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POVZETEK: Članek razvija praktičen okvir za klasifikacijo in izvajanje zveze z kriptovaluti pod IFRS. Vprašanje se nanaša na težave pri uvrstitvi kriptovalut, ki so zelo volitvene in niso prilagodljive tradicionalnim konceptom novča, novčnih ekvivalentov ali finančnih instrumentov. Nauka ponuja določen okvir, ki je založen na temeljnih principih obstojnih standardov in razprave večjih finančnih družb in standardov. Okvir omogoča finančnim odborom struktuirano razsudko in dokumentacijo odlok, dokler se standardi še uveljavljajo.

METODA: Članek je razvijen na podlagi obstojnih standardov IFRS in razprav, ki jih vodi večje finančne družbe in standardov. V članku je predstavljena osebna izkušnja avtorja in razprava o težavah, ki jih prinašajo kriptovalute pod IFRS. Pristop je založen na ekonomskega karaktera kriptovalut in namenu njihovega ustreznega uvrstitvi.

KLJUČNE UGOTOVITVE:

- Kriptovalute so zelo volitvene in niso prilagodljive tradicionalnim konceptom novča, novčnih ekvivalentov ali finančnih instrumentov.
- Finančni odbori morajo uporabljati znatno razsudilo za uvrstitvi kriptovalut pod IFRS.
- Nauka ponuja okvir, ki je založen na temeljnih principih obstojnih standardov in razprave večjih finančnih družb in standardov.

POMEN ZA TRGOVANJE: Ugotovitve so uporabne za praktiko, ker omogočajo finančnim odborom struktuirano razsudko in dokumentacijo odlok, dokler se standardi še uveljavljajo. To je pomembno, saj kriptovalute se pogosto pojavljajo na bilansnih listih podjetij, kar pomeni, da je jasen postopek uvrstitvi pomemben za investitorje, auditorje in regulatorje.

Navigating the Crypto Accounting Frontier: An IFRS Reporting Framework

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Abstract

The growth of cryptocurrencies and other digital assets has created a practical accounting challenge for CFOs and finance teams: how should these holdings be accounted for under International Financial Reporting Standards (IFRS)? Crypto assets can be highly volatile, liquidity can vary considerably between different assets, and they do not fit easily within the traditional concepts of cash, cash equivalents or financial instruments. As a result, companies are often required to apply significant judgment when determining the appropriate accounting treatment.

This article develops a practical framework for classifying and reporting crypto holdings under IFRS. The framework is based on the underlying principles of the existing standards and considers the approaches being discussed by major accounting firms and standards-setters. Rather than treating all crypto assets in the same way, the proposed approach considers the nature of the asset, how it is held and the purpose for which it is used. This provides finance teams with a more structured basis for making and documenting accounting decisions while formal guidance continues to develop.

1. Introduction

Cryptocurrencies and digital assets have moved from being largely a specialist investment topic to becoming part of the wider corporate and financial landscape. Companies such as Tesla, Square and MicroStrategy have held significant amounts of Bitcoin, bringing greater attention to the accounting implications of these assets (Livni, 2021). For companies reporting under IFRS, crypto holdings create a difficult question because the characteristics of these assets do not fit neatly into many of the categories traditionally used in financial reporting.

Crypto assets have characteristics that make their classification under existing IFRS standards difficult. They can be extremely volatile, liquidity can differ significantly between tokens, and many do not provide contractual rights to receive cash or another financial asset. They also generally do not represent an ownership interest in an underlying business (Deloitte, 2019; EY, 2021). These features make it difficult to apply the normal accounting models without first considering the specific facts and circumstances surrounding the holding.

The absence of specific and comprehensive IFRS guidance has also resulted in differences in practice. A 2019 survey by the Association of International Certified Professional Accountants (AICPA) found that entities were using a range of approaches, including intangible assets, investments, inventory and other classifications (AICPA, 2019). Such differences can make financial statements harder to compare, particularly as crypto holdings become more significant to corporate balance sheets.

The issue becomes more important as companies increase their exposure to digital assets. Investors, auditors and regulators need to understand not only the amount reported on the balance sheet but also how management arrived at the accounting treatment and what risks are associated with the assets (Segal, 2021).

This article proposes a decision framework for classifying crypto assets under IFRS by looking at their economic characteristics and the purpose for which they are held. The objective is not to create a new accounting standard, but to provide finance teams with a practical starting point for applying existing principles and documenting their judgments while the standard-setting process continues.

Section 2 considers the difficulties of fitting crypto assets within the existing IFRS framework and the different accounting approaches that have developed. Section 3 presents a decision tree for classification based on the approaches suggested by accounting firms and standards-setters. Section 4 considers the audit and governance issues associated with crypto holdings. Section 5 discusses the direction of IFRS standard-setting and the importance of disclosure and judgment during the transition.

2. The Crypto Accounting Gray Zone

Current IFRS standards do not contain a comprehensive set of requirements specifically designed for cryptocurrencies. Most of the relevant standards were developed before blockchain technology and digital assets became commercially significant. As a result, finance teams have had to apply existing principles to assets with characteristics that were not necessarily contemplated when those standards were written.

IAS 32 Financial Instruments: Presentation defines a financial asset as including cash, an equity instrument of another entity, a contractual right to receive cash or another financial asset, or certain contracts settled in an entity's own equity instruments (IASB, 2019, para. 11). Most cryptocurrencies do not fit comfortably within these definitions.

There are several reasons for this:

- Most cryptocurrencies experience price volatility that is significantly greater than traditional cash equivalents. This makes it difficult to support cash or cash equivalent treatment under IAS 7 (Deloitte, 2019).

- Holding a cryptocurrency generally does not provide an ownership interest in an underlying company and therefore does not represent an equity instrument.
- Crypto assets generally do not give the holder a contractual right to receive cash or another financial asset from another party. Their value is instead largely determined by supply and demand in the relevant market.
- The blockchain protocols supporting cryptocurrencies are generally software-based protocols rather than legal contracts between counterparties (PwC, 2019).

Inventory accounting under IAS 2 also presents difficulties. IAS 2 applies to assets held for sale in the ordinary course of business, assets being produced for such sale, and certain commodity broker-trader activities (IASB, 2019). This may be relevant to businesses whose normal operations involve dealing or trading in crypto assets. It is less straightforward for a company that simply holds cryptocurrency as part of its treasury or investment activities.

In the absence of a clearly defined category, accounting for crypto assets has therefore become an area where management judgment plays an important role. Similar holdings can be classified differently by different entities. The 2019 AICPA survey reported significant use of intangible asset treatment, with other entities using investment, inventory or other classifications (AICPA, 2019).

Some of this variation is understandable. Crypto assets differ substantially from one another, and the purpose for which an entity holds an asset can also differ. At the same time, inconsistent treatment can make it difficult for users of financial statements to compare companies with similar exposures. It can also create a risk that important information about the size and nature of crypto holdings is not adequately communicated through the financial statements.

As crypto balances become more material, consistency and transparency become increasingly important. Investors need to be able to understand how assets have been measured, what assumptions have been used and what risks could affect their reported value (Segal, 2021).

3. Classifying Crypto: An IFRS-Aligned Rubric

As the IASB and national standard-setters consider how IFRS should deal with crypto assets, accounting firms and preparers have developed a number of possible approaches using the standards that are currently available. Based on the approaches discussed by PwC (2019) and EY (2021), the following decision framework provides a way of thinking through the classification question.

4. Cash or cash equivalent (IAS 7)

- This treatment could be considered where a crypto asset is actively traded in a sufficiently liquid market, is held primarily for liquidity purposes, can be converted into

known amounts of cash with limited price impact and is genuinely used to meet short-term cash requirements (PwC, 2019).

- In practice, the number of cryptocurrencies that could satisfy all of these requirements is likely to be limited. Bitcoin and Ether, for example, have substantially greater market activity than many smaller tokens, but liquidity and price stability still need to be considered against the specific IAS 7 requirements.
- Where an asset qualifies as a cash equivalent, measurement would follow the applicable requirements for cash and cash equivalents, rather than being treated simply as a general crypto investment.

5. Inventory (IAS 2)

- Inventory treatment may be appropriate where crypto assets are held for sale in the ordinary course of business by an entity whose activities include dealing or trading in crypto assets.
- It may also be relevant to crypto assets generated through mining activities in circumstances where the entity's business model supports such treatment (EY, 2021).
- Where IAS 2 applies, the measurement requirements of that standard would need to be considered, including the lower of cost and net realisable value requirement in IAS 2.9.

6. Intangible asset (IAS 38) - with finite useful life

- Intangible asset treatment has generally been considered the main accounting category for crypto assets that do not qualify as cash or cash equivalents and are not held as inventory (PwC, 2019).
- This can include cryptocurrencies and other crypto assets held for purposes such as long-term investment or use within a blockchain ecosystem (EY, 2021).
- The asset would initially be measured at cost under IAS 38.24. Subsequent measurement would depend on the accounting policy selected, including the cost model or, where the relevant conditions are met, the revaluation model.
- Where an intangible asset has a finite useful life, it would be amortised over its useful life and assessed for impairment in accordance with the applicable requirements of IAS 36.

7. Intangible asset (IAS 38) - with indefinite useful life

- An indefinite useful life may be considered where there is no foreseeable limit to the period during which the asset is expected to generate net cash inflows for the entity, consistent with the principles in IAS 38.88.

- The asset would initially be recognised at cost under IAS 38.24. The subsequent measurement approach would depend on the applicable accounting policy and whether the conditions for revaluation are satisfied.
- An intangible asset classified as having an indefinite useful life would not be amortised, but would instead be subject to the required impairment assessment, including annual impairment testing under IAS 36.

8. Financial asset at fair value through profit or loss (IFRS 9)

- IFRS 9 treatment may need to be considered where a crypto asset forms part of an investment portfolio that is managed and evaluated on a fair value basis (PwC, 2019).
- This assessment is different from simply considering whether an asset is highly traded or liquid. The entity would need to consider the nature of the asset and the contractual rights and characteristics relevant to IFRS 9.
- Where IFRS 9 applies, the asset would be measured at fair value, with changes in fair value recognised in profit or loss in accordance with the applicable requirements of the standard.

The classification decision ultimately depends on the facts and circumstances of the particular holding. The same cryptocurrency may require different analysis depending on why and how the entity holds it. The economic substance of the arrangement should therefore be considered rather than relying only on the name or technical description of the token (EY, 2021).

For example, a crypto asset held as part of an entity's normal trading activities may require a different assessment from the same asset held as a long-term investment. Similarly, crypto assets received through mining activities may initially be considered under an inventory model where the relevant requirements are met, with subsequent accounting depending on what happens to those assets.

The purpose of this framework is to provide a more consistent process for making these judgments. It starts with the economic characteristics of the asset, considers the entity's business purpose and then asks which existing IFRS requirements most closely reflect those circumstances. This is preferable to selecting an accounting treatment simply because it produces a particular financial statement outcome.

The framework also places importance on the quality of the supporting evidence. Management should be able to explain why a particular classification was selected, what assumptions were used and why alternative treatments were rejected. This documentation becomes particularly important where the accounting treatment involves significant judgment.

Some classifications are less likely to be appropriate for ordinary crypto holdings. For example, property, plant and equipment under IAS 16 would generally not provide a suitable basis because cryptocurrencies do not have the physical characteristics or productive capacity associated with tangible assets. Similarly, the absence of a contractual obligation or ownership interest generally makes financial liability or equity classification under IAS 32 difficult to support.

Classification is only one part of the reporting issue. Disclosure is equally important because users of financial statements need enough information to understand what the entity actually owns and how management has accounted for it.

At a minimum, entities should consider clearly explaining:

- The nature and purpose of their crypto holdings
- The IFRS category used and the reasons for selecting it
- The measurement basis applied, including whether cost or fair value is used
- The fair value hierarchy and significant inputs or assumptions, where relevant
- Key risks and sensitivities, particularly exposure to price volatility
- Any significant changes in classification or valuation methodology from one reporting period to another
- Any supplemental non-GAAP information used by management to explain the economics of the holdings

Early discussions with auditors can also reduce problems later in the reporting cycle. Management should ideally discuss significant classification, valuation and disclosure judgments with the audit team before year-end rather than waiting until the financial statements are close to completion. This gives both sides an opportunity to understand the proposed treatment and identify areas where additional evidence may be required.

9. Auditing and Governance Challenges

Even where an entity has reached a reasonable classification conclusion, auditing crypto assets creates additional challenges. The nature of blockchain-based assets is different from that of most traditional financial assets, particularly where assets are held directly by the entity rather than through a regulated financial institution.

Auditors may need different tools and procedures to establish the existence and control of crypto assets. For self-custodied assets, traditional third-party confirmations may not provide the same type of evidence that they provide for bank balances or securities. On-chain analysis and direct examination of blockchain records may therefore become important parts of the audit process (AICPA, 2020).

The audit team may also need to understand the specific blockchain on which the asset exists, including the relevant protocol, smart contracts and consensus mechanism. This is not simply a matter of verifying a balance. The auditor may also need to determine whether the entity actually controls the asset and whether the balance observed on the blockchain can be linked to the reporting entity.

Private key control is an important part of this process. Possession or control of the relevant cryptographic keys can provide evidence of the entity's ability to control the asset, but the audit procedures required to establish that control may be very different from traditional IT and financial controls. Custody arrangements, access controls, cold storage and other security measures therefore become relevant to the audit (AICPA, 2020).

Valuation is another significant area of judgment. Many crypto assets trade across multiple exchanges, and the prices quoted on those exchanges may differ. For less liquid tokens, there may also be limited observable market information. Auditors therefore need to consider the appropriate market, the reliability of quoted prices and the inputs used in determining fair value (CPA.com, 2021).

These issues mean that finance, treasury, IT and internal audit teams may need to work together more closely. Traditional internal control frameworks such as COSO still provide a useful foundation, but the specific controls around wallet access, private keys, exchange accounts and blockchain transactions need to be clearly documented.

The audit environment around crypto assets is still developing. As corporate holdings increase, auditors and finance teams will likely continue to refine their procedures. Companies that establish clear custody, valuation, reconciliation and documentation processes early will be better positioned to deal with audit requirements as expectations develop.

Management should therefore keep track of developments from accounting firms, professional bodies and standards-setters. This is particularly important for companies with material crypto exposure, as the accounting and assurance expectations can change as the market and regulatory environment develop.

10. The Path Forward

The accounting treatment of crypto assets under IFRS is gradually becoming clearer, although significant questions remain. In the absence of a dedicated comprehensive IFRS standard, entities continue to rely on the existing standards and the interpretations and guidance that have emerged around them.

The IFRS Interpretations Committee has previously considered the accounting for holdings of cryptocurrencies and concluded that, in the fact pattern considered, cryptocurrencies did not meet the definition of cash or a financial asset and generally met the definition of an intangible asset under IAS 38. Inventory treatment could apply in narrower circumstances, particularly where the relevant business model and requirements of IAS 2 are met (IFRIC, 2019).

National standard-setters have also considered the issue. The Australian Accounting Standards Board has discussed digital assets and approaches that would generally result in intangible asset treatment, with inventory potentially applying to broker-traders (AASB, 2022). Similar discussions have taken place in Korea and Hong Kong.

At the international level, the IASB has also considered crypto assets as part of its broader research and standard-setting activities (IASB, 2022). The direction of future guidance will be important because the existing standards were not designed specifically for blockchain-based assets.

For finance leaders, the practical response in the meantime is to apply the existing standards carefully and document the reasoning behind significant judgments. The objective should not simply be to find a category that appears to fit the asset. Management needs to demonstrate why the selected treatment reflects the economic characteristics of the holding and the way the entity uses it.

The decision tree proposed in this article provides one possible starting point. It brings together the existing IFRS requirements with approaches discussed by accounting firms and regulators and provides a structured way for finance teams to assess classification. Its usefulness depends on the quality of the underlying analysis and the supporting evidence.

Good disclosure is particularly important while practice remains unsettled. Where significant judgment has been applied, users should be able to understand what management has decided, why it reached that conclusion and what assumptions could affect the reported amount. Auditor involvement should also be considered early, particularly where the holding is material or the accounting position is unusual.

The crypto accounting issue is therefore broader than simply deciding where an asset should appear on the balance sheet. It also involves valuation, controls, custody, audit evidence and communication with investors. As digital assets become more integrated into corporate finance, these issues will become increasingly relevant to CFOs and finance teams.

The challenge for finance professionals is to keep pace with the underlying technology while continuing to apply the principles of financial reporting. Blockchain and digital assets may change the way value is created, transferred and stored, but the fundamental need for reliable, relevant and understandable financial information remains.

For companies with significant crypto exposure, developing a documented accounting policy, establishing appropriate controls and maintaining regular dialogue with auditors can provide a more stable basis for reporting while formal guidance continues to evolve.

Ultimately, the quality of crypto reporting will depend less on finding a single universal accounting treatment and more on whether companies can explain and support the treatment they have selected. As the market develops, investors and other stakeholders will expect financial reporting to keep pace with the underlying economic reality.

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Author Disclosure

The author has no conflicts of interest to declare. This paper reflects the personal views of the author in his academic capacity and does not represent the views of any institution with which he is affiliated. The author is an adjunct faculty member at Manipal Academy of Higher Education (MAHE) Dubai, teaching Financial Accounting, Financial Modelling, and AI in Finance to MBA students.