides for the taxation of Exchange tokens, which also include Bitcoins in their definition, and this position is only for individuals and does not include businesses.³²² The Policy Paper points out that:

'In a majority of cases, individuals hold Cryptoassets as a personal investment, usually for capital appreciation in its value, or to make particular purchases. As a result, such individuals will be liable to pay capital gains tax when they dispose of their Cryptoassets, furthermore individuals will also be liable to pay Income Tax and National Insurance contributions on Cryptoassets which they receive from their employer as a form of non-cash payment, Mining, Transaction confirmation, and Airdrops.'³²³

Therefore, at present there is no classification of Cryptocurrencies in the United Kingdom. However, the HMRC, when applying tax on Cryptocurrencies categorises the application of tax consequences based on the activity that the individual that holds the Cryptocurrency uses it for when conducting transactions.³²⁴ In addition, it must be noted that, as evident from the policy paper, individual taxpayers may be liable to pay two kinds of taxes based on their intention for the Cryptocurrency in their possession. Individuals may attract Capital Gains Tax consequences if they hold Cryptoassets for investment purposes. In this instance an individual is only liable to pay tax on the profit that is made on the disposal of an asset that has had an increase in value.³²⁵ This in essence means that if an individual purchases Bitcoins for £ 100 (One Hundred Pounds) and four months later sells the Bitcoins for £ 1 500 (One Thousand Five Hundred Pounds), the individual will only be liable to pay tax on the £ 1 400 pounds profit that they have made on the disposal of the Bitcoins. It must further be noted that this may only apply on gains that are above the tax free allowance also called the "Annual Exempt Amount" which is £ 12, 300 and £ 6, 500 for trusts.³²⁶

Individuals may also liable to pay Income Tax if paid by their employer using Cryptocurrency such as Bitcoin as a non-cash form of payment. Furthermore, mining is a category that is subject to Income Tax where Cryptoassets are given as a reward to miners for solving puzzles on a

³²¹Her Majesties Revenue & Customs op cit note 98.

³²²Ibid.

³²³Ibid.

³²⁴Ibid.

³²⁵Gov.UK 'Capital Gains Tax' available at <https://www.gov.uk/capital-gains-tax> accessed 7 December 2020.

³²⁶Gov.UK 'Capital Gains Tax' available at <https://www.gov.uk/capital-gains-tax/allowances> accessed 7 December 2020.

blockchain in the generation of Cryptocurrencies.³²⁷ However the mining activity has to amount to a trade and this is determined by a variety of factors which include “the degree, organization, risk and commerciality of the mining activity.”³²⁸ The position is that where the mining activity does not amount to a trade the value of the Cryptoasset at the time of being awarded for successful mining will be taxable as income.³²⁹ However in a case where the taxpayer holds the Cryptoasset for a prolonged period they may pay for Capital Gains Tax at the time of disposal of that Crypto asset.³³⁰ In addition, Income tax is also applied to transaction confirmation.³³¹ Therefore, an individual may then get paid by Bitcoin, especially in the confirmation of Bitcoin mining transactions.

Lastly, another transaction that may attract Income Tax consequences is an airdrop transaction, whereby a person receives an award in the form of Bitcoin or other Cryptocurrency. This may for instance occur when there has been an allotment of Cryptocurrency during the conduct of advertising campaigns.³³² However, airdropped Cryptocurrency tokens such as Bitcoin will not always attract Income Tax consequences. Income Tax will not apply if the tokens are received “(i) Without doing anything in return (for example, not related to any service or other conditions) (ii) Not as part of a trade or business involving Cryptoassets or mining.”³³³

Having considered the position of the UK it is clear that UK is still conducting research on how to regulate Cryptocurrency. However, it is imperative to highlight that the Cryptoasset taskforce has in light of uses of Cryptocurrency been able to identify three different types of Cryptocurrencies of which Bitcoin was classified as an exchange token, which will aid in finding an appropriate classification for eSwatini’s jurisdiction. Furthermore, the different types of transactions where tax can be applied have also been identified which are Capital Gains Tax and Income Tax in the UK. The study then leads us to a brief exploration of the regulatory and tax implications in the United States of America in gathering lessons for eSwatini.

³²⁷Her Majesties Revenue & Customs op cit note 98.

³²⁸Ibid.

³²⁹Ibid.

³³⁰Ibid.

³³¹Thompson Reuters ‘Transaction Confirmation’ available at [https://uk.practicallaw.thomsonreuters.com/2-3868134?transitionType=Default&contextData=\(sc.Default\)&firstPage=true](https://uk.practicallaw.thomsonreuters.com/2-3868134?transitionType=Default&contextData=(sc.Default)&firstPage=true) accessed 1 October 2019 “a document whereby parties to a swap or other derivatives transaction use to specify the commercial terms of the transaction, including pricing terms such as the transaction spread.”

³³²Her Majesties Revenue & Customs op cit note 98.

³³³Ibid.

4.7.2 Regulating Virtual Currencies in the United States of America

The United States of America (USA) has also made many developments to its regulatory front on Cryptocurrencies through the “Department of the Treasury Financial Crimes Enforcement Network” (FinCEN) by issuing a guide to the Department’s regulations on Cryptocurrencies. The guide is meant for “persons administering, exchanging, or using virtual currencies”. In addition, the USA through FinCEN has classified Cryptocurrency, as we know it, as, “Convertible virtual currency” which is referred to as a monetary instrument that has an equal monetary value to fiat currency.³³⁴ Cryptocurrencies such as Bitcoin typify “convertible virtual currencies.” In the position of both South Africa and eSwatini³³⁵ these currencies may be bought or bartered for Swati Emalangen, South African Rands and other virtual assets. However, in the USA virtual currencies are not regarded as having legal tender status.³³⁶

In addition, even though convertible virtual currencies do not have legal tender status, the “Securities and Exchange Commission (SEC)”³³⁷ in the USA, on July 25 2017, upon conducting an investigation on distributed ledger technology and digital currency that operates through blockchain issued a report³³⁸ where it stated that.

‘.....the Commission has determined that DAO Tokens are securities under the Securities Act of 1933 (“Securities Act”) and the Securities Exchange Act of 1934 (“Exchange Act”). The Commission deems it appropriate and in the public interest to issue this report of investigation (“Report”) pursuant to Section 21(a) of the Exchange Act to advise those who would use a Decentralized Autonomous Organization (“DAO Entity”), or other distributed ledger or blockchain-enabled means for capital raising, to take appropriate steps to ensure compliance with the U.S. federal securities laws. In addition, any entity or person engaging in the activities of an exchange must register as a national securities exchange or operate pursuant to an exemption from such registration.....’³³⁹

³³⁴The ‘Application of FinCEN’s; Regulations to Persons Administering, Exchanging, or Using Virtual Currencies’ (published in FIN-2013-G001 of 18 March 2013) available at <https://www.fincen.gov/sites/default/files/shared/FIN-2013-G001.pdf> accessed on 2 April 2019.

³³⁵H Salkin, T Perez; ‘Virtual currency constitutes Taxable Property for U.S. Federal Tax purposes’ available at https://www.taxlitigator.com/virtual-currency-constitutes-taxable-property-for-u-s-federal-tax-purposes/#_edn5 accessed on 3 April 2019.

³³⁶Ibid.

³³⁷The ‘U.S. Securities and Exchange Commission’ available at <https://www.sec.gov/Article/whatwedo.html> accessed 2 January 2020. “The mission of the U.S. Securities and Exchange Commission is to protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation.”

³³⁸The ‘Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act of 1934: The DAO’ (published in Release No. 81207 of 25 July 2017) available at <https://www.sec.gov/litigation/investreport/34-81207.pdf> accessed 8 October 2019.

³³⁹Ibid.

With reference to the above extract from the report by the SEC it is clear that the USA is at an advanced stage with regard to the regulation and enforcement on ‘capital raised’,³⁴⁰ through blockchain and distributed ledger technology. Therefore the Commission can enforce transactions that are conducted using this type of technology, which in relation to this study will include Bitcoin. Furthermore the Commission has also requested entities that use this type of technology to register, classifying these types of entities as DAO’s which are “an example of a decentralised autonomous organization, which is a term used to describe a virtual organization embodied in computer code and executed on a distributed ledger technology or Bitcoin”.³⁴¹ However, it must be noted that this is not a comprehensive stance as the USA is still in the process of developing the Uniform Regulation of Virtual- Currency Businesses Act.³⁴² Having noted the regulatory aspect of the USA we now consider the Internal Revenue Services in relation to the application of tax on virtual currencies.

4.7.3 Tax Implications on Virtual Currencies in the United States of America

In the United States of America, the revenue collecting body is the Internal Revenue Service (IRS) and is the body responsible for the collection of taxes, providing tax statutory guidance and implementing the internal revenue code.³⁴³ The service issued a reminder to taxpayers that “virtual currency transactions are reportable on their income tax returns”. The reminder made reference to notice, IRS notice2014-21 which provides that for tax purposes in the United States virtual currency transactions will be taxed using the tax principles that apply to property transactions.³⁴⁴

Therefore, in understanding the Guidance issued by the Internal Revenue Service to treat Virtual Currencies as property it is important to understand how property tax is applied in the United States of America to draw lessons for eSwatini. What must be understood as a point of

³⁴⁰Ibid.

³⁴¹Ibid.

³⁴²Uniform Law Commission ‘Virtual Currency Business Act, regulation of ‘ available at <https://www.uniformlaws.org/committees/community-home?CommunityKey=e104aaa8-c10f-45a7-a34a-0423c2106778> accessed 13 November 2019 “The Uniform Regulation of Virtual-Currency Businesses Act (URVCBA) provides a statutory framework for the regulation of companies engaging in ‘virtual-currency business activity.’ Such as exchanging, transferring, or storing virtual currency, holding precious metals or certificates of electronic precious metals; or exchanging digital representations of value within online games for virtual currency or legal tender. The URVCBA’s unique, three-tiered structure clarifies whether an individual or company engaging in virtual currency business activity is (1) exempt from the Act; (2) must register; or (3) must obtain a licence.”

³⁴³Wikipedia ‘Internal Revenue Service’ Available at https://en.wikipedia.org/wiki/Internal_Revenue_Service accessed 5 April 2019.

³⁴⁴United States, Internal Revenue Services in Notice 2014-21 of 2014 1 available at <https://www.irs.gov/pub/irs-drop/n-14-21.pdf> accessed 2 April 2019.

departure is that to create a profit or gain the property or Bitcoin must be invested which may also pose the risk of loss for the investor. As such when invested Bitcoin may then be classified as “Investment Property” and may have the effect of income production for the investor³⁴⁵ and this may include ‘stocks and bonds’ and or Virtual Currency.³⁴⁶ In light of the foregoing before applying tax principles on gains or losses arising out of invested Bitcoins three steps are followed by the Internal Revenue Service in order to determine the gains or losses from the invested property and these include;

- i) Calculating the realized gain or loss;
- ii) Figure out the recognized portion of the gain or loss;
- iii) Characterize the recognized gain or loss as ordinary, capital, or IRC section 1231 property.³⁴⁷

In calculating a realized gain or loss from invested Bitcoin the starting point is knowing the initial cost also known as a “basis”³⁴⁸ this may include payment for the Bitcoin in cash, debt obligations or other property or services to purchase the Bitcoin.³⁴⁹ In certain other instances the position may differ especially where the receiver of the Bitcoin receives it without payment obligations and this may occur where the Bitcoin is acquired as a gift, inheritance received for services or the Bitcoin is received in taxable trades. In this case the “fair market value”³⁵⁰ of the Bitcoin would be applicable.

It is important to note that in some cases upon acquiring the Bitcoin an adjustment to the basis or initial cost to the Bitcoin may occur this may then have the resultant effect to the gain or loss that is realised on the invested Bitcoin, this is known as an “Adjusted Basis”.³⁵¹ In determining a gain from the “Amount realised” the amount from the sale should be greater than the basis including the adjusted basis of the Bitcoin. This also applies for losses incurred where

³⁴⁵K Yu ‘Bitcoin: Currency of the Future or Investment Property’ (Unpublished Mini Dissertation University of San Diego 2015) 12. available at https://digital.sandiego.edu/cgi/viewcontent.cgi?article=1005&context=honors_theses accessed 5 December 2020.

³⁴⁶Ibid at 12.

³⁴⁷Ibid at 12.

³⁴⁸Publication 551 (12/2018) ‘Basis of Assets’ available at <https://www.irs.gov/publications/p551> accessed 5 December 2020.

³⁴⁹K Yu op cit note 340 at 13.

³⁵⁰Internal Revenue Service ‘Publication 561 (02/2020), Determining the Value of Donated Property’ available at <https://www.irs.gov/publications/p561> accessed 6 December 2020. Defines Market value as the “value (FMV) is the price that property would sell for on the open market.”

³⁵¹K Yu op cit note 340 at 13. “An example is that the basis of stocks or bonds is usually the purchase price plus any costs and fees associated with the purchase price. After a stock purchase, the basis must be adjusted for certain events, including the receipt of more stock from non-taxable stock dividends or stock splits and the receipt of non-dividend distributions.”

the “Amount Realised” is lesser than the basis or initial cost and the adjusted basis of the Bitcoin.³⁵²

Upon determining the gain or loss the next step is “recognition.”³⁵³ In this phase it must be determined whether the portions of either the gains or losses are recognizable and this is a requirement that must be met for tax purposes.³⁵⁴ It must be noted however that with some exchanges, for example when goods of “like kind”³⁵⁵ are exchanged, they are not recognizable for tax purposes. This would be the case where a Bitcoin is exchanged for another Virtual Currency of like nature and of the same value in contrast to a Bitcoin being exchanged for fiat currency.

The final step is that of Characterization. This process involves determining the character of the gain or loss as this plays a role in determining a taxpayer’s liability on the amount realised.³⁵⁶ Gains or losses that are recognized are categorized as either;

- i) “Ordinary;
- ii) Capital or
- iii) Section 1231 gains or losses.”³⁵⁷

The characterization of gains or losses may differ and gains or losses may be characterised as either ordinary or capital or a combination of both.³⁵⁸ When characterizing gains or losses the nature of the assets sold, the time period of usage and keeping of that property or asset in our case being a Bitcoin is considered.³⁵⁹ Therefore if a sale of assets that are not of a capital nature also known as ‘ordinary assets’ occurs, then ordinary gains or losses may be realised ordinary assets include and are not limited to inventory accounts.³⁶⁰ On the other hand capital gains or losses are the consequence of a sale where the property has been kept for investing or personal usage by the taxpayer and these include and are not limited to bonds, cars, gold, silver and jewellery.³⁶¹

³⁵²M.S Wicht op cit note 13 at 37.

³⁵³Internal Revenue Service ‘Publication 544 (2019), Sales and Other Dispositions of Assets’ available at <https://www.irs.gov/publications/p544> accessed 6 December 2020.

³⁵⁴Ibid.

³⁵⁵Ibid.

³⁵⁶M.S Wicht op cit note 13 at 37.

³⁵⁷K Yu op cit note 340 at 14.

³⁵⁸M.S Wicht op cit note 13 at 38.

³⁵⁹K Yu op cit note 340 at 14.

³⁶⁰Ibid.

³⁶¹Ibid.

A further characterization is that of Internal Revenue Code section 1231 treatment of gains and losses. In this instance property will qualify to be treated as a section 1231 gain or loss if it is held by the taxpayer for more than one year.³⁶² These are characterised by sales or exchanges of property that is either used in a trade or business or held for the production of rents or royalties.³⁶³ Therefore the sale and exchange of tangible property or “depreciable personal property, leaseholds, cattle, horses and other livestock and unharvested crops constitutes transactions that are section 1231 gains or losses.”³⁶⁴ The characterization of section 1231 gains or losses as being capital or ordinary is therefore determined from the gains and losses from transactions by a taxpayer.³⁶⁵ What must further be noted is that recapture rules will be applied on section 1231 transactions, in order to determine if any part of the gain or loss can be recognisable as ordinary income due to “prior deductible depreciation expense.”³⁶⁶

4.7.4 Lessons for South Africa

Having considered the lessons from the UK and the USA, a few lessons that can be taken away by South Africa from the study are the following. As a point of departure regarding the regulatory aspects towards Cryptoassets, South Africa should consider adopting a flexible approach in addressing the regulation of Cryptocurrencies in line with the rapid and frequent technological advancements that are associated with Cryptocurrencies. This may be done by taking a position or stance that will move with the fast evolving technology of Cryptocurrency. It is further well worth mentioning that SARS has taken a bold approach in relation to the taxation of Cryptocurrency which has set the ball rolling, by categorising Cryptocurrencies as assets of an intangible nature. This approach encourages the development and usage of Cryptocurrencies. However, his approach should be in line with the approach that has been adopted in the UK where there are tax exempt amounts and Capital Gains Tax is only applied once the gains have surpassed the said amounts. Furthermore, in order to effectively apply Tax on Cryptocurrencies a system should be developed within which all Cryptocurrency users, be it for investment or trade purposes should be registered in order to fast track the payment of taxes in line with the IFWG proposals. Lastly it is also worth noting that SARS should expand its Tax net by not only considering Cryptocurrencies typified by Bitcoin for Tax purposes but to also consider Cryptoassets in general as this term is much broader and further focuses on other Cryptoassets such as utility tokens and security tokens when applying Taxes. In light of

³⁶²M.S Wicht op cit note 13 at 38.

³⁶³Ibid.

³⁶⁴Ibid.

³⁶⁵K Yu op cit note 340 at 16.

³⁶⁶Ibid.

the foregoing the legal regulatory and Tax developments are evidently embracing the new developments presented by this new phenomenon.

4.8 Conclusion

In conclusion, it is apparent that South Africa, through SARS, has taken great strides in applying the relevant legislation in regulating Cryptocurrency. The SARB through the IFWG is still however, like many other jurisdictions, in the process of finding suitable solutions on how to regulate Cryptocurrency. The working group formed under the auspices of the SARB has had its delegates highlighting the need to address emerging innovations and the identification of the risks that are associated with the technology when formulating regulations.

In addition, when considering taxation, South Africa has a regime that differs from that of eSwatini in that South Africa taxes its citizens on a residence basis, which also assesses their worldwide income. Furthermore, tax in South Africa is also assessed on non-residents who acquire income from a source within the Republic of South Africa. Therefore, it is evident that no matter where the Bitcoin earnings are derived from, they can be assessed and taxed by SARS. SARS has furthermore made its position clear regarding Cryptocurrency by classifying Cryptocurrencies as “assets of an intangible nature” for purposes of tax, stating that normal tax rules are to apply to Cryptocurrencies. This approach adopted by SARS has been done through making Bitcoin a reference point due to the high number of Bitcoin transactions that have been reported to occur regarding this Cryptocurrency. This essentially means that normal tax consequences, including Capital Gains Tax consequences, are attracted by Bitcoin transactions.

This chapter has also briefly examined the position of the UK and the United States of America to acquire lessons on how they treat Cryptocurrencies in applying tax and examining how these jurisdictions classify Cryptocurrencies in terms of regulations. The UK has not set out a classification for Cryptocurrency transactions, in their regulation and application of taxes. But the UK applies taxes based on individual transactions to which it applies both Capital Gains Tax and Income Tax. Lastly, the United States of America has classified Cryptocurrencies as ‘Convertible virtual currencies’ and the IRS has set out that the tax consequences for these currencies are Property Tax consequences.

This chapter has therefore presented a valuable contribution to the eSwatini jurisdiction on the different ways in which tax consequences may be applied to Cryptocurrencies such as Bitcoin. Furthermore, it is apparent from the discussion above that just like the current position in the kingdom of eSwatini the jurisdictions covered in this chapter are also still in the process of

conducting research on Cryptocurrencies. This includes the developing of tax laws that will accommodate the rapid growth of the technology on Cryptocurrencies. However, unlike eSwatini the jurisdictions covered have relied on their existing tax legal frameworks on the application of tax on Cryptocurrencies. Therefore, in the next chapter we will analyse the application of tax laws and regulations on Cryptocurrencies in order to find ways in which to regulate and apply tax on Cryptocurrency.

CHAPTER 5 RECOMMENDATIONS AND CONCLUSION

5.1 Introduction

Having considered the nature of Bitcoin the study has discovered that there is a growth in the adaptation of Cryptocurrency in the unregulated virtual financial markets. In addition, it is clear from its nature that Bitcoin is highly innovative and is set to bring, if accepted and properly regulated, a significant change in the financial market of eSwatini. This change will have the consequence of minimizing costs when conducting financial transactions, and increasing the speed at which financial transactions are conducted in eSwatini, therefore enhancing the ease of conducting business for eSwatini internationally.

However as pointed out in the study, Bitcoin still poses a huge challenge to financial regulators, especially in eSwatini and South Africa, due to the Cryptocurrency's highly technological and anonymous nature.³⁶⁷ The blockchain technology embedded at the heart of the Cryptocurrency is in line with current technology trends and as technology improves, the Cryptocurrency has a high possibility of evolving. The rapid technological change affecting Cryptocurrency is the main challenge that financial regulators and tax commissioners face with regard to the development of regulations that may be applicable to Bitcoin.

In addressing the challenges that come with accepting Cryptocurrency in the financial markets, the more developed jurisdictions have been in the forefront in addressing the issue of applying taxes and regulating the Cryptocurrency. In addition, the study has also explored developments on the current position of research that is being conducted by the CBE and SARB on new financial technologies, focusing on the issue of financial regulations for Cryptocurrency. In this regard the study has considered briefly the position of the United States of America and the United Kingdom in addressing the regulation and the tax treatment of Bitcoin. Therefore, to properly address the issue of uprooting the relevant and favourable recommendations for the Kingdom of eSwatini a comparative analysis of the direct tax consequences of eSwatini and South Africa is conducted. As such brief lessons from more advanced jurisdictions which have been addressed in chapter 4 will then be usurped in order to gather useful solutions for the kingdom of eSwatini.

³⁶⁷Note 87 (See paragraph 2.5)

5.2 The regulatory consequences of Bitcoin

In developing the appropriate regulatory framework for Cryptocurrencies such as Bitcoin, both South Africa and eSwatini have taken active steps in a bid to avoid the adverse risks that are associated with the Cryptocurrency. The study has therefore uncovered that both eSwatini and South Africa have noted the risks that are associated with Bitcoin by issuing a user alert to Cryptocurrency users of the gap in the regulation of Cryptocurrency, noting that users may have no recourse should a dispute regarding Cryptocurrencies arise.³⁶⁸ In addition, both authorities have also embarked on the process of conducting research on the possible solutions on how to develop regulations that may best suit the legal framework of both jurisdictions. In the development of a suitable regulatory framework, eSwatini through the CBE has thus formed a task team that is responsible for conducting research to address the regulation of Cryptocurrencies in eSwatini. Furthermore, in South Africa, a task team known as the IFWG working group made up of members of the national treasury, SARB, SARS, FSCA, and FIC has also been formed. This group has been tasked with the mission of developing knowledge amongst the stakeholders placing them in line with the developments of financial technology, examples of such financial technology being the development of Cryptocurrency.³⁶⁹

Therefore, as a point of departure, it must be highlighted that in addressing the question of Cryptocurrency regulation, the representatives of the IFWG working group have frowned upon assigning new definitions and regulations to Cryptocurrency, citing that the currency is still in its development stage. The group further mentioned that if regulations are created, this might result in the regulations becoming outdated because of the Cryptocurrency's evolving nature.³⁷⁰ However, it is useful to mention that the representatives should have also considered an approach that would accommodate the rapid development of the emerging financial technologies. This is because there is a possibility that more technologies may emerge and the law needs to adopt a more flexible approach as technology has become a growing part of the global financial markets.

Furthermore, the UK and the USA have taken an approach that is similar to that taken by both eSwatini and South Africa on the application of regulations on Cryptocurrencies. As highlighted in chapter 4 of the study, the FCA and FinCEN do not consider Cryptoassets to be

³⁶⁸Note 130 (See paragraph 3.2)

³⁶⁹Note 238 (See paragraph 4.2)

³⁷⁰Note 240 (See paragraph 4.2)

legal tender in as much as they may be a means of exchange.³⁷¹ This position adopted by the Working Group, the FCA and FinCEN is in line with the position taken by the eSwatini Central Bank. This position strengthens the notion that regulators should assign flexible regulations giving strong consideration to the fact that the technology behind Cryptocurrency is still developing.

Furthermore, the proposal presented by the working group seems appealing for adoption by the eSwatini task team. The proposal suggests “that existing legislation be amended by altering existing definitions to allow the better development of emerging innovation.”³⁷² Secondly, “that the regulations for Cryptocurrencies must be proportional and appropriate to the risk of the innovation or instrument and that the activity and not the entity be regulated, and regulation must as far as possible be technology neutral.”³⁷³ The approach taken by the working group encourages the adoption of new financial technologies by the CBE, as it sheds light to the CBE which is still in the process of monitoring and conducting research on Cryptocurrencies. In addition, the view seems to show that not only financial regulation of Cryptocurrency but also other legislation will have to begin the process of adapting to the fourth industrial revolution in order to accommodate new technologies.

A highlight of adapting legislation to new technologies is evident on the approach adopted by the SEC in the USA. Taking the position that virtual currencies operating through blockchain or distributed ledger technology are considered Securities in terms of the USA’s Acts namely “the Securities Act of 1934 and the Securities Act of 1933.”³⁷⁴ Therefore, criminal activity conducted through these technologies may attract criminal liability. This approach seems appealing for eSwatini because as research is being conducted on finding regulations there may be transactions that may be processed by users and an interim regulatory approach is a necessity to protect the citizens of eSwatini from illicit activity.

Therefore, the position taken by SARS and CBE needs to be corrected because it leaves a gap that becomes vulnerable to criminal manipulation. This is because both the CBE and the SARB expressed in the alerts that they issued that users would not be protected in the event they fell victim to criminal activity. Therefore, an approach that may enable the enforcement of illegal

³⁷²Note 244 (See paragraph 4.2)

³⁷³Note 245 (See paragraph 4.2)

³⁷⁴Securities Exchange Act of 1934 and Securites Exchange Act 1933.

transactions and fraudulent activity is essential to combat any criminal activity associated with Cryptocurrencies such as Bitcoin. Thus, having considered the development of research on the regulatory aspect of Cryptocurrency, the study now moves on to a comparative analysis of the application of tax rules on Cryptocurrencies in the jurisdictions of eSwatini and South Africa.

4.3 A comparative analysis of eSwatini and South Africa acquiring brief lessons from the USA and the UK

The common law has had a vital input in the development of laws in both the jurisdictions of eSwatini and South Africa and as such, the direct tax consequences in both jurisdictions are relatively similar. However, the South African jurisdiction has a broader application than that of the Kingdom of eSwatini in the sense that unlike South Africa, eSwatini does not apply Capital Gains Tax. Findings from this research have also uncovered that, Income Tax in both jurisdictions is levied on the gross income of the taxpayer in any year of assessment. It must further, be highlighted that a thread of similarity on the wording of the provisions has also been noted between the jurisdictions. As such, both jurisdictions in their definitions of gross income provide “for the taxation of amounts in cash or otherwise that are received by or have accrued to or in favour of any person in any year of assessment.”³⁷⁵

Therefore, in assigning interpretations on the components of the gross income definition, the findings have given the result that South African case law has a highly persuasive nature on eSwatini tax legislation. This is mainly because the legislations of both jurisdictions have been developed under the same common law. Therefore, when interpreting the legislations of both jurisdictions, it has been determined that Bitcoin as a Cryptocurrency does fit into the Gross Income definition of both the South African and eSwatini Income Tax legislations and is therefore an otherwise amount. A further finding is that the virtual nature of Bitcoin as it exists on the internet fits in well with the principle established in the *Lategan* case³⁷⁶ as an incorporeal thing to which a value can be assigned. This approach is correct because it is in harmony with the approach adopted by SARS of classifying Cryptocurrencies typified by Bitcoin as assets of an intangible nature, which cannot be touched but exist on the internet.

Furthermore, both the Income Tax Act 58 of 1962 and the Income Tax Order No. 21 of 1975 provide that the amounts must have been received by the taxpayer or in other cases must have accrued to the taxpayer. These provisions are well set out in the *Geldenhuis* case,³⁷⁷ where the

³⁷⁵Income Tax Order 1975.

³⁷⁶*WH Lategan* supra note 152 at 19.

³⁷⁷*Geldenhuis* supra note 164 at 431.

court held “that this must be on the taxpayer’s behalf for the taxpayers own benefit.”³⁷⁸ In addition, as held in the case of *MP Finance*³⁷⁹ the individual does not need to be entitled to the amount in question for the amount to be received or accrued but what matters is that it has been acquired and therefore received and duly taxable. Furthermore that the amount does not need to be due and payable to the Bitcoin user, but can be assessed from a right that has been vested on the user for a future payment in Bitcoin as set out in *Peoples Stores* case.³⁸⁰ These principles, therefore accommodate Bitcoin amounts that have accrued as awards from the mining of Bitcoin, Bitcoin that has been received or accrued as a form of payment for the provision of goods or services, and Bitcoin that has been received in exchange for fiat currency. However, what must be noted is that as uncovered from this research the intangible nature of this Cryptocurrency will mostly result in Bitcoin amounts accruing to an individual rather than being received. This is because when payments are made by the sender of Bitcoin to the receivers Bitcoin wallet, they accrue to the individual online entitling them to a future payment rather than a direct physical form of payment like fiat currency.

A further finding is that eSwatini exercises a source based tax regime on its citizens where tax is applied on income sourced from eSwatini “or from a source deemed to be ”³⁸¹ eSwatini. However, South Africa has a much broader tax regime to that of eSwatini in the sense that, South Africa applies tax on a residence basis; this includes worldwide income of South African residents. Furthermore as discussed in chapter 4 “Non-South African residents are taxed on a source based tax system on income that they have derived from a source within South Africa.”³⁸² Therefore, eSwatini and South Africa for non-residents in determining the source of Bitcoin earnings in both jurisdictions, the originating cause of the earnings is the guiding factor as set out in the case of *Lever Bros and Unilever Limited*.³⁸³ Thus, in essence this means that if the transactions conducted on the internet give rise to Bitcoin earnings, any dispute that arises may be solved by tracing back the earnings to the source where the transaction took place.

However, a feature about Bitcoin that creates a problem for the Swati jurisdiction is that this Cryptocurrency is not tied to any jurisdiction. Therefore, this strongly suggests that if a user

³⁷⁸Ibid.

³⁷⁹*MP Finance* supra note 165 at 6 par 12.

³⁸⁰*People’s Stores (Walvis Bay) (Pty) Ltd* supra note 155 at 20.

³⁸¹Income Tax Order 1975.

³⁸²Note 248 (See paragraph 4.3)

³⁸³*Lever Bros & Unilever Ltd* supra note 180 at 12.

can successfully establish that the originating cause of the earnings derived from Bitcoin were not conducted in eSwatini then the ERA will not be able to enforce the collection of tax on the earnings. However, this would not be the case in South Africa because SARS assesses taxes on worldwide income from a source that is anywhere in the world. This position presents us with a valuable lesson for eSwatini in that the laws in eSwatini should be developed in order to cover a broader context as that of South Africa thus applying tax on the worldwide income of its citizens.

In essence, the worldwide income provision in the South African Income Tax Act entails that the worldwide income from investments and all worldwide income of a natural person who is a resident is subject to normal tax. Thus, if income from Bitcoin transactions has been originally processed in Zimbabwe then the provision on worldwide income causes such earnings to fall within the in the gross income definition of the Income Tax Act of South Africa. Therefore, eSwatini which assesses income on a source based basis suffers a gap in the sense that if a person can cross the border from eSwatini and just be two metres from the eSwatini side of the border to process a transaction via the internet, he would not be liable to pay tax on those earnings. Therefore, an adoption of taxing worldwide income in eSwatini like its counterpart South Africa seems more favourable with the advent of the fourth industrial revolution.

However, it must be noted that in as much as eSwatini does not apply tax on worldwide income, eSwatini exercises tax on amounts that are deemed to be from a source within eSwatini. The same approach is used by SARS to apply tax on non-residents in South Africa who have a source of their earnings from a South African source. This essentially entails that if a company in eSwatini is carrying on a particular business and attracts customers from outside eSwatini and as a result renders services outside eSwatini, the earnings derived from this transaction are deemed to be from a source within eSwatini. It is submitted that these provisions are not enough. This is because, in order for amounts to be assessed from a deemed source the same trade has to be carried on from within eSwatini in order to be subject to Income Tax. This is different from the assessment of worldwide income where any income would be assessed from a source outside South Africa. Therefore, it is essential for eSwatini to not only consider its assessment of tax on a source from eSwatini or deemed to be from eSwatini but to also include the worldwide income of natural persons in its tax legislation.

Furthermore, a further finding is that unlike South Africa, eSwatini does not have Capital Gains Tax. Therefore, interest that has been gained or losses that have been incurred from the disposal

of capital assets cannot be subject to capital gains tax. An example is when a Bitcoin user invests Bitcoins which he has acquired from mining or has been paid by Bitcoin through the exchange of goods or services for Bitcoin. If the Bitcoins gain interest or incur losses, then these losses or interest may not be subject to capital gains tax. However, in South Africa the position is different because Capital Gains Tax is provided for in the Income Tax Act and is applied on interest that has been gained or losses that have been incurred on the alienation “of capital assets” as established in chapter 4 of the study. Therefore, an addition of Capital Gains Tax provisions on Swati legislation will aid in covering more ground not only on Cryptocurrency but also on many investments that may that have accumulated gains or have incurred loss on the alienation “of capital assets”. Lastly, what has been established from both jurisdictions of eSwatini³⁸⁴ and South Africa³⁸⁵ is that they apply deductions on expenses and loss that “have been incurred in the production of income and are not of a capital nature.” However, it must be noted that the deductions provisions from both jurisdictions are slightly different. Section 11(a) of the South African Income Tax Act³⁸⁶ has as one of its components that “the income must have been derived from the carrying on of a trade.”³⁸⁷ However, the stance in eSwatini the differs as the components do not include that the income “must have been derived from the carrying on of a trade”³⁸⁸ but merely states that income must have been derived in the production of income and must not be of a capital nature.

It is therefore submitted that the provisions of the Swati legislation give room for manipulation in the sense that without the component in the carrying on of trade as provided for “in section 11 of the South African Income Tax Act.”³⁸⁹ The Swati legislation allows a person that has produced income on Bitcoin earnings once off without having been carrying on a trade as an active step to claim deductions on expenditure or have losses moved forward to the following year. As set out in Income Tax Case 1476³⁹⁰ “that if in any year of assessment a company does not carry on a trade, it is not permitted to carry forward to that year any balance of assessed loss.”³⁹¹ This gap in the Income Tax Order presents further lessons for eSwatini which are

³⁸⁴Note 216 (See paragraph 3.8)

³⁸⁵Note 297 (See paragraph 4.7)

³⁸⁶Income Tax Act 1962.

³⁸⁷*Ibid.*

³⁸⁸*Ibid.*

³⁸⁹*Ibid*

³⁹⁰Income Tax Case 1476.

³⁹¹*Ibid.*

essential for adoption in the making of amendments of the deductions provisions in the Swati legislation.

Therefore, having considered the direct tax consequences of the Swati legislation on Bitcoin as set out in the study compared to those of the South African jurisdiction. It is evident that there are a number of gaps that need to be addressed in the Income Tax Order 1975 in order to accommodate the new emerging financial technologies. However, before making a conclusion on the study it is essential to gather a few lessons from the UK and the USA which are jurisdictions that have more advanced regulations on Bitcoin Cryptocurrency transactions.

5.4 Lessons Acquired from the United Kingdom and the United States of America

The United Kingdom in the application of taxes on Cryptocurrency earnings has also noted that users may be liable to pay two kinds of taxes which are Income Tax and Capital Gains Tax. These taxes are applied based on the intention that the user may have regarding Cryptocurrencies in their possession. Therefore, similar to the South African jurisdiction users that have invested Bitcoins as capital assets to acquire gains or losses may then incur Capital Gains Tax consequences. This position presents a very vital lesson for the Kingdom of eSwatini which currently does not apply Income Tax, regarding the application of Capital Gains Tax where Cryptocurrency gains have been acquired or losses incurred. Therefore, the position in the UK strengthens the notion that eSwatini should adopt Capital Gains Tax in their system to fall in line with advanced jurisdictions like the UK and South Africa. Consequently, if Capital Gains Tax is adopted, investments made by Bitcoin users may consequently be subject to Capital Gains Tax by the ERA curbing the problem of tax evasion.

Furthermore, a useful aspect about the position in the UK is that the approach followed by HMRC which focuses on the intention of the user and the nature of each specific transaction can provide valuable lessons and clarity for the ERA. Therefore, in order to be able to apply the appropriate Income Tax consequences on Cryptocurrency transactions, HMRC has set out a list of transactions that can attract Income Tax consequences. Thus if a user confirms transactions on a blockchain, when a user mines Bitcoin which results in rewards for the user, when salaries are paid to an individual and when Cryptocurrency is applied as an airdrop, these transactions may attract Income tax consequences in the UK. This approach is the same as that

adopted by the by SARS in South Africa where different transactions³⁹² that may occur through Cryptocurrency such as Bitcoin have been used as a guide on the application of normal tax for the South African jurisdiction. The approach from the two jurisdictions presents further lessons for eSwatini in the sense that when adopting suitable ways to apply tax and develop laws that will accommodate the technological developments it is vital to thoroughly understand the nature of how the transactions may occur.

5.5 Recommendations for the Kingdom of eSwatini

Having considered the different jurisdictions on the regulations and tax treatment of Cryptocurrency, the study now sets out recommendations that can add to policy for the eSwatini legal framework.

5.5.1 The financial regulatory framework

1. The CBE of eSwatini whilst still conducting research on emerging technologies, should adopt an interim regulatory framework in order to combat potential criminal activity associated with Cryptocurrency.
2. In developing regulations the CBE needs to formulate a more flexible regulatory framework on Cryptocurrency with the aim of accommodating the rapid development of Bitcoin and other Cryptocurrencies in the financial markets.
3. The CBE needs to formulate a more informative approach on Cryptocurrency in order to increase awareness amongst the general public not to fall victim to digital currency scams whilst still conducting research in the Kingdom of eSwatini.

5.5.2 The Tax legal framework

1. The ERA should change its current tax system from a source based tax regime to a much broader tax regime that will classify between tax on Swati residents and Non Swati residents further allowing the taxation of Swati resident's worldwide income.
2. The ERA, in formulating regulatory amendments to the current Tax legislation in eSwatini, should adopt an approach that will take into consideration the nature of the new and emerging financial technologies allowing flexibility on the rapidly changing nature of Cryptocurrency.

³⁹² Note 216, 217 and 218 (See paragraph 3.8 and 3.8.1).

3. Furthermore, the ERA in improving the Swati tax legislation should add Capital Gains Tax to enable the application of tax on the gains or losses from the disposal of capital assets.
4. The ERA should adopt an approach as that of South Africa and classify Cryptocurrencies as assets of intangible nature in order to be able to apply the proper tax rules on Cryptocurrency.
5. A further favourable approach by the ERA pursuant to an introduction of Capital Gains Tax into the Swati Tax legislation would be to add into and define Cryptocurrency under the definition of Financial Instrument to curb any tax avoidance of Capital Gains Tax.
6. Lastly the ERA should when enacting or amending legislation, adopt a broader sphere that will cover all Cryptoassets operating through distributed ledger technology.

5.6 Conclusion

The study has shown that in light of the emerging technologies there is a need to address the regulation and application of tax on Cryptocurrency. The need has been fueled by the anonymous nature of Bitcoin which has exposed a gap for criminal networks to make use of in conducting criminal activities. This has also prompted international organizations such as the OECD to assist countries in improving their tax rules and regulatory framework to fit Cryptocurrency into the development of their regulations. In addition, what must be noted is that countries such as eSwatini and South Africa have noted that Cryptocurrency has a potential if accepted to present a positive revolution in the financial markets thus there is a need to embrace the positive aspects about the technology and merge it into the current financial system.

The study has further examined different jurisdictions which include eSwatini, South Africa and briefly the USA and the UK in a bid to acquire lessons for eSwatini. A common feature on the jurisdictions is that the development of regulations on the Cryptocurrency depends mainly on their functioning in the virtual world. Furthermore, all the jurisdictions are still conducting research on what can be the best way of regulating Cryptocurrency given the fact that it is not tied to any jurisdiction or being monitored by a third party. Therefore there has been no final pronouncement by the above jurisdictions on the regulations that may be regarded as appropriate for the regulation of Cryptocurrency.

The tax treatment of Cryptocurrency has, however, taken a different direction as in all the discussed jurisdictions the already existing tax legal frameworks were confirmed to be applicable to the Cryptocurrency. The USA confirmed that Bitcoin is regarded as a convertible virtual currency and therefore the tax rules applicable to property apply on virtual currency. The UK on the other hand has classified Cryptocurrencies such as Bitcoin as exchange tokens which attract both Income Tax consequences and Capital Gains Tax. Furthermore, South Africa has classified Cryptocurrency typified by Bitcoin as assets of an intangible nature stating that normal tax rules apply to Cryptocurrency.

Having considered the position in the other jurisdictions, the study then drew lessons for the Kingdom of eSwatini. Therefore, a gap was identified in the Swati jurisdiction necessitating the need to improve the Swati tax legislation. Improvements identified as a necessity in this regard include the application of tax on worldwide income, and the introduction of Capital Gains Tax to the Swati tax legislation. In addition, the revenue authority seek to find a proper classification for Cryptocurrency which will aid in the application of tax on the new digital currencies.

Having discussed the different legal aspects in relation to the regulation and tax treatment of Cryptocurrencies typified by Bitcoin the study then comes to an end. However, for further research it has been identified that studies in relation to Cryptocurrency may for future purposes include a study of how to combat cross border tax evasion that may be a consequence of Cryptocurrency. This may be done by assessing current bilateral agreements on how they can be improved to address the question of cross border tax evasion.

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