

Accounting for Crypto-assets Held on Behalf of Others

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Crypto trading platforms (“Platforms”) facilitate the buying and selling of crypto assets and may also perform functions similar to one or more of exchanges, alternative trading systems, clearing agencies, custodians and dealers¹. Platforms allow clients to trade crypto assets for other assets, such as fiat money, or for other crypto assets. They also regularly hold crypto assets in a custodian capacity, securely store and protect the crypto assets for clients. The terms and conditions for such arrangements can vary significantly.

Platforms store crypto assets for clients in a shared (commingled) wallet or in segregated wallets for each individual client. Each wallet has corresponding public and private keys that are generated together as part of the private-public key pairs. A public blockchain address is the identification (ID) where the crypto assets are held and a possible destination of crypto assets, functioning like an e-mail address. A public blockchain address is a shortened version of the public key. A shared wallet is where the same wallet is used to facilitate transactions relating to multiple clients. A separate wallet may be used to facilitate transactions for each individual client on the blockchain.

Private keys are secure passcodes used to unlock and spend crypto assets belonging to a specific blockchain wallet address. Private keys are stored in either software wallets or hardware wallets, also known as “hardware security modules”. Software and hardware wallets keep the private keys safe using encryption and allow for the signing of transactions after the user has entered the correct password to access the private key.

The Group discussed factors to consider when assessing whether crypto assets held by the Platform on behalf of others should be recognized in the Platform’s statement of financial position.

Issue 1: What considerations should be made in assessing whether a Platform should record the client crypto assets in its statement of financial position?

Analysis

Current IFRS Standards do not directly provide guidance on whether an entity’s holding of crypto assets on behalf of others should be presented on its statement of financial position. Therefore,

¹ Canadian Securities Administrators. “[Joint Canadian Securities Administrators/Investment Industry Regulatory Organization of Canada Staff Notice 21-329 Guidance for Crypto-Asset Trading Platforms: Compliance with Regulatory Requirements.](#)” March 29, 2021. The CSA’s document provides guidance on how Canadian securities legislation applies to Platforms facilitating or proposing to facilitate trading of contracts involving crypto assets or crypto assets that are securities or instruments.

entities should consider the guidance in [IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors](#) when developing an accounting policy for such assets.

The accounting for the crypto assets held by Platforms is either on balance sheet as a crypto asset with a corresponding liability, or off balance sheet for the crypto assets to be considered “held-in-trust” for their clients. The on-balance-sheet treatment is consistent with how banks and brokers account for customer’s cash deposits. The off-balance-sheet treatment is consistent with how brokers account for stocks and bonds held on behalf of their customers.

Therefore, as with traditional custodians of client money, the assessment should focus on the concepts of “control” and “benefits”. The Platform should assess whether it is subject to substantial risks and rewards incidental to asset ownership. To determine this, the Platform should consider the terms of the agreement with its clients, the laws governing the jurisdiction(s) in which it operates and how it manages and stores crypto assets held on behalf of clients. Some of the considerations include:

- (a) local laws and regulations, in particular those around legal ownership of assets held by others;
- (a) the extent to which the parties’ rights and obligations are clear or contractually enforceable;
- (b) analysis of which party has legal title to the asset;
- (c) the status of the crypto assets in the event of the custodian’s bankruptcy or insolvency (i.e., are the crypto assets available to satisfy general claims from the custodian’s creditors in the event of its bankruptcy);
- (d) the contractual limitations on the custodian’s use and transfer of the crypto assets, including whether the custodian is required to keep matching holdings of crypto assets at all times;
- (e) whether the entity has the ability to “borrow” the crypto asset and use it for its own purpose or to lend the crypto assets to third parties;
- (f) whether the arrangement allows for commingling client and custodian crypto assets (i.e., is the custodian required to keep its clients’ crypto assets in a different digital wallet from its own crypto assets);
- (g) whether crypto assets held on behalf of others are held in an account/wallet of the entity or in an account/wallet at a third party (i.e. a sub custodian);
- (h) traceability to a dedicated blockchain address (not all transactions can be individually traced to a dedicated blockchain address);
- (i) whether regulatory or contractual requirements are imposed on the custodian regarding appropriate record keeping and internal controls;
- (j) whether the agreement with the client is clear that the custodian is holding the crypto assets in the capacity of an agent and whether the substance of the arrangement is consistent with an agents rights and responsibilities;

- (k) whether the access to clients' crypto assets require a multi-signature authorization by both the client and the custodian, or whether the custodian has unilateral access to the private key; and
- (l) whether the custodian bears the security risk (i.e., is the custodian obligated to reimburse the client for any crypto assets lost in a security breach).

The Group's Discussion

Most Group members agreed with the analysis. They analogized crypto assets to client money and agreed the assessment should focus on whether the Platform is acting in the capacity of the principal and is subject to substantial risks and rewards incidental to ownership of the crypto assets. One Group member analogized crypto assets as non-cash collaterals and thought the Platform could consider the guidance in [paragraph 3.2.23](#) of IFRS 9 *Financial Instruments* to account for the non-cash collateral when accounting for these assets.

Several Group members emphasized the importance of the control assessment in the Platform's accounting for crypto assets and thought the considerations included in the analysis are useful in this assessment. They observed that the Platform's client agreements are often complex and unique to each transaction. In addition, some Group members noted that some Platforms may operate in both banking like and broker like models. Therefore, they noted that Platforms should review these agreements in detail to understand each party's rights and obligations and whether these contractual rights are enforceable when assessing control. A representative from the Canadian Securities Administrators (CSA) commented that some client agreements may appear to provide rights to clients that indicate the Platform is acting in an agent capacity. However, when considering other factors identified in the analysis, this may not be the case. For example, to assess the legal ownership of crypto assets, the Platform needs to consider where these assets are stored to determine whether the client's rights are enforceable under the local law. Given the complexity and technical nature of client agreements, a legal opinion may be needed in the control assessment.

In addition to the factors listed in the analysis, one Group member noted that another factor to consider in the control assessment is the Platform's ability to safeguard crypto assets stored against potential hacks or breaches of data.

Issue 2: Should the Platform record client crypto assets in its statement of financial position in the following Fact Patterns?

Fact Pattern 1

- Entity A is a Canadian Platform that hosts crypto wallets and offers exchange services.
- Entity A's Client Agreement stipulates that Entity A:
 - (a) offers a shared wallet (commingled) as opposed to segregated wallets and uses shared blockchain addresses;

- (b) can, at its discretion at any time, apply any of the funds and digital assets allocated to the client's account to set-off or satisfy any amounts the client may owe to Entity A;
 - (c) is not prohibited from lending the crypto assets out to other parties, or from making use of the crypto assets while they are in its possession;
 - (d) accepts no liability for losses that an entity may incur related to its action or inaction around certain activities involving the crypto assets, including security-related risks.
- Entity A obtained a legal opinion which indicates that the crypto assets would be available to settle general claims from Entity A's creditors in the event of bankruptcy.

Analysis

A commingled wallet presents higher risks for clients because the deposited crypto assets originally allocated to one client could be used to benefit another client or Entity A itself. Further, the legal opinion supports that the crypto assets are available for general claims from Entity A's creditors in the event of bankruptcy.

The factors above and the absence of language in the Client Agreement limiting the use and transfer of the crypto assets, imposing appropriate record keeping and other terms indicate that Entity A is holding the crypto assets in the capacity of a principal. Thus, Entity A is subject to substantial risks and rewards incidental to ownership of the assets under its control. Therefore, Entity A should record the client crypto assets in its statement of financial position with an offsetting liability representing the obligation to the client.

An analogy of this accounting treatment can be drawn to how a bank presents its client's cash. The cash is commingled in the bank's account with the Bank of Canada. It is available to the bank to lend out for mortgages, lines of credit, credit cards, and other investments. The cash is presented on the bank's balance sheet, with an offsetting customer liability.

Where significant judgments have been made in determining whether Entity A should recognize the client crypto assets in its statement of financial position, Entity A should provide disclosure in accordance with [paragraph 122](#) of IAS 1 *Presentation of Financial Statements*.

The Group's Discussion

Most Group members agreed with the analysis presented in the Fact Pattern. They noted that Entity A is holding crypto assets in the capacity of a principal and should record the client crypto assets in its statement of financial position.

One Group member thought the crypto assets should not be analogized to cash given they are not cash instruments. Instead, this Group member analogized crypto assets as non-cash collateral and thought they should be disclosed on the Platform's financial statements and only be recognized as an asset when the Platform uses them.

Fact Pattern 2

- Entity B is a Canadian Platform that hosts crypto wallets and offers exchange services.
- Entity B's Client Agreement stipulates that Entity B:
 - (a) offers a shared wallet (commingled) as opposed to segregated wallets and uses shared blockchain addresses;
 - (b) Records the ownership of crypto assets will be clearly recorded in its books and records as belonging to the client and stored in a custody account on behalf of the client, and that the records will at all times identify the client's crypto assets separately;
 - (c) has no rights, interest or title to the crypto assets;
 - (d) Will use none of the crypto assets in connection with any loan, lien or claim; and
 - (e) Is the custodian and the sole entity with access to the private key. The client must authorize all transactions, but Entity B will only act on its clients' direction.
- Entity B obtained a legal opinion which supports that the crypto assets are not available to settle general claims from Entity B's creditors in the event of bankruptcy.

Analysis

Although Entity B uses a commingled wallet, separate record keeping allows for the separate identification of the client's crypto assets. Furthermore, the language in the Client Agreement specifies that the client must authorize all transactions, and the custodian can only act on the direction of the client. These factors indicate that Entity B is holding the crypto asset in the capacity of an agent.

Therefore, despite the arrangement allowing for comingling of crypto assets in the wallet, Entity B is not subject to substantial risks and rewards incidental to ownership of the assets given that it is acting in its capacity as an agent. Therefore, Entity B should not record the client crypto assets in its statement of financial position.

An analogy of this accounting treatment can be drawn to the broker's accounting for the securities it holds on-behalf of its clients. For example, a broker may hold a client's securities that are commingled with other clients' securities in a Canadian Depository for Securities (CDS) account. Although the CDS recognizes the broker as the owner of the securities, the broker maintains client sub-ledgers clearly identifying each client's ownership in the pool of securities. In addition, the broker is not authorized to transact using the client's securities without the client's approval. Therefore, the securities belong to the clients and are not recorded on the broker's balance sheet, even though these securities are in a commingled CDS account.

Where significant judgments have been made in determining whether Entity B should recognize the client's crypto assets in its statement of financial position, Entity B should provide disclosure in accordance with [paragraph 122](#) of IAS 1.

The Group's Discussion

Group members agreed with the analysis.

A representative of the CSA noted that even though the crypto assets are not presented on Entity B's balance sheet, given the importance of these managed assets to Entity B's performance, it should consider whether additional information needs to be included in a note in its financial statements. Information such as the types of clients' assets may provide useful information to financial statement readers.

One Group member commented that the custodian of the crypto assets is providing a service. Thus, the entity should analyze this service under [IFRS 15 Revenue from Contracts with Customers](#) and provide required disclosures.

The Group's discussion of these issues raises awareness about the factors a Platform should consider when assessing whether it has control over client's assets. Given the prominence of crypto assets in the market, one Group member highlighted the need for the IASB to develop standards specifically for crypto currencies. Staff from the AcSB commented that the topic of accounting for crypto currency is highlighted as a priority project in the AcSB's response letter to the IASB's agenda consultation request. No further action was recommended to the AcSB.