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Mr Dexter Marcenko
Director
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Australian Taxation Office

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2 October 2026

Dear Dexter,

TD 2026/D2 Income tax: capital gains tax consequences of using a smart contract to wrap and unwrap crypto assets

CPA Australia is Australia's leading professional accounting body and one of the largest in the world. We represent the diverse interests of more than 176,000 members in over 100 countries and regions. We make this submission on behalf of our members and in the broader public interest in response to the ATO's draft **TD 2026/D2 Income tax: capital gains tax consequences of using a smart contract to wrap and unwrap crypto assets** (draft TD).

Executive summary

CPA Australia appreciates the Australian Taxation Office's (ATO) efforts to provide clarity in the rapidly evolving digital asset ecosystem. However, we submit that the Commissioner's preliminary view that wrapping or unwrapping a crypto asset triggers a capital gains tax (CGT) event, generally CGT event C2, or potentially another CGT event on an alternative analysis, warrants reconsideration. The CGT outcome should depend on the legal rights created by the particular protocol, including whether ownership of the locked asset has ended, rather than on control of a blockchain address alone. The final determination should also explain the potential application of sections 106-50 and 106-60 of the *Income Tax Assessment Act 1997*, consider relevant judicial developments, and address disproportionate tax and compliance outcomes through appropriately targeted legislative relief and practical compliance guidance.

Key comments and recommendations

We make the following key comments and recommendations:

- The draft TD should adopt a protocol-specific analysis of the legal rights created by a wrapping arrangement, including the identity and legal capacity of relevant parties, the wrapped-token holder's redemption rights and whether ownership of the locked asset has ended.
- The ATO should explain the potential application of sections 106-50 and 106-60. Section 106-50 should be considered only where an identifiable trustee holds the asset on trust and the beneficiary is absolutely entitled to that asset as against the trustee. Section 106-60 should be considered separately by reference to whether the arrangement creates or maintains a security, charge or encumbrance over the asset.
- Finalisation should be deferred until the High Court delivers judgment in *Poulton v Conrad*, so the ATO can consider whether the Court's reasoning affects the draft TD.
- If the Commissioner maintains that a CGT event occurs, the ATO should refer to Treasury the need for targeted legislative relief, such as replacement-asset rollover relief or a carried-over cost-base rule for qualifying technical token conversions.
- The ATO should also consider a practical compliance approach addressing valuation, record keeping and low-risk technical transactions, without purporting to alter substantive CGT liability.

Please refer to the Appendix for our detailed discussion. If you have any queries, please contact me at jenny.wong@cpaaustralia.com.au or Bill Leung, Tax Technical Advisor, at bill.leung@cpaaustralia.com.au.

Yours sincerely,

Jenny Wong
Tax Policy Lead

Appendix

Detailed discussion

Introduction
CPA Australia welcomes the opportunity to provide comments on Draft TD 2026/D2. Our submission focuses on whether wrapping and unwrapping crypto assets should give rise to CGT consequences, and on the broader legal, practical and policy implications of treating technical token conversions as taxable disposal events.

The concept of abandonment and continuing proprietary rights
The draft TD considers that ownership of the native crypto asset ends when it is transferred to and locked by the wrapping contract, with CGT event C2 occurring. That conclusion should depend on the legal rights and obligations created by the particular arrangement, rather than control of the relevant blockchain address alone.

Programmatic rights: Depositing native tokens into an autonomous wrapping contract does not necessarily amount to abandonment. The holder of the corresponding wrapped token will generally have a protocol-based right to redeem the underlying asset on a 1:1 basis, subject to the contract terms, continued operation of the protocol and the holder retaining the wrapped token.

Lack of a conventional counterparty: A smart contract is code and is not itself a legal person capable of owning property or acting as trustee. Nevertheless, the absence of a conventional intermediary does not, by itself, establish that the depositor retains legal or beneficial ownership. The analysis should identify any person or entity that controls, administers or has enforceable obligations under the arrangement and determine the proprietary effect of the protocol as a matter of law.

The draft TD treats the loss of direct private-key control over the locked token as relevant to whether the taxpayer's ownership has ended. However:

- Section 106-50 of the *Income Tax Assessment Act 1997* can apply only if there is a trust, an identifiable trustee and a beneficiary who is absolutely entitled to the relevant CGT asset as against the trustee.
- A smart contract is code and cannot itself undertake the legal obligations of a trustee. The analysis must therefore identify whether a person or entity holds the locked asset on trust and whether the wrapped-token holder has the rights necessary to be absolutely entitled to that asset as against the trustee.
- Fungibility, pooled reserves and transferability of the wrapped token may complicate absolute entitlement and the identification of the relevant CGT asset. These features should be examined under the protocol terms and applicable trust law; they should not be treated as conclusively establishing or excluding absolute entitlement.
- Where the facts establish a trust and absolute entitlement, section 106-50 treats acts done by the trustee in relation to the asset as acts of the beneficiary. Where those requirements are not met, the analysis must instead turn on the nature and continuity of the taxpayer's proprietary rights under the particular arrangement.

Section 106-60: The final determination should separately explain whether section 106-60 is relevant. That provision concerns the vesting of a CGT asset, and acts done in relation to it, for the purpose of enforcing, giving effect to or maintaining a security, charge or encumbrance. Its application therefore depends on whether the particular wrapping arrangement creates such an interest over the locked asset and, if so, on identifying the entities whose acts are treated as relevant for CGT purposes. The analysis should not conflate section 106-60 with absolute entitlement under section 106-50.

Relevance of *Poulton v Conrad*
The draft TD places weight on control through a private key when analysing ownership. That factor is relevant but should not be treated as determinative without considering the wider proprietary rights created by the arrangement.

Poulton v Conrad: The High Court proceeding concerns whether Bitcoin is property capable of possession and the application of the torts of conversion and detinue. It does not directly determine the CGT consequences of

wrapping or the application of section 106-50. However, the Court's reasoning may inform the broader legal characterisation of control and proprietary interests in digital assets. Deferring finalisation until the judgment is available would allow the ATO to consider whether any aspect of that reasoning requires the draft TD to be revised.

Form versus economic substance
The statutory CGT analysis must be grounded in the legal rights created by the transaction. Commercial and economic consequences nevertheless remain relevant when assessing whether the draft interpretation produces coherent outcomes and whether a policy response is required.

Economic equivalence: ETH and WETH are designed to be redeemable on a 1:1 basis and ordinarily provide closely aligned economic exposure. Their market values may, however, diverge because of liquidity, protocol, smart-contract or market risk. Conversion between them is commonly a technical step required to interact with decentralised protocols. That commercial function does not determine the CGT outcome, but it supports distinguishing standard 1:1 wrapping from transactions that materially alter the taxpayer's rights or economic exposure.

The draft TD characterises the locking of the token as the ending of ownership (CGT event C2):

- The holder does not retrieve the locked asset merely by controlling the original wallet's private key. Redemption ordinarily requires the holder to control and surrender or burn the corresponding wrapped token and to interact successfully with the contract.
- Because the wrapped token is transferable, the original depositor may cease to hold the redemption right. Any analogy with bailment, custody or a warehouse receipt must therefore be tested against the protocol terms and the legal character of the rights held at the relevant time, rather than treated as conclusive.

No cash proceeds or material economic disposal: The draft treatment may require taxpayers to recognise a capital gain or loss even though they receive no cash and retain substantially similar economic exposure. We acknowledge that the CGT provisions can produce a statutory realisation event without cash proceeds. Our concern is that repeated CGT events for standard 1:1 wrapping and unwrapping may impose tax and compliance consequences disproportionate to the commercial substance of the interaction.

Paragraph 48 and the 'nil cost base' issue
Paragraph 48 of the draft TD states that recognising a continuing property interest in the locked asset may produce a nil cost base for the wrapped token. That material consequence requires a clear legal explanation but should not determine whether ownership of the locked asset has ended. The final determination should explain how the cost-base rules apply to each asset under the competing legal characterisations. If the legislation produces an inappropriate outcome for qualifying 1:1 technical conversions, the ATO should refer the issue to Treasury for consideration of targeted relief, such as a carried-over cost-base rule or replacement-asset rollover.

Practical and administrative implications
If finalised in its current form, TD 2026/D2 may create significant administrative burdens:

Compliance burden: Some DeFi protocols wrap and unwrap tokens automatically or frequently as part of a broader transaction. Treating each interaction as a separate CGT event would require taxpayers to identify the time and Australian-dollar market value of each event and maintain corresponding cost-base records. Where transaction volumes are high, this may create significant record-keeping and valuation burdens.

Liquidity effects: Treating wrapping as a disposal at market value may give rise to tax on an accrued gain even though the taxpayer receives no cash or third-party consideration. A taxpayer may therefore need to fund the liability from other resources or dispose of assets. This possible liquidity effect reinforces the need for clear valuation guidance and, where the policy outcome is considered inappropriate, targeted legislative relief.

Data fragmentation: Third-party tax software may not consistently identify automated wrapping transactions or maintain accurate cost-base records across protocols and blockchains. Clear guidance on valuation, transaction identification and cost-base treatment would reduce error and compliance costs.

Broader economic effects: Some DeFi applications may execute numerous wrapping and unwrapping operations within automated workflows. Treating each operation as a separate CGT event may:

- substantially increase the number of transaction records and valuation points for investors and digital-asset businesses; and
- discourage the use and development of compliant DeFi services in Australia unless the resulting tax and compliance outcomes are clearly explained and proportionate.

These consequences support two distinct responses. First, the final determination should distinguish standard technical wrapping from arrangements that materially change legal rights or economic exposure. Secondly, the ATO should provide practical guidance on transaction identification, valuation and record keeping, together with a compliance approach for low-risk transactions that operates within the legislation. Any substantive tax neutrality should be provided through targeted legislative relief.

Recommendations

CPA Australia recommends that the Commissioner:

1. *Adopt a protocol-specific ownership analysis:* Revise the draft TD so that the CGT outcome depends on the legal rights created by the particular arrangement. The analysis should identify the relevant parties and their legal capacity, the wrapped-token holder's redemption rights and whether ownership of the locked asset has ended.
2. *Clarify sections 106-50 and 106-60:* Explain when each provision may apply and how it interacts with the ATO's ownership analysis. Section 106-50 should be considered only where an identifiable trustee holds the asset on trust and the beneficiary is absolutely entitled to that asset as against the trustee. Section 106-60 should be considered separately by reference to whether the arrangement creates or maintains a security, charge or encumbrance over the asset and the CGT consequences prescribed by that provision.
3. *Defer finalisation:* Defer finalisation until the High Court delivers judgment in *Poulton v Conrad*, and then consider whether the Court's reasoning on possession, control and proprietary interests in digital assets affects the draft TD.
4. *Refer legislative relief to Treasury:* If the Commissioner maintains that a CGT event occurs, refer to Treasury the need for targeted relief for qualifying technical token conversions, such as replacement-asset rollover relief or a carried-over cost-base rule.
5. *Publish a practical compliance approach:* Provide guidance on transaction identification, valuation and record keeping, together with an administrative approach for low-risk standard wrapping and unwrapping transactions that operates within the legislation and does not alter substantive CGT liability.