IFRS

STAFF PAPER

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IFRS® Interpretations Committee meeting

Project	**Holdings of cryptocurrencies**
Paper topic	Item for continuing consideration

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Introduction

1. At its meeting in September 2018, the IFRS Interpretations Committee (Committee) discussed holdings of cryptocurrencies in response to a request for advice from the International Accounting Standards Board (Board). At that meeting, the Committee discussed:

   (a) how an entity might apply IFRS Standards in determining its accounting for holdings of cryptocurrencies and initial coin offerings;

   (b) whether the application of IFRS Standards provides users of financial statements with useful information about holdings of cryptocurrencies; and

   (c) whether standard-setting is needed and should be a priority for holdings of cryptocurrencies.

2. The Board discussed the Committee's advice at its meeting in November 2018. At that meeting, the Board decided not to add to its work plan a project on holdings of cryptocurrencies or initial coin offerings, but instead to monitor developments regarding cryptoassets.

3. The Board also decided to ask the Committee to consider publishing an agenda decision that would explain how IFRS Standards apply to holdings of cryptocurrencies, including consideration of applicable disclosure requirements.

4. The purpose of this paper is to ask the Committee whether it agrees with our recommendation to publish a tentative agenda decision on holdings of cryptocurrencies.

Structure of the paper

5. The paper includes:

   (a) background information (paragraphs 7–9);

   (b) September Committee discussion (paragraphs 10–28);

   (c) November Board discussion (paragraphs 29–31); and

   (d) staff analysis and recommendation (paragraphs 32–35).

6. Appendix A to this paper includes the proposed wording of the tentative agenda decision.

Background information

7. Investopedia defines a cryptocurrency as 'a digital or virtual currency that uses cryptography for security. A cryptocurrency is difficult to counterfeit because of this security feature. Many cryptocurrencies are decentralized systems based on blockchain technology, a distributed ledger enforced by a disparate network of computers… [a cryptocurrency] is not issued by any central authority, rendering it theoretically immune to government interference or manipulation.' [1]

8. We consider cryptocurrencies to be a specific type of asset that is part of a broader asset class known as cryptoassets. A cryptoasset is a digital asset class that includes assets recorded on a blockchain. A cryptoasset could be intended for use as a medium of exchange (eg cryptocurrencies) or may be an asset that provides the holder with particular rights (eg crypto tokens).

[1] https://www.investopedia.com/terms/c/cryptocurrency.asp

9. The scope of the analysis requested by the Board did not extend beyond holdings of cryptocurrencies. Additional analysis would be necessary if the scope of the Board's work were to extend to other types of cryptoassets.

September Committee discussion

Applying IFRS Standards to holdings of cryptocurrencies

10. We provided the Committee with a staff analysis of the application of IFRS Standards to holdings of cryptocurrencies in paragraphs 7–67 of Agenda Paper 4A to the Committee's September 2018 meeting.

Cash or another financial asset

11. As explained in that analysis, we think an entity does not account for holdings of cryptocurrencies as cash or another financial asset. This is because cryptocurrencies do not currently have the characteristics of cash nor do they meet the definition of a financial asset in IAS 32 *Financial Instruments: Presentation*.

12. Regarding cash, AG3 of IAS 32 states that 'currency (cash) is a financial asset because it represents the medium of exchange and is therefore the basis on which all transactions are measured and recognised in financial statements'. This description implies that cash is expected to be a medium of exchange (ie widely-used in exchange for goods or services) and a unit of account (ie used as the monetary unit in pricing goods or services). Although some cryptocurrencies can be used in exchange for some goods or services, we are not aware of any that are used as a unit of account.

13. If the use of a particular cryptocurrency evolved to such an extent that it was widely used as a medium of exchange and unit of account, we think an entity would then reassess whether that cryptocurrency is cash.

Inventory

14. If an entity holds cryptocurrencies for sale in the ordinary course of business, those holdings of cryptocurrencies would meet the definition of inventories in paragraph 6

of IAS 2 *Inventories*[2]. Accordingly, the entity would apply IAS 2 in accounting for those holdings. If such an entity is a broker-trader as described in paragraph 5 of IAS 2, the entity might apply paragraph 3(b) of IAS 2 and measure its holdings of cryptocurrencies at fair value less costs to sell.

Intangible asset

15. We think cryptocurrencies meet the definition of an intangible asset in paragraph 8 of IAS 38 *Intangible Assets*—ie an identifiable non-monetary asset without physical substance. Consequently, if holdings of cryptocurrencies are not inventories for an entity, the entity would apply IAS 38 in accounting for those holdings as follows:

    (a) After initial recognition at cost, paragraph 72 allows an entity to choose to measure its intangible assets using either the cost model or the revaluation model. The same measurement model is used for all assets in a particular asset class (subject to the active market requirements described in (c)(i) and (c)(iv) below).

    (b) Applying the cost model (paragraph 74 of IAS 38), an entity measures intangible assets at cost less any accumulated amortisation and impairment losses.

    (c) Applying the revaluation model (paragraph 75 of IAS 38):

        (i) an entity measures intangible assets at fair value at the date of the revaluation less any subsequent accumulated amortisation and impairment losses. Fair value is measured by reference to an active market.

        (ii) an entity recognises any increase in the carrying amount of an intangible asset resulting from a revaluation in other comprehensive income. However, the increase is recognised in profit or loss to the extent that it reverses a revaluation decrease of that asset previously recognised in profit or loss.

[2] Paragraph 6 of IAS 2 defines inventories as 'assets (a) held for sale in the ordinary course of business; (b) in the process of production for such sale; or (c) in the form of materials or supplies to be consumed in the production process or in the rendering of services'.

(iii) an entity recognises any decrease in the carrying amount of an intangible asset resulting from a revaluation in profit or loss. However, the decrease is recognised in other comprehensive income to the extent of any credit balance in the revaluation surplus in respect of that asset.

(iv) if there are assets for which there is no active market in a class of assets measured using the revaluation model, then an entity measures those assets using the cost model.

Presentation and disclosure

16. An entity applies the presentation and disclosure requirements of the same IFRS Standard it uses to recognise and measure its holdings of cryptocurrencies. For example, if an entity applies IAS 38 then it applies the disclosure requirements in paragraphs 118–128 of that Standard.

17. IAS 1 *Presentation of Financial Statements* and IAS 10 *Events after the Reporting Period* also contain relevant disclosure requirements.

18. Paragraph 122 of IAS 1 requires an entity to disclose any judgements regarding its accounting for holdings of cryptocurrencies if those are part of the entity's judgements that had the most significant effect on the amounts recognised in the financial statements.

19. Paragraph 21 of IAS 10 requires an entity to disclose any material non-adjusting events, including information about the nature of the event and an estimate of its financial effect (or a statement that such an estimate cannot be made). For example, an entity holding cryptocurrencies would consider whether changes in the fair value of those holdings after the reporting period are of such significance that non-disclosure could influence the economic decisions that users of financial statements make on the basis of the financial statements.

The Committee's discussion

20. In September 2018, most Committee members agreed with the staff analysis of the application of IFRS Standards to holdings of cryptocurrencies.

21. However, one Committee member disagreed. In that Committee member's view, cryptocurrencies are excluded from the scope of IAS 38 applying paragraph 7 of that Standard. Paragraph 7 of IAS 38 states:

> Exclusions from the scope of a Standard may occur if activities or transactions are so specialised that they give rise to accounting issues that may need to be dealt with in a different way. Such issues arise in the accounting for expenditure on the exploration for, or development and extraction of, oil, gas and mineral deposits in extractive industries and in the case of insurance contracts. Therefore, this Standard does not apply to expenditure on such activities and contracts. However, this Standard applies to other intangible assets used (such as computer software), and other expenditure incurred (such as start-up costs), in extractive industries or by insurers.

22. In that Committee member's view, an entity applies paragraphs 10-11 of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* in selecting and applying an accounting policy for its holdings of cryptocurrencies.

23. In our view, and as explained in paragraphs 55–62 of Agenda Paper 4A to the Committee's September 2018 meeting, paragraph 7 of IAS 38 applies only to the transactions specifically mentioned in that paragraph. We think an entity cannot apply that scope exclusion to cryptocurrencies by analogy. No other Committee member disagreed with our analysis.

Committee's advice to the Board on standard-setting

24. One Committee member suggested an amendment to IFRS 9 *Financial Instruments* to include cryptocurrencies within its scope.

25. Four Committee members suggested an amendment to IAS 38 to remove cryptocurrencies from its scope but not explicitly include them within the scope of another Standard. This would result in an entity applying paragraphs 10-11 of IAS 8 in selecting and applying an accounting policy for its holdings of cryptocurrencies, unless those holdings were inventories for the entity. Other Committee members and

observers expressed concerns about such an approach, noting that it would leave the development of appropriate accounting to practice and could increase diversity.

26. Two Committee members said the Board should add a standard-setting project on cryptocurrencies to its agenda immediately. Those Committee members observed that the standard-setting process could take time and that cryptocurrencies are evolving rapidly.

27. Seven Committee members said it is too early for the Board to consider standard-setting for cryptocurrencies. However, some of those members also said the prevalence of cryptocurrencies may develop to such an extent that standard-setting becomes necessary. They suggested that the Board continue to monitor developments in this area.

28. Two of those Committee members said, in the short-term, it would be helpful if the Committee were to publish an agenda decision highlighting the application of IFRS Standards to holdings of cryptocurrencies. Those Committee members said it would be particularly useful to highlight the disclosure requirements in the Standards.

November Board discussion

29. The Board discussed the Committee's advice at its meeting in November 2018 (see Agenda Paper 12D for that meeting). At that meeting Board members agreed with the Committee's analysis of the requirements in IFRS Standards, as described in paragraphs 10–23 of this paper.

30. Having considered the Committee's advice and information provided on the prevalence of cryptocurrency transactions, the Board decided not to add to its work plan a project on holdings of cryptocurrencies or initial coin offerings at this time. Instead, the Board decided to monitor developments regarding cryptoassets.

31. The Board also decided to ask the Committee to consider publishing an agenda decision that would explain how IFRS Standards apply to holdings of cryptocurrencies.

Staff analysis and recommendation

32. Paragraph 5.15 of the *Due Process Handbook* states that the objectives of the Committee are to 'interpret the application of IFRSs, provide timely guidance on financial reporting issues that are not specifically addressed in the IFRSs and undertake other tasks at the request of the IASB'. That paragraph goes on to say the Committee works in partnership with the Board to give guidance that responds to the implementation needs of those applying IFRS Standards.

33. In this instance, the Board has asked the Committee to consider publishing an agenda decision regarding holdings of cryptocurrencies, and thus we think this fits into what paragraph 5.15 of the *Due Process Handbook* refers to as 'undertake other tasks at the request of the IASB'.

34. The Board has asked the Committee to consider publishing an agenda decision in the light of input the Board received and considered in deciding not to add a project on cryptocurrencies to its work plan. Although the Board decided not to add such a project, some stakeholders had suggested that it would be helpful for the Committee to set out in an agenda decision how IFRS Standards apply to holdings of cryptocurrencies. Indeed, since the November Board meeting we have been informed by a number of stakeholders interested in the accounting for holdings of cryptocurrencies that they would view such an agenda decision as helpful. In addition, our research on the prevalence of holdings of cryptocurrencies among IFRS reporters indicated that there is diversity in the reporting methods applied and, thus, an agenda decision would help to support consistent application of the Standards to such holdings.

35. For these reasons, we recommend that the Committee publish a tentative agenda decision that explains how IFRS Standards apply to holdings of cryptocurrencies. Appendix A to this paper sets out the proposed wording of the tentative agenda decision. Because the agenda decision would not be published in response to a submission to the Committee, the introduction and concluding remarks in a typical agenda decision have been adjusted accordingly.

Questions for the Committee

1. Does the Committee continue to agree with the analysis of IFRS Standards as described in paragraphs 10–23 of this paper?
2. Does the Committee agree with our recommendation to publish a tentative agenda decision?
3. Does the Committee have any comments on the proposed wording of the tentative agenda decision set out in Appendix A to this paper?

Appendix A—Proposed wording of the tentative agenda decision

Holdings of cryptocurrencies

The Committee discussed how IFRS Standards apply to holdings of cryptocurrencies.

A cryptocurrency is a digital or virtual currency that is recorded on a distributed ledger and uses cryptography for security. A cryptocurrency is not issued by a jurisdictional authority or other party. A holding of a cryptocurrency does not give rise to a contract between the holder and another party.

Nature of a cryptocurrency

Paragraph 8 of IAS 38 *Intangible Assets* defines an intangible asset as an identifiable non-monetary asset without physical substance.

Paragraph 12 of IAS 38 states that an asset is identifiable if it is separable or arises from contractual or other legal rights. An asset is separable if it is capable of being separated or divided from the entity and sold, transferred, licensed, rented or exchanged, either individually or together with a related contract, identifiable asset or liability.

Paragraph 16 of IAS 21 *The Effects of Changes in Foreign Exchange Rates* states that the essential feature of a non-monetary item is the absence of a right to receive (or an obligation to deliver) a fixed or determinable number of units of currency.

The Committee observed that holdings of cryptocurrencies meet the definition of an intangible asset in IAS 38 on the grounds that (a) they are capable of being separated from the holder and sold or transferred individually; and (b) they do not give the holder a right to receive a fixed or determinable number of units of currency.

Which IFRS Standard applies to holdings of cryptocurrencies?

The Committee concluded that an entity applies IAS 2 *Inventories* to cryptocurrencies held for sale in the ordinary course of business. If IAS 2 is not applicable, an entity applies IAS 38 to holdings of cryptocurrencies. The Committee considered the following in reaching its conclusion.

Intangible Asset

IAS 38 applies in accounting for all intangible assets except:

a) intangible assets that are within the scope of another Standard;

b) financial assets, as defined in IAS 32 *Financial Instruments: Presentation*;

c) the recognition and measurement of exploration and evaluation assets; and

d) expenditure on the development and extraction of minerals, oil, natural gas and similar non-regenerative resources.

Accordingly, the Committee considered whether holdings of cryptocurrencies meet the definition of a financial asset in IAS 32 or are within the scope of another Standard.

Financial asset

Paragraph 11 of IAS 32 defines a financial asset. To summarise that definition, a financial asset is any asset that is (a) cash, (b) an equity instrument of another entity, (c) a contractual right to receive cash or another financial asset from another entity, (d) a contractual right to exchange financial assets or financial liabilities with another entity under particular conditions, or (e) a particular contract that will or may be settled in the entity's own equity instruments.

The Committee concluded that holdings of cryptocurrencies are not financial assets. This is because a cryptocurrency is not cash (see below), is not an equity instrument of another entity, does not give rise to a contractual right for the holder and is not a contract that will or may be settled in the holder's own equity instruments.

Cash

Paragraph AG3 of IAS 32 states that 'currency (cash) is a financial asset because it represents the medium of exchange and is therefore the basis on which all transactions are measured and recognised in financial statements. A deposit of cash with a bank or similar financial institution is a financial asset because it represents the contractual right of the depositor to obtain cash from the institution or to draw a cheque or similar instrument against the balance in favour of a creditor in payment of a financial liability.'

The Committee observed that the description of cash in paragraph AG3 of IAS 32 implies that cash is expected to be used as a medium of exchange (ie used in exchange for goods or services) and as a unit of account (ie used as the monetary unit in pricing goods or services) to such an extent that it would be the basis on which all transactions are measured and recognised in financial statements.

Some cryptocurrencies can be used in exchange for particular good or services. However, the Committee noted that it is not aware of any cryptocurrency that is used as a medium of exchange and as a unit of account to such an extent that it would be the basis on which all transactions are measured and recognised in financial statements. Consequently, the Committee concluded that holdings of cryptocurrencies are not cash.

Inventory

IAS 2 applies to inventories of intangible assets. Paragraph 6 of IAS 2 defines inventories as assets:

a) held for sale in the ordinary course of business;

b) in the process of production for such sale; or

c) in the form of materials or supplies to be consumed in the production process or in the rendering of services.

The Committee observed that an entity may hold cryptocurrencies for sale in the ordinary course of business. In that circumstance, holdings of cryptocurrencies are inventory for the entity and, accordingly, the entity applies IAS 2 to those holdings.

The Committee also observed that an entity may act as a broker-trader of cryptocurrencies as described in paragraph 5 of IAS 2. In that circumstance, paragraph 3(b) of IAS 2 specifies requirements for commodity broker-traders who measure their inventories at fair value less costs to sell. Paragraph 5 of IAS 2 states that broker-traders are those who buy or sell commodities for others or on their own account. The inventories referred to in paragraph 3(b) are principally acquired with the purpose of selling in the near future and generating a profit from fluctuations in price or broker-traders' margin.

Disclosure

An entity applies the disclosure requirements in the IFRS Standard applicable to its holding of cryptocurrencies. Accordingly, an entity applies the disclosure requirements in (a) paragraphs 36–39 of IAS 2 to holdings of cryptocurrencies held for sale in the ordinary course of business, and (b) paragraphs 118-128 of IAS 38 to holdings of cryptocurrencies to which it applies IAS 38.

The Committee noted that, applying paragraph 122 of IAS 1 *Presentation of Financial Statements*, an entity would disclose any judgements regarding its accounting for holdings of cryptocurrencies if those are part of the entity's judgements that had the most significant effect on the amounts recognised in the financial statements.

The Committee also noted that paragraph 21 of IAS 10 *Events after the Reporting Period* requires an entity to disclose any material non-adjusting events, including information about the nature of the event and an estimate of its financial effect (or a statement that such an estimate cannot be made). For example, an entity holding cryptocurrencies would consider whether changes in the fair value of those holdings after the reporting period are of such significance that non-disclosure could influence the economic decisions that users of financial statements make on the basis of the financial statements.