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Virtual Currencies
Issues paper

Purpose of this paper

1 This paper summarises the accounting requirements for virtual currencies under Japanese GAAP as published in March 2018 by the Accounting Standards Board of Japan (ASBJ), and considers potential issues that might be relevant for IFRS reporting.

Note for EFRAG CFSS and EFRAG TEG members

2 The objective of the session is to ask EFRAG CFSS and EFRAG TEG members for initial observations on the accounting for virtual currencies under Japanese GAAP and how the requirements might interact with the applicable/forthcoming legislation in your jurisdiction in an IFRS reporting context.

3 Agenda paper 07-02 for this session informs that the IASB is currently considering whether it should undertake a project that would include the accounting for virtual currencies.

4 Appendix 1 of this paper includes an overview (as at January 2018) of the various initiatives being considered by European national standard setters on virtual currencies. The overview was prepared by the EFRAG Secretariat based on information provided by EFRAG CFSS members.

5 At this stage, the EFRAG Secretariat have neither examined the Japanese GAAP requirements in detail nor considered their interaction with IFRS reporting.

Background

What is the issue with cryptocurrencies?

6 Virtual currencies (also referred to as digital currencies, cryptocurrencies or crypto-assets) as well as Initial Coin Offerings (ICOs) have become a much talked about topic in recent years, with the total cryptocurrency market capitalisation increasing significantly in the last few years.

7 The accounting treatment of cryptocurrencies under IFRS Standards is unclear. They may not qualify as financial assets, as they neither represent a right to receive cash or other financial instruments, nor a contract to exchange assets. They may qualify as intangible assets, but they are not legally protected and have no useful life. Some jurisdictions have reported diversity in the accounting for virtual currencies under IFRS Standards and asked the IASB to consider developing guidance on the topic.

Past discussions and developments

8 At its meeting in November 2016, EFRAG CFSS and EFRAG TEG discussed a paper on digital currencies prepared by the Australian Accounting Standards Board (AASB) for discussion at the December 2017 ASAF meeting.

9 EFRAG TEG-CFSS members generally agreed that interpretation issues on the accounting for digital currencies could arise; however they did not think there was an urgent need for guidance at this stage. Members did not support the suggestion made in the AASB paper to address digital currencies as part of a broader project on investments in intangible assets and commodities.

10 ASAF members also thought that cryptocurrencies were in its infancy and was too early to address accounting matters. However, they recommended that the IASB continue to monitor developments in this area.

11 At its meeting in January 2018, the IASB discussed a potential new research project on Commodity loans and related transaction including Digital currencies. Many Board members agreed that digital currencies should be a different project, not included in the commodity loans discussion. Some members mentioned that they would like some additional information about the real impact and applicability of digital currencies.

The ASBJ Standard

12 The ASBJ Standard on virtual currencies (the ASBJ Standard) addresses the accounting for virtual currencies as defined in the Payment Service Act in Japan (the Act), except for those that were issued by the entity itself. The ASBJ Standard was published in Japanese with a summary of the requirements published in English (see ASAF AP 03B provided as agenda paper 07-06 for background information).

13 The Act recognises virtual currencies as a means of payment and defines them as proprietary value that can be transferred using electronic data processing system and can either be:

(a) used against unspecified parties as a means of payment and can be traded with unspecified parties; or

(b) can be exchanged with other virtual currencies as defined by the Act.

Scope

14 The ASBJ Standard scopes out virtual currencies issued by the entity itself (including its parent, subsidiaries and affiliates) such as Initial Coin Offerings (ICO's). The ASBJ explain that further work is needed in this area before appropriate guidance can be developed.

15 The ASBJ Standard addresses the following:

(a) virtual currencies held by an entity on its own behalf; and

(b) virtual currencies held by a dealer on behalf of its customers.

Virtual currencies held by an entity on its own behalf

16 Virtual currencies held by the entity on its own behalf should be recognised and measured as follows:

(a) if an active market exists: measured using the market price at the balance sheet date, with changes in the market price recognised in Profit or Loss (FVTPL);

(b) if an active market does not exist: measured at cost. However, if the estimate disposal value is lower than the cost, the difference should be recognised as a loss and should *not be reversed* in subsequent periods; and

(c) if an active market changes to an inactive market: The initial cost should be the price observed in the active market immediately before it became inactive.

17 Consistent with the definition in IFRS 13 *Fair Value Measurement,* the ASBJ Standard defines an active market as 'a market in which transactions for the virtual currency take place with sufficient frequency and volume to provide pricing information on an ongoing basis'.

18 When an entity sells its virtual currencies, it should present the net amount (selling proceeds less the cost of the virtual currencies sold) in the income statement.

19 An entity must disclose the balance sheet amount of virtual currencies held by the entity on its own behalf, unless the amount is immaterial compared to the total assets of the entity.

20 The EFRAG Secretariat's notes that for accounting purposes, the ASBJ Standard does not seem to differentiate between virtual currencies held for trading and those held for capital appreciation or used as a means of payment.

Virtual currencies held by a dealer on behalf of its customers

21 Virtual currencies held by a dealer on behalf of its customers should be recognised and measured as follows:

(a) recognise an asset when a virtual currency is deposited from the customer; and

(b) at the same time recognise a liability as the obligation to return the virtual currency to the customers. The measure used should be the same amount of the responding asset.

22 The virtual currency asset should be measured at the market price (applying the guidance in paragraph 16) at the date the virtual currency was deposited, with a virtual currency liability measured at the same amount of the responding asset. Accordingly, there is no gain or loss from these transactions.

23 A virtual currency dealer must disclose the balance sheet amount of virtual currencies held on behalf of its customers, unless the amount is immaterial compared to the total assets of the entity.

24 The EFRAG Secretariat notes that the ASBJ Standard does not seem to addresses subsequent measurement for the virtual currency assets and liabilities that are held by a dealer on behalf of its customers.

Presentation as an asset – what type of asset?

25 The ASBJ concluded that virtual currencies were assets for accounting purposes, because they may contribute to cash inflows to the entity through sales or conversion to cash[1]. In deciding what type of asset, the ASBJ concluded that there is no category of assets that would be appropriate for virtual currencies and that they should be considered as an independent category of assets. The ASBJ analysis is summarised as follows:

[1]The ASBJ inform that currently the legal status of virtual currencies under Japanese private law is not clear, and it is not clear whether any legal property rights could be attached to virtual currencies.

(a) foreign currencies: Virtual currencies are not backed by the government (or any other authority) and have different characteristics compared to foreign currencies;

(b) financial assets: Virtual currencies are not a contract that results in a financial asset for one party and a financial liability or equity instrument for another party and therefore do not meet the definition of financial assets (other than cash) for accounting purposes;

(c) inventories held for trading: Virtual currencies can be held for purposes other than inventories (for example, they can be used as a means of payment) different on what it is included in IAS 2 *Inventories.* It would therefore be inappropriate to classify all virtual currencies as inventories held for trading; and

(d) intangible assets: IAS 38 *Intangible Asset*s does not contemplate the existence of intangible assets held for trading. It would therefore be inappropriate to classify virtual currencies as intangible assets.

Questions for EFRAG TEG and EFRAG CFSS members

26 At this stage, do you have any observations on the accounting requirements in the ASBJ Standard and how they might interact with the applicable/forthcoming legislation in your jurisdiction within an IFRS reporting context?

Potential issues to consider under IFRS

27 Agenda paper 07-05 for this session (provided as background information) (ASAF Agenda paper 03A) discusses two examples of virtual currency transactions and asks for views on the outcome under IFRS.

28 The examples **assume** that the entity reports under IFRS and applies the following accounting policies:

(a) Virtual currencies held for trading are **classified as inventories and measured at fair value less costs of disposal**.

(b) Virtual currencies held on behalf of its customers **are classified as inventories and measured at fair value less costs of disposal** (and the liability is measured at the same amount).

(c) Virtual currencies that are **not inventories are classified as intangible assets with indefinite useful lives and measured at cost less impairment** (if any).

Example 1 – fact pattern

29 Company B exchanges newly issued X-coins for Y-coins, a virtual currency with an active market. The fair value of Y-coins at the date of exchange was 10 million CUs. Company B recognised Y-coins as assets at 10 million CUs.

30 X-coins can be used for future price reductions of services provided by Company B. Company B recognised “deferred revenue” (i.e. liabilities) of 10 million CUs.

31 At the end of the reporting period, Company B had not provided the services, but the fair value of Y-coins had increased to 50 million CUs.

Questions for EFRAG TEG and EFRAG CFSS members

32 Applying the assumptions in paragraph 28:

(a) Do you think that the initial 10 million CUs worth of Y-coins received should be recognised as income in the Profit or Loss or as a liability in the balance sheet?

(b) Do you think that the change in the value of Y-coins should be recognised in the period the change occurred?

Example 2 – fact pattern

33 Company C issues 10 million units of Z-coins at an ICO. Upon issuance, 8 million units are sold to third parties and 2 million units are assigned to itself. The cost of Z-coins to Company C is zero.

34 After a successful ICO, Z-coins are traded in an active market and the fair value of Z-coins is 10 CU per unit of Z-coins at the end of the period.

Questions for EFRAG TEG and EFRAG CFSS members

35 Applying the assumptions in paragraph 28:

(a) Do you think that the 2 million units of Z-coins assigned to Company C should be recognised, and if so when?

(b) Would the assignment of Z-coins to itself qualify as a transaction that should be accounted for? If so, how?

Appendix 1 - European National Standard Setters and accounting for digital currencies

1 The following table tables an overview as at January 2018 of the initiatives being considered by European national standard setters on digital currencies.

Jurisdiction	Standard?	Comments
Austria	No	No plan to issue rules or guidance in the near future.
Belgium	No	The Belgian Accounting Standards Board is working on a standard relating to cryptocurrencies. No further details available at this stage.
Czech Republic	No	Czech accounting legislation does not have any special requirements related to digital currencies and there is no current plan to develop any special requirements.
Denmark	No	Very few questions received. We have referred the inquirers to the international debate, e.g. the discussion paper issued by Australian Accounting Standards Board, and to an article made by Mikkel B. Larsen in the professional magazine Revision & Regnskabsvæsen, April 2016, in which he says that the treatment of bitcoins in financial statements is not clarified as yet. The issue might be dealt with in the next edition of our accounting standard (non-mandated guideline) for non-listed companies: Regnskabsvejledning for klasse B- og C-virksomheder. However, this is not yet decided and no draft has been prepared.
Lithuania	No	Our Authority had received a couple of requests from market participants to explain how to account for mined or bought cryptocurrencies. There was also a question regarding accounting of virtual tokens issued during the ICO of the start-up. The requests were answered by our Authority on the basis of requirements in our national GAAPs. At the moment there are no plans to issue a standard. Despite that there are no specific standards on cryptocurrencies, other standards in our jurisdiction are flexible enough to apply them to cryptocurrencies accounting. In particular, we have BAS 18 on Financial assets and financial liabilities. According to it, mined or bought cryptocurrencies are recognised as a type of financial assets (money equivalents) and accounted accordingly at FV through P&L at the date of initial recognition and subsequent measurement. In case there are issued virtual tokens, which are linked to the value of particular cryptocurrency (typically Ethereum), the financial assets acquired are accounted in the same way at FV, but the related liabilities from this issue could be accounted as type of provision (BAS 19), financial liabilities (BAS 18) or incomes (BAS 10) depending on of the issuer’s commitments related to issued virtual tokens. The commitments from issue of virtual tokens are not recognized as equity as there are strict restrictions what kind of equity instruments could be recognized in it (BAS

		8) and as there are not recognized as securities with their ordinary features.
Luxembourg	No	
Netherlands	No	The Dutch board discussed the issue and the fact that questions are coming from practice and instructed our staff to develop a proposal for accounting guidance but not in a fast track procedure.
Poland	No	Not regulated in Polish Accounting law. However, taking into account the current provisions of the Polish Accounting Act, we are of the opinion that virtual currencies like bitcoin could be recognized as an asset if the criteria of the asset definition (stemming from the Accounting Directive or IFRS) are met. At the moment there is no intention to develop legal requirements or non-binding guidelines in this area.
Sweden	No	No plans to develop requirements or guidance.