8 Misconceptions Crypto Investors Face and How to Avoid Them!

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Introduction

Investing in cryptocurrency can be thrilling—markets move fast, new tokens launch daily, and the potential for profit seems endless. However, with rapid growth comes equally rapid complexities, especially when it comes to taxes and regulatory rules. Many investors dive into the crypto world without a clear understanding of the tax implications or the responsibilities that come with this new digital asset system.

Much like influencers who suddenly find themselves managing businesses, crypto investors often don’t have all the guidance they need from the start because the rules around cryptocurrency are evolving. So, it’s easy to get trapped in the common misconceptions. Mistakes can lead to costly tax bills or even penalties, but there’s good news: by educating yourself now, you can avoid the most common issues and protect your investments.

In this guide, we’ll break down the 8 misconceptions that crypto investors often fall for. Each issue will be explained in clear terms, including practical steps to avoid downsides and maximise your gains in a tax-compliant way. So, even if you’re new to crypto or an expert investor, this guide will help you understand the regulatory landscape and make sure that your investments are managed smartly.

Ready? Let’s dive in!

1 Misconception – Tax is Only Owed When Exchanging to Fiat (Traditional Currencies)

Many believe that taxes only apply when crypto is converted to fiat, such as, USD/EUR. In reality, taxable events occur even when trading from one cryptocurrency to another.

Solution

Be aware that each trade does trigger a taxable event. Keep detailed records of your transactions to simplify reporting and avoid underpayment.

2 Misconception – Crypto That is Lost Can Be Claimed as a Tax Deduction

Many believe that if crypto is stolen, they can write it off on their taxes. However, HMRC does not allow theft losses to be claimed for CGT purposes.

Solution

Maintain strong security practices. If your crypto is stolen, keep detailed evidence because it may help in legal claims or future policy changes. However, don't rely on deducting those losses unless rules change.

3 Misconception – Receiving Income in Crypto is Exempt from VAT

Some investors assume that because they're paid in digital currency, they won't need to pay VAT. However, VAT can still apply in many cases, particularly in certain services or goods transactions.

Solution

Check the VAT laws applicable to crypto and work with a tax advisor to ensure that you're not surprised by unexpected tax bills.

4 Misconception – Shopping Items With Crypto is Exempt from Tax

Buying items with crypto doesn't eliminate tax obligations. Such purchases trigger a taxable event, as it's seen as selling or disposing of an asset.

Solution

Consult a tax advisor to understand the implications of using crypto for purchases and set aside funds for any resulting tax liability.

5 Misconception – Using a Company is More Tax Efficient

Many investors believe that holding crypto will result in lower taxes. While this can be true for traditional assets, crypto assets often work differently. When it comes to tax treatment of crypto, and setting up a company without a full understanding of the rules can lead to higher tax rates and compliance costs. For example, when crypto is held within a company, any gain is taxed at the UK corporation tax rate (25%), not the Capital Gains Tax (CGT) rates which are only applicable to individuals depending on your overall tax bracket. Furthermore, companies do not receive the Capital Gains Tax annual exemption, (£3,000) whereas individuals do receive this benefit.

Additionally, another point to address is that once a company has paid corporation tax on their crypto capital gains, they can also extract the net gain from the company through dividends. The issue here is that you are effectively paying dividend tax on the amount you want to extract, resulting in double taxation.

Solution

Consider speaking to a tax advisor specialising in crypto. In some cases, remaining an individual investor is simpler and more tax-efficient than incorporating a company.

6 Misconception – Swapping Crypto is Not Subject to Tax

A key misconception with crypto investors is that when you simply exchange one cryptocurrency for another (such as swapping Bitcoin for Ethereum) creates no taxable event.

However, under UK tax law, any disposal of a crypto asset is treated as a taxable event, and this includes exchanging between different assets. When you perform the exchange, HMRC requires you to calculate the capital gain or loss based on the market value of the asset you gave up (in GBP) at the time of the transaction. For example, you purchased Ethereum worth £1,000 but later swapped it for Bitcoin when Ethereum had a market value of £3,000. Although you didn't receive any cash, you still made a £2,000 gain at the time of the transaction, which is a taxable event.

It is common that people fail to recognise this, which can lead to underreporting taxable gains, unexpected tax liabilities, and even penalties. Therefore, it's essential for crypto investors to understand that tax doesn't always just apply when we "cash out", it also can apply when we exchange or swap from one crypto asset for another.

Solution

Stay on top of your portfolio and utilise strategies like tax-loss harvesting if allowed in your jurisdiction. In addition, using Crypto tax software's such as Koinly are a great way of accounting for every transaction.

7 Misconception – All Crypto Received Falls Under Capital Gains Tax

Not all crypto income is treated equally. Depending on how it's earned—through staking, mining, or simply holding—it may fall under Capital Gains tax or Income tax, including income tax in some cases.

Solution

Research the specific tax treatment for different crypto activities in your country. Consulting a tax expert or accountant can make sure that you're classifying and reporting your income correctly.

8 Misconception – Disposing of Crypto Assets While Gifting to Spouse

When disposing of crypto assets in the UK (gifting to a spouse, or paying transaction fees), capital gains tax (CGT) must be calculated. Mostly people overlook the key considerations (transaction fees as separate disposals, pooling rules for cost calculations, and new tax reporting requirements from 2024/25).

Solution

To minimise capital gains tax (CGT) on crypto disposals in the UK, individuals can utilise several strategies. Firstly, the Spousal Transfer Exemption allows tax-free transfers of crypto assets between spouses— this enables both partners to use their CGT exemptions effectively. This transfer is done at cost and therefore can result in significant tax benefit if utilised efficiently. Also, by claiming Allowable Costs, such as transaction fees, legal expenses, and marketing costs, one can further reduce taxable gains.

Bottom Line

Reporting Capital Losses makes sure that losses can be carried forward and offset against future gains, lowering overall tax liability. Lastly, using HMRC's Voluntary Disclosure service helps correct any underpaid taxes from previous periods; this prevents potential penalties.