Bitcoin Policy UK: Response to HMRC's Draft Legislation on Cryptoasset Loans and Liquidity Pools

Submitted by: Bitcoin Policy UK (BPUK)

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In response to: HMRC's technical consultation on draft legislation inserting new Part 4A (Cryptoassets etc.) into the Taxation of Chargeable Gains Act 1992, published 13 July 2026 as part of the Finance Bill 2026-27 draft legislation package.

Consultation deadline: 7 September 2026

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Executive Summary

HMRC is introducing 'no gain, no loss' (NGNL) capital gains tax treatment for qualifying cryptoasset lending, borrowing and automated market making (AMM) liquidity pool arrangements. In simple terms, entering these arrangements should not trigger a tax charge where the conditions are met. BPUK supports this approach. It reflects the position we have previously taken that lending Bitcoin should not be treated in the same way as disposing of it. [1]

Our concerns are mainly with how some of the conditions may work in practice. These include conditions that may exclude ordinary Bitcoin loans from the relief, the treatment of forfeited collateral where a borrower could face a tax charge despite being economically worse off, and the complexity of the rules around default and repayment. We also think the legislation should distinguish more clearly between native Bitcoin and wrapped or tokenised Bitcoin (wBTC), which have different characteristics and risk profiles.

The measure also does not address the separate issue of capital gains tax on everyday Bitcoin payments, which BPUK raised in its May 2026 response on stablecoins. [2]

Our Approach to This Response

This consultation is focused on whether HMRC's draft clauses work as intended, rather than on the policy question of whether Bitcoin lending or liquidity pool activity should be taxed. Our response is based on the following principles:

- Tax should follow the actual economic substance of the transaction.

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[1] Joint industry letter to the Chancellor of the Exchequer, "Tax inequality of DeFi lending and staking transactions," 5 February 2025: https://recap.io/blog/fair-tax-treatment-for-defi-lending-and-staking

[2] Bitcoin Policy UK, 6 May 2026, Response to HM Revenue and Customs Call for Evidence: Taxation of Stablecoins

- Bitcoin should only be distinguished from other cryptoassets where its mechanics affect how the legislation operates.
- We have tested whether the NGNL treatment works properly for Bitcoin lending and borrowing without creating unintended tax charges.
- Where the legislation already works correctly for Bitcoin, we say so.
- We have focused only on DeFi or cryptoasset technicalities that are relevant to Bitcoin.

1. What Works Well

The core approach works well. Where a Bitcoin holder lends BTC and receives BTC of the same type back, or provides BTC to a qualifying liquidity pool and later withdraws it, entering and exiting the arrangement is treated as no gain, no loss, and capital gains tax only arises when the holder disposes of the Bitcoin, for example by selling or spending it. This correctly reflects that lending Bitcoin is not the same as disposing of it, which has been BPUK's position since our 2024 DeFi consultation response, in which we said that treating cryptoasset lending as a disposal "is not reflective of the underlying economic activity or reality." [3]

Ordinary Bitcoin collateralised borrowing also works well as drafted: borrowing Bitcoin and later returning it does not, on its own, create a taxable gain or loss for the borrower, and collateral posted against a loan is correctly left out of account for tax purposes for as long as it remains returnable. This achieves HMRC's intended outcome.

We have also checked the drafting against Bitcoin's own technical characteristics. Bitcoin has no issuer, a fixed supply and settles on its own base layer. These characteristics do not create a problem for the core NGNL mechanism, which turns on whether a Bitcoin holder receives back cryptoassets "of the same type," not on the identity of any specific coin. We are satisfied that this test works correctly for Bitcoin and does not require different treatment from other qualifying cryptoassets.

Illustrative example: *a UK Bitcoin holder lends 1 BTC to a qualifying platform for six months and receives 1 BTC back at the end of the term, plus a return. Under the new rules, neither handing over the Bitcoin nor getting it back is treated as a disposal, so no capital gains tax is due at either point, regardless of how the Bitcoin price has moved in the meantime. Tax only becomes due if and when the holder actually sells or spends the Bitcoin. This is the outcome BPUK asked for, and the drafting delivers it in this straightforward case.*

2. Where the Drafting Falls Short of What We Asked For

The relief is conditional on tests that do not fit how Bitcoin lending actually works. The relief for lending arrangements only applies where the arrangement is "low risk of loss" and either between unconnected parties or "widely available." It is not clear how the 'low risk of loss' condition should be applied where the value of the underlying asset can move significantly over the life of the loan, including where that asset is Bitcoin. Recent high-profile failures in the sector, including Celsius, BlockFi and FTX, involved custodial, counterparty and management failures rather than movements in the price of Bitcoin alone. We therefore ask HMRC to clarify that significant price movements do not, by themselves, mean an arrangement fails the 'low risk of loss' test.

[3] Bitcoin Policy UK, 22 June 2024, [The Taxation of Decentralised Finance (DeFi) Involving the Lending and Staking of Cryptoassets]().

Bitcoin-backed lending can have a different risk structure from conventional unsecured lending because the lender may rely primarily on collateral adequacy and liquidation terms rather than the borrower's creditworthiness.

HMRC should clarify that the 'low risk of loss' test should consider the structure of the lending arrangement as a whole, including collateral adequacy, liquidation risk and counterparty risk.

Illustrative example: *a UK Bitcoin holder lends 1 BTC directly to a known counterparty against posted collateral. The arrangement includes defined collateral requirements and liquidation terms. If the value of Bitcoin falls significantly, this may affect collateral adequacy and could trigger a margin call or liquidation. However, that price movement should not alone determine whether the arrangement fails the 'low risk of loss' test. The assessment should consider how the loan is structured, including collateral, liquidation arrangements and counterparty risk.*

The treatment of forfeited collateral is not clear. Where a borrower loses Bitcoin collateral following a default, the drafting does not clearly show how any taxable gain should reflect the borrower's actual economic position. A borrower could face a tax charge when their collateral is taken, even though they have lost the Bitcoin and are worse off overall. We ask HMRC to clarify how these provisions are meant to interact, so that a borrower is not taxed on a gain that does not reflect what actually happened to them.

Illustrative example: *a borrower posts 1 BTC as collateral against a loan and later defaults. The lender seizes the collateral. If Bitcoin's price has risen between the borrower posting the collateral and the default being recognised, the drafting could treat the borrower as making a taxable gain on the forfeited Bitcoin, purely from the mechanics of how the acquisition and disposal values are calculated at different points in time, even though the borrower has, in reality, lost their Bitcoin and has no cash or other proceeds with which to pay any resulting tax bill.*

The drafting remains complex. HMRC's own stated aim for this measure is to reduce the "disproportionate administrative burdens" created by its 2022 guidance.[4] For a straightforward Bitcoin loan where the same amount is returned, the new rules simplify the tax treatment. The provisions covering default, partial repayment and collateral forfeiture remain dense and interlinked, and BPUK has previously criticised HMRC's DeFi proposals in similar terms, describing earlier drafting as "unnecessarily complex and littered with day-to-day complexities for the accountant trying to make sense of their client's activities." We ask HMRC to publish plain-English guidance with worked Bitcoin examples well ahead of the 6 April 2027 start date, developed with industry input.

3. Native Bitcoin versus Wrapped or Tokenised Bitcoin (wBTC)

The draft legislation does not clearly separate native Bitcoin from wrapped or tokenised representations of Bitcoin, such as wBTC. This distinction is important because they are not the same financial instrument. Native Bitcoin is a bearer asset with no issuer and no third party standing between the holder and the asset. Wrapped Bitcoin is a token issued by a custodian that holds the underlying BTC and represents a claim on it on a different, smart-contract-capable network. Holding wrapped Bitcoin therefore introduces custodial, bridge and issuer risks that do not apply to native Bitcoin; if the custodian fails, is compromised, or the bridge holding the underlying BTC is exploited, as has happened to wrapped-asset bridges elsewhere, the holder can lose their claim even though the underlying Bitcoin remains unaffected.

[4] HMRC, "Tax treatment of Cryptoasset Loans and Liquidity Pools" (policy paper), 13 July 2026: https://www.gov.uk/government/publications/cryptoasset-loans-and-liquidity-pools/tax-treatment-of-cryptoasset-loans-and-liquidity-pools

Bitcoin's base layer does not support the type of smart contracts used by liquidity pools. In practice, where 'Bitcoin' is used in an automated market making pool, it is usually wrapped Bitcoin rather than native Bitcoin. On our reading, the drafting may allow wrapped Bitcoin to receive the same NGNL tax treatment as native Bitcoin when used in a liquidity pool, because a token representing a claim on Bitcoin can fall within an exception in the definition of "qualifying cryptoasset." We do not think this is necessarily wrong, but tax treatment should not be the only place this distinction is drawn. If wrapped Bitcoin and native Bitcoin receive the same tax treatment without clear guidance on their different risks, users may be steered toward wrapped Bitcoin, and its additional custodial risk, solely to access a liquidity pool that Bitcoin's base layer cannot support. We recommend that HMRC guidance clearly distinguish native Bitcoin from wrapped or tokenised Bitcoin, explain how each is treated, and make clear that equal tax treatment does not mean equal risk.

4. Transitional Issues

The measure takes effect from 6 April 2027. HMRC has confirmed that it is still considering whether the new rules should apply to lending and liquidity pool positions already open on 6 April 2027, rather than only to arrangements entered into after that date.[5] This matters in practice because a Bitcoin holder with an open lending position spanning 6 April 2027 could have been treated as making a disposal when the arrangement was entered into under the old rules, even though the same arrangement entered into after that date would not be. That would create an inconsistent outcome and could encourage people to unwind and re-enter positions purely to access the new treatment, adding unnecessary complexity.

5. What This Measure Does Not Address

This measure does not address the CGT treatment of everyday Bitcoin payments, which BPUK addressed separately in our May 2026 response to HMRC's call for evidence on the taxation of stablecoins. [6] In that response, we recommended a full CGT exemption for retail Bitcoin payments because the current rules create a disproportionate compliance burden while raising negligible tax revenue.

The reforms in this consultation improve the tax treatment of Bitcoin lending and borrowing, but a Bitcoin holder using Bitcoin for everyday goods and services remains subject to the current CGT rules. We ask HMRC to confirm whether, and on what timeline, the CGT treatment of everyday Bitcoin payments will be addressed separately.

These are two separate issues. This consultation deals with Bitcoin that is temporarily transferred and later returned, without changing the underlying holding period. The payments question deals with Bitcoin that is permanently transferred in exchange for goods or services, regardless of the size of the transaction. HMRC has separately confirmed favourable treatment for eligible stablecoins because of their payment function, while indicating that Bitcoin is outside the scope of that reform. BPUK does not view this as HMRC's final position on Bitcoin payments, and we continue to support the case made in our May 2026 submission, but this measure should not be taken as resolving the separate issue of Bitcoin payments.

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[5] HMRC, 'Taxation of Stablecoins' (call for evidence outcome), 13 July 2026, confirming that the government is still assessing whether the new rules for cryptoasset loans and liquidity pools should have retrospective effect for a limited period. https://www.gov.uk/government/calls-for-evidence/cryptoasset-taxation-stablecoins/outcome/taxation-of-stablecoins

[6] Bitcoin Policy UK, 6 May 2026, Response to HM Revenue and Customs Call for Evidence: Taxation of Stablecoins.

Summary of Recommendations

- Confirm that movements in the value of Bitcoin should not, in isolation, determine whether an arrangement is ‘low risk of loss’. The assessment should consider the lending arrangement as a whole, including collateral adequacy, liquidation terms, counterparty risk and custody.
- Clarify how any taxable gain should be treated when a borrower’s collateral is forfeited, so that the tax outcome reflects the borrower’s economic position.
- Publish plain-English guidance with Bitcoin-specific examples covering default, partial repayment and collateral forfeiture before 6 April 2027.
- Clearly distinguish native Bitcoin from wrapped or tokenised Bitcoin (wBTC) in guidance, and confirm that equal tax treatment does not mean equal risk.
- Provide transitional relief for Bitcoin lending and liquidity pool positions that remain open on 6 April 2027.
- Confirm when HMRC will address the CGT treatment of everyday Bitcoin payments, as raised in BPUK’s May 2026 stablecoins submission.

A Note on Scope

This response focuses on the points where BPUK has a clear, evidence-based view. It does not comment on every clause of the draft legislation or address DeFi or cryptoasset questions that are not directly relevant to Bitcoin. This response should be read alongside BPUK’s June 2024 DeFi consultation response and our May 2026 stablecoins response, which address related but separate issues.

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