EUROPEAN ASSOCIATION OF CO-OPERATIVE BANKS
The Co-operative Difference: Sustainability, Proximity, Governance

Brussels, 30th July 2021

EACB Comments on the EFRAG Discussion Paper "Accounting for crypto-assets (liabilities): holder and issuer perspective"

General remarks

The members of the EACB welcome the opportunity to comment on the EFRAG's Discussion Paper on the accounting treatment of crypto-assets (liabilities). Despite the currently limited exposure to crypto-assets of IFRS entities, the issue can become extremely relevant very fast. The trend toward crypto-asset markets becoming mainstream is rather obvious. The EACB therefore acknowledges that there is the growing need for the crypto market that is framed, with enforceable legal contracts, and clear and transparent accounting standards.

In this regard, the EACB appreciates the initiative undertaken by the EFRAG to assess the potential need for the development of IFRS accounting standard for crypto-assets (liabilities). The EACB also appreciates that this DP covers the accounting issues concerning the issuers of crypto-assets, thereby complementing the agenda decision of the IFRS Interpretation Committee that focused solely on the holders' accounting topics.

Generally, the EACB members find it essential that the accounting information is transparent and relevant for various users. Such information has to help investors in their economic decision making. It also has to be comparable across different entities. As a general rule, it is clear that different accounting standards have to be developed for crypto-assets that differ in their underlying economic characteristics. Moreover, we advocate for accounting standards that are flexible enough to adopt to a rapidly evolving crypto-asset market.

The EACB members also believe in the importance of determining rights and obligations of a holder or an issuer in specific crypto-assets. The legal enforceability of rights and obligations and the presence of a legal contract should be foundations for the reliable accounting for crypto-assets (liabilities).

Further to that, the EACB supports the harmonization of the accounting requirements for crypto-assets at an international level. There is a need for crypto-asset (liabilities) taxonomy and standardization. We also support convergence of crypto specific accounting standards developed at the national/regional level with the globally accepted solutions for crypto-asset accounting.

Finally, for banks the treatment of crypto-assets by prudential standards needs to be reflected. A double accounting or complicated reconciliation between IFRS standards and prudential standards must be avoided.

Possible approaches to the clarification or development of IFRS requirements

Consistent with the general principles and the crypto-assets' classification outlined in the Basel Committee's recent consultation paper on prudential treatment of crypto-asset exposures, the EACB particularly sees the need to connect accounting for crypto-assets with the prudential aspects. In particular, one of the general principles *"same risk, same activity, same treatment"* postulates that crypto-assets that provide the same economic functions as traditional assets underlying these crypto-assets should be subject to the same prudential treatment as these traditional assets. However, the Basel Committee is of the view that any additional and higher risks posed by these crypto-assets relative to traditional assets should be met by additional prudential requirements.

As for the Committee's preliminary proposed classification of crypto-asset exposures, Group 1a crypto-assets (tokenized traditional assets) and Group 1b crypto-assets (stablecoins) will be subject to the requirements that are at least equivalent to those already set out in the existing prudential framework, while Group 2 crypto-assets (such as bitcoin) will be subject to a "newly prescribed conservative treatment".

In light of the above, the EACB Members believe that the accounting treatment of crypto-assets should go hand in hand with the proposed prudential regulation of banks' crypto-asset exposures. In particular, the Basel Committee's proposed approach to classify crypto-assets into Group 1a, 1b and Group 2 categories should be the basis for the accounting principles. For instance, the accounting treatment of crypto-assets based on current IFRS Standards should be possible as long as the crypto-assets belong to the Group 1a category, in other words as long as the economic functions of such crypto-assets are equivalent to traditional assets, such as shares, bonds, commodities or cash.

However, should there be differences in the level of legal rights (e.g., rights to cash flows, claims in insolvency, etc.) or in the likelihood of paying the owner amounts due on time, as compared with traditional asset, then either the clarifying guidance on the application of existing IFRS requirements or the amendment of IFRS Standards to account for crypto-assets have to be implemented, when possible. This is due to the fact that the value creation of digital assets may not be well captured by existing standards that are at times out of date.

Similarly to the Basel Committee's recommendation to develop new conservative minimum risk-based capital treatment for Group 2 crypto-assets that pose additional and higher risks, such as bitcoin, the EACB Members might agree it necessary to develop a separate new IFRS accounting standard for this category of crypto-assets. These are a unique class of crypto-assets that have no physical asset representation in the real world and for which in turn there might not be a representation in the existing accounting framework. Should such class of crypto-assets be considered different in their economic characteristics as to fail to classify under the amended IFRS requirements, then the EACB believes that a separate accounting standard has to be developed.

Possibly further interpretations necessary that could over the time enter into a standard.

Holders accounting

The EACB members acknowledge that there is lack of explicit IFRS guidance for when crypto-assets are non-financial assets held as investments and agree particularly that IAS 2 and IAS 38 may need to be updated to better outline the relevant measurement of intangible assets and commodities for holders of crypto-assets. We also agree that clarifications are needed for accounting by holders of utility tokens, as there is limited guidance in existing IFRS requirements on accounting for prepayment assets. As for accounting for hybrid tokens with multiple economic functions, it has to be carefully assessed whether the primary purpose or bifurcation of hybrid tokens approach is chosen. Further to that, in relation to Paragraphs 3.79-3.93 of the DP, we support the need to clarify the accounting treatment for holders of crypto-assets on behalf of others and the need for clear guidance on who has economic control.

Classification of crypto-assets as cash or cash equivalent

The EACB agrees with the conclusions of the IFRS Interpretation Committee with regards to the holdings of crypto-assets as cash or cash equivalent. In particular, our members believe that a crypto-asset cannot be considered as medium of exchange to the extent that it could be treated as cash for accounting purposes as in IAS 32.

The EACB is of the view that the treatment as cash or cash equivalent should be subject to high standards, especially in terms of liquidity and stability of value. Crypto-assets cannot be readily exchanged for cash and are subject to a substantial risk of variation in their value. Furthermore, the EACB agrees that the recognition of some crypto-assets (such as e-money or stablecoins pegged for fiat currencies) as cash or cash equivalent could lead to an increased demand for these crypto-assets by banks and, in turn, could potentially raise financial stability concerns and represent additional and higher risks to their holders.

The recent case of a price freefall of the cryptocurrency called "Titan" has shown that certain digital assets may be prone to a run and extreme volatility. Despite the announced characteristics of Titan coins as "highly secure digital assets", this DeFi token dropped into a freefall until its price reached nearly $0. The reason for the sell-off was that crypto whales initiated a sell-off which triggered a panic selling in the market. This example of the "first large-scale crypto bank run" shows that crypto-assets' significant price volatility and speculative focus clearly pose financial stability concerns and may harm the reputation of the whole financial sector.

Valuation techniques

Furthermore, the valuation methods used for crypto-assets have to take into account the fact that there is no concept of an end of day and no closing day in a crypto market. Moreover, we advocate for valuation methods that are flexible enough to adopt to the evolution of crypto-assets.

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