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July 26, 2021

Submitted electronically to cryptoassets@efrag.org

EFRAG
35 Square de Meeûs
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Dear EFRAG members,

Re: Accounting for Crypto-assets (liabilities): Holder and Issuer Perspective (DP/2020/7)

This letter is the response of the staff of the [Canadian Accounting Standards Board](http://www.frascanada.ca) (AcSB) to the European Financial Reporting Advisory Group (EFRAG) Discussion Paper, “Accounting for Crypto-assets (liabilities): Holder and Issuer Perspective” issued in July 2020.

The views expressed in this response letter do not represent the view of the Canadian Accounting Standards Board. Views of the Canadian Accounting Standards Board are only developed through due process.

Consultations and outreach performed

As part of informing our response for this Discussion Paper, we consulted with stakeholders including the CPA Canada Crypto-asset Working Group (Group). The Group is a collaboration of audit firms and regulators established to share perspectives on crypto-asset activities and Canadian Auditing Standards (CAS). We considered the results of these discussions when developing this letter.

Our view

We strongly support EFRAG in its efforts to identify and raise awareness of the accounting issues for crypto-asset activities that are likely to be relevant to entities applying IFRS® Standards.

The growth of the crypto ecosystem is rapidly increasing. Prior to 2020, it was primarily retail investors that dominated crypto-asset markets. However, more recently participation in crypto-asset activities has attracted more institutional interest. Current macroeconomic factors and the suppression of yields by most central banks around the world to the zero bound have also accelerated institutional interest in the investment opportunities presented by the crypto ecosystem. Technological developments to improve the blockchain infrastructure and decentralized finance opportunities further enhance the appeal of crypto-assets as a long-term investment.

The growth in Canadian publicly traded entities' holdings of crypto-assets is significant and will continue to materially impact financial statements. Furthermore, the regulatory environment in Canada also continues to develop and provide greater clarity over crypto-asset activities.

We think improving the accounting requirements relating to the recognition, measurement, presentation and disclosure of crypto-asset activities would better serve users of financial statements. We are concerned with IAS 38 *Intangible Assets* being applicable to the holdings of cryptocurrencies. IAS 38 was written long before cryptocurrencies were developed. As a result, we have reservations about the appropriateness of the measurement model in IAS 38 in achieving fair presentation for holdings of cryptocurrencies. In our view, the fair value performance of a cryptocurrency is important to ensure a user's understanding of the entity's financial position and profit or loss.

Holdings of crypto-assets by Canadian institutions applying IFRS Standards extend beyond holdings of cryptocurrencies with no claim on the issuer. Furthermore, growth in the market capitalization of stablecoins has been increasing significantly since 2018. We think that the adoption and growth of stablecoins is an indication of the importance of the stablecoins market and the urgent need to address concerns with the accounting for stablecoins. The current gaps in the accounting requirements for stablecoins and other crypto-assets with no claim on the issuer could lead to diversity in practice and an increased risk of inadequate or misleading information being provided to users of financial statements. The appendix provides our detailed recommendations, including a phased approach to addressing the concerns with applying the current IFRS accounting requirements to crypto-assets.

Additionally, we think IFRS accounting requirements need to consider emerging issues such as decentralized financial (DeFi) and non-fungible tokens (NFT). Although the DeFi and NFT space is still an experimental and emerging space, the blockchain infrastructure already exists and some entities are participating in the opportunities from these developments.

Our responses to your questions

[The Appendix](#) to this letter responds to the questions posed in the **Discussion Paper** and expands on the points raised above.

We would be pleased to elaborate on our comments in more detail if you require. If so, please contact me or, alternatively, Katharine Christopoulos, Associate Director, Accounting Standards (+1 416 204-3270 or email kchristopoulos@acsbcanada.ca) or Jayshal Daya, Principal, Accounting Standards (+1 416 204-3501 or email jrdaya@acsbcanada.ca).

Yours truly,



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APPENDIX

Question 1 – Use of crypto-assets (liabilities)

Question 1.1

Chapter 7 discusses some of the factors that may influence the uptake of crypto-assets (liabilities) by mainstream institutions. Furthermore, as noted in Chapter 3 (Paragraph 3.98), the business purpose for holding a crypto-asset should be a key consideration in the accounting classification.

Please describe the areas in which your company (or institutional clients) use or expect to use crypto-assets (liabilities).

What are the main factors influencing the usage of crypto-assets (liabilities)?

For what purposes are crypto-assets usually held or issued by your company or institutional clients?

1. We are not directly engaged in the use of or investment in crypto-assets (liabilities). As such, we have presented our findings based on the research we compiled and the views we heard from the stakeholders we consulted. In presenting our findings, we considered the growth of crypto-asset activities in the Canadian market as well as the global developments influencing the overall participation and growth in crypto-asset activities more broadly. Furthermore, we think that the global and macro-economic factors are important considerations that are propelling institutional interest in crypto-asset activities.

Overview of crypto-asset activities in Canada

2. As at May 2021, there are 38 publicly traded entities that are engaged in crypto-asset activities, 39% of which are engaged in crypto-asset mining activities and 3% represent crypto-asset trading platforms. Three of the entities engaged in crypto-asset activities are publicly traded on the Toronto Stock Exchange (TSX). This contrasts with data we collected as of July 2019 when all entities engaged in crypto-asset activities were either listed on the venture exchange (TSXV) or on alternate exchanges in Canada. In addition to these 38 entities, there are 16 publicly traded crypto-asset exchange traded funds (ETFs) and closed-ended funds that hold either Bitcoin or Ethereum.
3. The stakeholders that we consulted informed us that there is strong anticipated growth in crypto-asset activities in Canada in the foreseeable future. Furthermore, several publicly traded entities have signaled an intent to become involved in crypto-asset activities and have taken some notable action to act on that intent, that included, for example, signing a letter of intent or acquiring crypto-asset mining equipment.

4. The table below depicts an overview of the Canadian crypto-asset landscape (publicly traded entities):

	Number of entities		
	May 2021	July 2019 ¹	July 2018 ¹
Entities other than funds	38	42	18
Publicly traded funds	16	0	0
Total	54	42	18
Engaged in mining activities	15	24	4

Regulatory developments in Canada

5. The Canadian Securities Administrators (CSA) released [CSA Staff Notice 21-327 Guidance on the Application of Securities Legislation to Entities Facilitating the Trading of Crypto Assets](#) on January 16, 2020. The notice indicates that custodial platforms that offer services to Canadian users, which do not immediately transfer ownership, possession and control of all crypto-assets purchased by customers, are likely dealing in derivatives or securities and may be subject to regulation as dealers or marketplaces under the applicable securities laws.
6. In February 2021, the Ontario Securities Commission (OSC) approved the first publicly traded bitcoin ETF in North America. Subsequently, the OSC approved multiple other Bitcoin and Ethereum ETFs in Canada. The regulatory environment continues to develop and provide greater clarity over crypto-asset activities.
7. Furthermore, there have been several industry veterans and U.S. congress representatives² that have publicly emphasized the importance of accounting standards to address the accounting for crypto-asset activities to ensure fair presentation that provides users with relevant and useful information over crypto-asset activities. Although these concerns raised were in relation to U.S. GAAP, we think that some of these concerns are also applicable under IFRS Standards.

Reasons for institutional holdings or participation

8. Prior to 2020, it was primarily retail investors that dominated crypto-asset markets. However, more recently the participation in crypto-asset activities has attracted more institutional interest. In the recent [S-1 filing](#) by Coinbase³, it noted that it works with approximately 7,000 institutions.

¹ Source: IASB staff paper Crypto-assets – Monitoring activities, November 2019 <https://cdn.ifrs.org/-/media/feature/meetings/2019/november/iasb/ap12j-implementation-matters.pdf>

² Source: <https://emmer.house.gov/press-releases?ID=9140E045-E94B-4EEE-85B3-DE28676A1131>

³ Coinbase Global, Inc., known as Coinbase, is an American company that operates the largest cryptocurrency exchange platform in North America.

9. Current macroeconomic factors and the suppression of yields by most central banks around the world to the zero bound has accelerated the institutional interest in the investment opportunities presented by the crypto ecosystem. Crypto-assets, such as bitcoin, could provide an alternate store hold of wealth that is disinflationary, intangible, transferable, and subject to simpler and more cost-effective self-custody solutions than precious metals. Furthermore, technological developments to improve the blockchain infrastructure and decentralized finance opportunities may further enhance the appeal of crypto-assets as a long-term investment.
10. Based on our research, we observed that most Canadian entities that have invested in crypto-assets are directly engaged in blockchain and crypto-asset activities as their primary line of business. However, recent news articles have indicated that there is rising interest from pension funds, endowment funds, hedge funds and other institutions to invest a portion of their assets under management in crypto-assets.⁴
11. Most stakeholders that we consulted told us that Canadian entities invest in crypto-assets primarily as a long-term investment. However, some stakeholders mentioned that some traditional⁵ Canadian entities have invested in crypto-assets as a short-term speculative investment.

Question 2 – Way forward

Question 2.1.

As detailed in Chapters 3 and 4, this DP proposes that there is need to address accounting topics, not in scope of the IFRS IC agenda decision on cryptocurrencies and to include unaddressed holders' and issuers' accounting topics.

Do you agree that there is need to address accounting topics not in scope of the IFRS IC agenda decision on cryptocurrencies? Please explain.

12. We agree that there is a need for standard-setting activity to address accounting topics not in scope of the IFRIC agenda decision on cryptocurrencies and to include unaddressed holders' and issuers' accounting topics.

Types of Crypto-asset holdings by Canadian institutions

13. According to the research we performed and the stakeholders that we consulted, Canadian institutions hold Bitcoin, Ethereum, stablecoins, and other altcoins as an investment. Furthermore, most of these Canadian entities holding crypto-assets apply IFRS Standards as their accounting framework.
14. We think that as holdings of crypto-assets with no claim on the issuer become more prevalent among entities applying IFRS Standards, the current gaps in the accounting requirements may increase. This could lead to further diversity in practice and an increased risk of an entity providing inadequate or misleading information to users of financial statements. For example, holdings of uncollateralized algorithmic stablecoins do not have the same underlying risks as fully collateralized stablecoins that may have a fiat redemption feature. Furthermore, we think that because of the lack of accounting guidance and significant

⁴ Source: <https://www.coindesk.com/grayscale-ceo-says-crypto-interest-is-rising-from-pension-endowment-funds/>; <https://news.bitcoin.com/coinbase-interest-pension-funds-hedge-funds-skyrocketed-institutional-holdings-soar-170/>

⁵ Entities that are not engaged in blockchain and crypto as a line of business

management judgment, an entity may account for stablecoins as intangible assets, inventory, or as financial instruments, thus leading to diversity in practice.

Question 2.2.

Chapter 6 and Paragraphs ES35 to ES46 of the executive summary section analyses three possible approaches on the way forward for addressing IFRS requirements. Chapter 6: Paragraph 6.26, Table 6.1 outlines the pros and cons of each option. The three options are as follows:

- Option 1: No amendment to existing IFRS requirements;
- Option 2: Amend and/or clarify existing IFRS requirements; and
- Option 3: A new Standard on crypto-assets (liabilities) or digital assets (liabilities).

Which of the three options do you consider to be the most appropriate solution to address IFRS requirements?

Alternatively, please elaborate if you consider there to be other possible approaches towards clarifying and developing IFRS requirements for crypto-assets.

If a new standard is to be developed, what should be in its scope?

15. We think that given the rapid growth of institutional participation and the continued maturity of the crypto ecosystem, there is a need to robustly address the IFRS requirements applicable to crypto-assets (liabilities), to ensure that users are provided with useful information.
16. Furthermore, it is our understanding that although blockchain native-assets have gained significant market attention, there are other traditional asset classes, such as equities, commodities, real estate and other non-native blockchain assets, that are being tokenized and traded on the blockchain. Therefore, we think a more comprehensive approach is needed when addressing the shortcomings of the accounting standards for the broader subsets of crypto-asset activities.
17. Although we favor option 3, the stakeholders that we consulted told us that they prefer option 2 as a timelier solution to address the current accounting challenges. As well, the crypto ecosystem continues to evolve and present new accounting challenges, therefore option 3 may be premature at this stage of the crypto ecosystem lifecycle.
18. Our recommendation is a phased approach to address the IFRS requirements for crypto-asset activities to mitigate the concerns raised by stakeholders, achieve future proofing of the accounting standards, and provide a more comprehensive long-term solution.

Phased approach

First Phase: An interim standard as a timely temporary solution

19. The first phase of the project could be the development of an interim standard to clarify how the existing IFRS requirements should apply to crypto-assets activities to ensure a timely solution to address the diversity in practice.
20. Stakeholders have told us that the recognition and measurement issues are the most time sensitive and critical areas that need clarification. These primary concerns highlighted were the accounting for prepayment tokens, crypto-asset mining activities, barter transactions and clarifying the eligibility to apply

IFRS 9 *Financial Instruments*. For example, there is a lack of clarity whether the newly mined crypto-assets and the transaction fees earned by crypto-asset miners may be recognized as revenue under IFRS 15 *Revenue from Contracts with Customers*, if no contract with a third party exists. Furthermore, we think that the IFRIC agenda decision on the holdings of cryptocurrencies could be reconsidered as part of this first phase.

21. We think that an interim standard would be a more efficient temporary solution than amending each of the respective existing IFRS Standards to clarify the accounting for crypto-asset activities.

Second Phase: Disclosure requirements

22. The second phase of the project can focus on addressing the disclosure shortcomings for the various crypto-asset activities. We think that the second phase can run simultaneously with the first phase, subject to capacity constraints, and once completed, included in the interim standard developed as part of the first phase. Furthermore, similar to phase one above, we think that this would be more efficient than amending the disclosure requirements in the existing standards.
23. The CPA Canada's Research, Guidance and Support [An Introduction to Accounting for Cryptocurrencies](#) publication and the more recent [CSA Staff Notice 51-363](#) provide suggestions on the types of additional disclosures entities engaged in crypto-asset activities can be mandated to provide to meet the disclosure requirements developed as part of this second phase and to help provide users with more useful information about their crypto-asset activities.

Third Phase: Develop a comprehensive new standard on crypto-asset activities

24. The third phase of the project can be the development of a comprehensive new standard that addresses all crypto-asset activities. We think that this phase of the project will take a considerably longer time to develop to address the many different types of crypto-assets in the market.
25. We think that crypto-assets are assets with unique characteristics and risks. Forcing crypto-assets (liabilities) into the existing accounting requirements as a long-term solution may not achieve fair presentation and useful information. Developing a specific standard to address crypto-asset activities will allow for a tailored solution specific to their nature and risks. Furthermore, trying to fit the more complex crypto-assets with hybrid features within the confines of the existing accounting requirements may create unnecessary noise and complexity in the financial statements.

Question 3 Accounting for holders

Question 3.1.

This DP (Chapter 3: Paragraphs 3.37 to 3.41) has identified that applicable IFRS Standards for crypto-assets holders (IAS 2 and IAS 38) do not explicitly address situations where crypto-assets are considered to be held as non-financial asset investments. Furthermore, as outlined in Chapter 3: Paragraphs 3.42 to 3.48, there are situations where the measurement requirements under IAS 2 or IAS 38 may not allow FVPL or FVOCI to reflect the economic characteristics of crypto-assets with trading or investment asset attributes. For example, under IAS 38, FVOCI is only allowed if there is an active market.

Do you agree that standard-setting activity is needed to address the limitations of IAS 2 and IAS 38 requirements towards addressing non-financial asset investments; namely that: IAS 38 does not allow

FVPL when cryptocurrencies are held as trading or investment assets; and IAS 38 does not allow fair value measurement when markets are inactive? Please explain.

26. We agree there is a need for standard-setting activity to address the limitations of the IAS 38 *Intangible Assets* requirements towards addressing non-financial asset investments, more specifically the holdings of cryptocurrencies.
27. As noted in our response to the [IFRIC Agenda Decision - Holdings of Cryptocurrencies](#), we are concerned with the IFRIC's observation that IAS 38 is applicable to the holdings of cryptocurrencies. The creation of IAS 38 was before a time that considered complex instruments such as cryptocurrencies. As a result, we have reservations about the appropriateness of the measurement model in IAS 38 in achieving fair presentation for holdings of cryptocurrencies. Furthermore, the stakeholders that we consulted told us that both the revaluation model and the cost model under IAS 38 do not appropriately capture the volatility and impact of cryptocurrencies on an entity's financial performance. We think a more proactive way of ensuring the appropriateness of reporting crypto-assets would be to undertake a project in this area given these concerns expressed with IAS 38's measurement model.
28. In our view, the fair value performance of a cryptocurrency is important to ensure a user's understanding of the entity's financial position and profit or loss. Furthermore, we think that the unique risk profile, price volatility and opaque characteristics of several cryptocurrencies may not always be comprehensively captured in the accounting requirements in IAS 38.

Question 3.2.

This DP (Chapter 3: Paragraphs 3.49 to 3.56) has identified the need to clarify the eligibility of some crypto-assets for classification as financial assets. There may be a need to update IAS 32 such that crypto-assets that have similar characteristics or functional equivalence to equity or debt securities (e.g. rights to profit, stakes in partnership arrangements, voting rights, right to cash flows from entities) but do not meet the current definition of financial assets under IAS 32. Alternatively, there may be a need to classify crypto-assets as a unique asset and to allow accounting treatment that is similar to that of financial assets where appropriate.

Do you agree that there is need to clarify crypto-asset holders' eligibility to apply IFRS 9? Please explain.

Do you have views on whether or not IAS 32 needs to be updated to include crypto-assets (tokens) with functional equivalence to equity or debt securities, within the IAS 32 definition of financial instruments (financial assets for holders and financial liabilities for issuers) or alternatively whether crypto-assets should be classified as a unique asset and allowing accounting treatment similar to financial instruments where appropriate? Please explain.

29. We agree that there is a need to clarify crypto-assets holders' eligibility to apply IFRS 9 as an interim solution.
30. IFRS 9 should consider whether crypto-assets that have equity-like features or cash-like features would be eligible for classification as a financial instrument. We think in many cases, having crypto-assets with equity-like or cash-like features classified as a financial instrument could result in more useful information

than the current classification of an intangible asset because the recognition and measurement requirements would better reflect the substance of these crypto-assets, which have the functional equivalence to equity or debt securities.

31. Although this could temporarily address the diversity in practice, it may not be a suitable long-term solution because treating crypto-assets with equity-like or cash-like features as financial instruments could give rise to significantly more complex accounting requirements for hybrid tokens that express the features of an equity instrument, utility token and/or a payment token. The Binance Coin (BNB) is an example of such a token with multiple features and use cases. Hybrid tokens with a combination of equity, payment and utility (loyalty program) characteristics are common in the crypto-ecosystem. We think that the bifurcation of these tokens into its equity, payment and utility components could prove very challenging and costly to prepare and may not result in useful information to users. Therefore, we think that a unique accounting standard on crypto-asset activities may explore alternate ways of providing more useful information to users.

Question 3.3.

This DP (Chapter 3: Paragraphs 3.57 to 3.63) has identified that the definition of cash or cash equivalents may need to be updated to include some of the stablecoins that are pegged to fiat currency on a 1:1 basis, cryptocurrencies that qualify as e-money and CBDCs. And that crypto-assets received in exchange for goods and services could also be treated as being equivalent to foreign currency.

Do you have views on whether or not the definition of cash or cash equivalents needs to be updated? Please explain.

32. We think that the definition of cash and cash equivalents needs to be revisited to provide more robust criteria on the specific instruments that are eligible to qualify as cash and cash equivalents. The current definition of cash is very loosely defined and therefore gives rise to several uncertainties as it relates to crypto-assets. Paragraph AG3 of IAS 32 *Financial Instruments: Presentation* defines cash as *a financial asset because it represents the medium of exchange and is therefore the basis on which all transactions are measured and recognized in financial statements*. Accordingly, to qualify as cash the instrument needs to be a financial asset. However, according to paragraph 11 of IAS 32, *a financial asset is any asset that is cash*, therefore creating a circular reference and placing the emphasis on whether the instrument is a *medium of exchange*. We think that this gives rise to the following questions about whether some crypto-assets should qualify for classification as cash:

- *Is designation as legal tender required for a financial asset to qualify as cash?*
For example, the acceptance of bitcoin as legal tender in El Salvador could give rise to entities with operations in El Salvador classifying their bitcoin balance as cash and cash equivalents.
- *Should payment tokens that are used as a medium of exchange on the blockchain qualify as cash?*
Cryptocurrencies such as Bitcoin and Ethereum are used as mediums of exchange in the blockchain ecosystem, and a question therefore arises whether these cryptocurrencies should qualify as cash. A few notable companies that are currently accepting cryptocurrencies as payment include Microsoft, Overstock, PayPal, Newegg and Whole Foods.⁶ We think that the continued adoption of

⁶ Source: <https://ca.finance.yahoo.com/news/10-major-companies-accept-bitcoin-110009655.html>

cryptocurrencies as a medium of exchange by non-native blockchain companies creates an increasing need for the reconsideration of the definition of cash under IFRS Standards.

- *Should the high volatility inherent to some crypto-assets preclude its eligibility to qualify as cash?*
Critics of bitcoin and other cryptocurrencies often indicate that the high volatility inherent to cryptocurrencies should preclude their classification as cash. However, there are several foreign currencies subject to high volatility and hyperinflation, that are not precluded from classification as cash.
- *Should there be a minimum transaction volume or cross chain acceptance of the token as a medium of exchange?*
Other considerations include, whether smaller payment tokens such as Zcash which has a market capitalization of USD 1.32 Billion⁷ and a much lower transaction volume than Bitcoin; or whether the token is accepted as a medium of exchange outside of its native blockchain could be eligible to qualify as cash.
- *Should stablecoins pegged to fiat currency, which are used as medium of exchange be assessed against the definition of cash or should they be assessed from the perspective of cash equivalents?*
Cash equivalents are defined in paragraph 6 of IAS 7 *Statement of Cash Flows*, as *short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value*. Stablecoins pegged to fiat currencies usually derive their value based on an underlying asset. Although most stablecoins may have the same purpose of providing its holders the ability to reduce exposure to crypto-assets with high volatility and by functioning as a medium of exchange in the crypto ecosystem, not all stablecoins pegged to a fiat currency have the same characteristics. Some stablecoins may have a cash redemption feature and are managed by a centralized organization which may create a contractual obligation with the stablecoin holder. One may also question whether there is a need for stablecoins to be collateralized for it to qualify as cash. The existence of a legally enforceable right to the residual interest in a collateralized stablecoin could result in such stablecoins having equity like features. The lack of classification guidance under IFRS Standards could result in assessing stablecoins against the definition of *cash* or that of *cash equivalents* depending on the facts and circumstances and management judgment. The lack of clear guidance could also result in classifying stablecoins as financial assets, equity instruments, intangible assets or as inventory, thus increasing the risk of diversity in practice.

Central Bank Digital Currencies (CBDCs)

33. To the extent that CBDCs are deployed, we think consideration needs to be given whether these should qualify for classification as cash. Although most CBDCs are still in development, CBDCs are different from stablecoins, in that CBDCs represent a claim against the issuing central bank. It is our understanding that all the different variations of CBDCs contemplated by the Bank of International settlements continue to include a claim against the issuing central bank.⁸ Therefore, CBDCs could more easily meet the eligibility requirements for a financial instrument and cash.

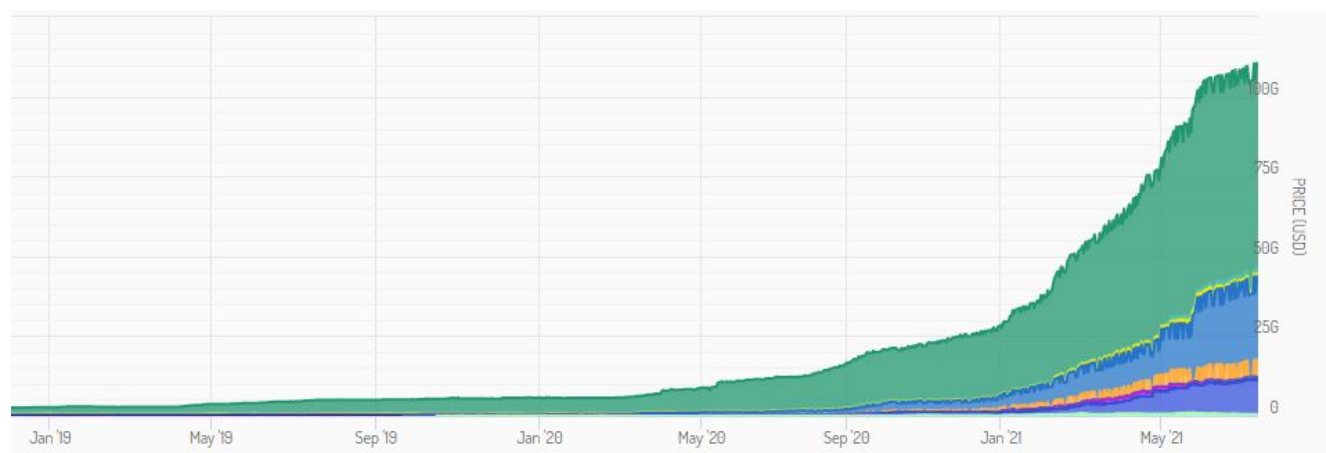
⁷ Market capitalization as of July 12, 2021

⁸ Source: <https://www.bis.org/publ/arpdf/ar2021e3.htm>

Stablecoins

34. Stablecoins were created to manage price swings often seen in other more volatile cryptocurrencies and to serve as the payment rails outside of the traditional financial system. Stablecoins are neither pre-mined nor minable, instead, the total supply of stablecoins constantly changes and reacts to the movement in the market.⁹ Stablecoins play a critical role in ensuring the efficiency and in maintaining the capital within the crypto ecosystem, by reducing the interactions with the traditional financial system and allowing for near instant settlement with finality.
35. Stablecoins represent a significant proportion of market capitalization of the crypto ecosystem. As of July 13, 2021, the market capitalization of Tether (USDT) and USD Coin (USDC), the top two stablecoins, was USD 64.37 Billion and USD 26.57 Billion respectively.¹⁰ The growth in the market capitalization of stablecoins has been increasing significantly since 2018 and this growth is an indication of the importance of the stablecoin market and the urgent need for the IASB to clarify the accounting for stablecoins.

Market capitalization of stablecoins since 2019



Source Stablecoin Index (market capitalization)⁹

36. Recently, Visa announced that it will allow users to settle transactions in USDC, and Mastercard announced that it plans to use USDC as the bridge asset for cardholders that want to pay for their goods and services in cryptocurrencies.^{11, 12} Accordingly, this will remove hurdles for crypto firms that previously had to switch between crypto and fiat to interact with Visa and Mastercard. These developments by traditional finance companies in the crypto space are indicative of the anticipated use and adoption by more entities over time.

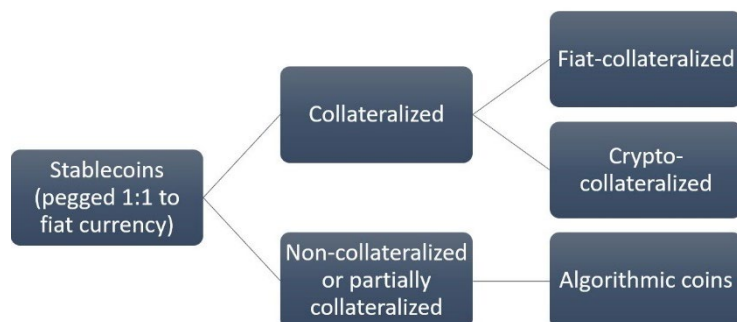
⁹ Source: <https://crypterium.com/news/post/stablecoins-definition-four-types-explained>

¹⁰ Source: <https://stablecoinindex.com/marketcap>

¹¹ Source: https://www.coindesk.com/visa-uses-anchorage-to-settle-usdc-transaction-on-ethereum-in-further-crypto-push?utm_source=Sailthru&utm_medium=email&utm_campaign=NODE%20MARCH%2029%202021&utm_term=Blockchain%20Bites

¹² Source: https://www.coindesk.com/mastercard-to-test-usdc-for-payments-as-stablecoin-scrutiny-intensifies?utm_source=Sailthru&utm_medium=email&utm_campaign=THE%20NODE%20JULY%2020%202021&utm_content=A&utm_term=The%20Node

37. Stablecoins are categorized as follows¹³:



Fiat-collateralized stablecoins

38. Fiat-collateralized stablecoins are usually fully collateralized and are pegged on a 1:1 ratio to fiat currencies like the US dollar (USD). Circle’s USDC¹⁴ has a redemption feature that allows its users to receive a payout from their stablecoin balance directly to their traditional bank account.¹⁵ However, very few stablecoins in practice have a redemption feature. Most fiat-collateralized stablecoins, such as USDT and USDC, operate on centralized systems.

Crypto-collateralized stablecoins

39. Crypto-collateralized stablecoins are backed by other crypto-assets and are usually over-collateralized to compensate for the increased volatility in the value of other crypto-assets. The stability of these stablecoins depends on a series of complex processes that are written into the smart contract to regulate the demand, supply, and governance of the underlying assets. MakerDAO’s DAI stablecoin is an example of a crypto-native decentralized, over-collateralized stablecoin that attempts to maintain a 1:1 ratio with USD.

Non-collateralized or fractional algorithmic stablecoins

40. Algorithmic stablecoins can be non-collateralized or partially collateralized (fractional-algorithmic or hybrid-algorithmic) stablecoins. These stablecoins are governed by complex algorithms that attempt to maintain the 1:1 ratio with the respective fiat currency. Many algorithmic stablecoins are based on a two-token system consisting of one pegged asset and a second speculative asset. The pegged asset maintains stability through the speculative asset absorbing the volatility of the system as well as incentivizing its users to profit from deviations from the pegged ratio. TerraUSD and FRAX are examples of algorithmic stablecoins pegged on a 1:1 ratio with USD.

¹³ Source: <https://crypterium.com/news/post/stablecoins-definition-four-types-explained>

¹⁴ Circle is the principal operator of USDC, a regulated and fully reserved dollar digital currency

¹⁵ Source: <https://developers.circle.com/docs/payouts-quickstart>

Risks

41. Although stablecoins may provide safety from the high levels of volatility in crypto-markets, they do pose significant risks to their holders. Several attempts to create crypto-native algorithmic stablecoins have failed, resulting in large losses for their holders.
42. In May 2021, TerraUSD fell below its peg for several days due to a combination of the LUNA price crashing and several collateral liquidations in Anchor.¹⁶ MakerDAO's DAI is also prone to drastic price shocks when the system faced overwhelming pressure from large decreases in the value of the collateralized crypto-assets. In March 2020 MakerDAO systematically failed resulting in 5.67 million DAI in losses.¹⁶ Concerns have also been raised about the opacity of Tether's operations, as critics continue to question USDT's backing by a significant portion of unspecified commercial paper.¹⁷
43. The increased adoption of fiat-collateralized stablecoins may result in the creation of collateral silos, which may contribute to the scarcity of safe assets in the traditional financial markets and regulatory intervention to manage the impact on these markets.¹⁸ Regulatory intervention over the stablecoin market may also impact the accounting classification of stablecoins.

Our view on stablecoins

44. Despite these prevailing risks, we think that the growth of the stablecoin market capitalization and traditional institutions participation in this space is a clear indication that there is a need for clarification of the accounting treatment for stablecoins. Recent and future developments by payment giants such as Visa and Mastercard may provide stablecoins pegged to fiat currencies the functional equivalence to fiat currency.
45. Overall, we think accounting guidance should consider whether stablecoins that are pegged to a fiat currency on a 1:1 basis should be eligible for classification as cash and cash equivalents. However, given that not all stablecoins have the same attributes, collateralization, risk profiles and redemption features, we think that at a minimum, the cash and cash equivalents note should include a reconciliation based on categorization of the various stablecoins, i.e., fiat-collateralized, crypto-collateralized, non-collateralized algorithmic and fractional-algorithmic stablecoins. An entity should separately identify each stablecoin listed under the respective category, because stablecoins may carry additional unique risks and characteristics. Narrative disclosures could help users better understand the nature, risks and characteristics of the various specific stablecoins and ensure that users are provided with useful and transparent financial reporting.

Our view on cryptocurrencies other than stablecoins

46. We think that cryptocurrencies such as Bitcoin and Ethereum that function solely as a fungible payment token, store of value, unit of account and a medium of exchange could also be eligible for recognition as cash. Cryptocurrencies such as Bitcoin and Ethereum, have a functional equivalence of cash in the digital ecosystem. *Visa recently reported that more than \$1 billion was spent on crypto-linked Visa cards in the*

¹⁶ Source: <https://thedefiant.io/why-algorithmic-stablecoins-will-fullfill-satoshis-dream/>

¹⁷ Source: <https://www.coindesk.com/tether-first-reserve-composition-report-usdt>

¹⁸ Source: <https://www.ft.com/content/863fdb33-a756-4a17-a788-21e8095d7b75>

*first half of 2021 after partnering with over 50 crypto platforms to enable crypto payments.*¹⁹ These and other developments by traditional finance companies are indicative of the potential mainstream adoption of crypto-assets as a medium of exchange in the future.

47. However, if cryptocurrencies are eligible for classification as cash, we think there is a need for robust disclosure requirements to ensure that the nature, risk, and characteristics of each cryptocurrency classified as cash are clearly communicated to users.

Question 3.4.

This DP (Chapter 3: Paragraphs 3.79 to 3.93) proposes that the clarification of IFRS requirements is needed for holders on behalf of others (e.g. custodial services) including on interpretation of the indicators of economic control.

Clarification is also needed for accounting by holders of utility tokens and hybrid tokens, and for holdings arising from barter transactions and proof-of-work mining activities (Chapter 3: Paragraphs 3.64 to 3.76). For hybrid tokens, there is a question of whether the predominant component should be considered or if/how bifurcation principles should be applied to determine their classification and measurement. For utility tokens, there is also a question of the appropriate recognition and measurement of atypical tradeable rights (e.g., rights to update network functionality; and rights to contribute resources and effort to the system) and the lack of IFRS guidance for prepayment assets.

Do you agree that the aforementioned areas need clarification in IFRS requirements as has been identified in this DP? Please explain.

48. We agree that all the aforementioned areas need clarification in IFRS requirements as identified in the DP. The stakeholders that we consulted, told us that there is a need for standard setting to address these areas to ensure less diversity in practice and more useful financial reporting. Stakeholders also told us that other related matters need clarification under IFRS Standards such as the accounting for airdrops, prepayment tokens and Simple Agreements for Future Tokens (SAFTs).
49. We think that there is a growing urgent need to address the accounting for proof-of-work mining, given the growth in the number of entities partaking in crypto-mining activities and applying IFRS Standards as their financial reporting framework. Furthermore, the stakeholders that we consulted told us that there are some companies with traditional lines of business that are using excess power capacity to engage in mining activities to derive additional income.
50. The stakeholders that we consulted told us that they are anticipating an increasing number of crypto-asset trading platforms that will begin operating in Canada given the regulatory clarification on the requirements applicable to such trading platforms. As a result, we think the clarification of the accounting requirements for custodial holdings should be addressed under IFRS Standards to prevent any resulting diversity in practice.
51. We also think that the growth of hybrid and community tokens needs to be closely monitored, to observe how entities applying IFRS Standards engage with these crypto-assets. We think that these multiple use

¹⁹ Source: https://news.bitcoin.com/visa-cryptocurrency-card-australian-startup/?ref=coingecko&utm_medium=email&utm_source=coingecko&utm_content=%F0%9F%9A%80+Sam+wants+Goldman%3F+%F0%9F%92%B0&utm_campaign=CoinGecko+Newsletters

cases could create accounting complexity and may need to be carefully studied to ensure an appropriate accounting solution is developed.

Question 4 - Accounting for issuers

Question 4.1.

This DP (Chapter 4: Paragraphs 4.23 to 4.29) concludes that in the absence of clarification by the IASB, the preliminary conclusion of this research is that ICO issuers (and issuers in similar offerings) can apply one or a combination of the following IFRS Standards: IFRS 9 Financial Instruments, IAS 32 Financial Instruments: Presentation, IFRS 15 Revenue from Contracts with Customers, IAS 37 Provisions, Contingent Liabilities and Contingent Assets and IFRS 13 Fair Value Measurement.

Do you consider that existing IFRS Standards provide a suitable basis to account for crypto-liabilities by issuers of ICOs, IEOs and STOs? Please explain.

52. Although ICOs, IEOs and STOs are not currently prevalent among Canadian entities applying IFRS Standards, we think a comprehensive standard should be developed to address more holistically the accounting for crypto-asset activities, which would include the accounting for crypto-liabilities by issuers. As noted in our response to question 2.2, the accounting for crypto-liabilities for issuers could be addressed in the third phase of the overall project.
53. While we think that the existing accounting standards can provide an interim solution for addressing the accounting challenges faced by token issuers. However, standard setting may be required to address more complex hybrid token issuances and any diversity in practice should token offerings become more prevalent.

Question 4.2.

The DP (Chapter 4: Paragraph 4.28) highlights a number of areas that could pose concerns with the application of IFRS 15 for an entity issuing crypto-assets through ICOs (or other offerings such as IEOs and STOs).

In cases when an issuing entity establishes that the issuance of crypto-assets falls within the scope of IFRS 15, which areas, if any, would you consider need further guidance/clarification for an entity to apply the principles in IFRS 15? Please explain.

54. Despite token offerings by entities applying IFRS Standards not being prevalent, we think that clarification of the accounting requirements for issuances that fall within the scope of IFRS 15 should be considered as part of the third phase²⁰ of the project on crypto-asset activities. Furthermore, we think that this area becomes more complex when it involves the issuance of hybrid tokens with utility features.

Question 4.3.

The DP (Chapter 4: Paragraphs 4.25 and 4.29) highlights a number of areas that could pose concerns with the application of IAS 37 for an entity issuing crypto-assets through ICO (or other offerings such as IEOs and STOs).

²⁰ Refer to our response to question 2.2 for our recommendation on a phased approach to the address the IFRS requirements for crypto-asset activities.

In cases when an issuing entity establishes that the issuance of crypto-liabilities qualify as a financial liability under IAS 32/IFRS 9 or as a provision under IAS 37, which areas, if any, would you consider need further guidance/clarification for an entity to apply these Standards? Please explain.

55. It is our understanding that ICOs, IEOs and STOs are not currently prevalent among Canadian entities applying IFRS Standards and that the current accounting guidance under IAS 32, IFRS 9 and IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* will suitably address these token issuances. However, as noted above we think that hybrid token issuances will require further guidance or clarification to ensure an optimal accounting outcome that results in useful information.

Question 5 - Valuation

Question 5.1.

The DP (Chapter 5: Paragraphs 5.44 and 5.45) observes that when considering fair value measurement under IFRS 13, determining an active market for crypto-assets is not always straightforward.

Do you consider that the guidance in IFRS 13 provides an adequate basis to determine an active market for crypto-assets (and, if applicable, related crypto-liabilities) when these are measured at fair value?

56. We are not aware of any concerns with regards to whether the guidance in IFRS 13 *Fair Value Measurement* provides an adequate basis to determine an active market for crypto-assets. The stakeholders that we consulted told us that IFRS 13 is working well and adequately addresses any valuation concerns with the current accounting requirements.

Question 5.2.

The DP (Chapter 5: Paragraph 5.42) observes that there is an emergence of valuation methodologies, that might differ from the fair value measurement guidance in IFRS 13, tailored for crypto-assets.

In the absence of an active market under IFRS 13, do you consider that IFRS 13 provides an adequate basis to determine an appropriate valuation technique to measure crypto-assets (and, if applicable, related crypto-liabilities) at fair value? If not, what alternative measurement bases do you propose?

57. Based on the feedback that we heard from stakeholders, we are not aware of any concerns in this regard. However, we think that valuation challenges may occur with emerging issues such as decentralized finance and non-fungible tokens, which we discussed in more detail in our response to question 6.

Question 6 – Other

Question 6.1

Do you have other comments on the accounting for crypto-assets (liabilities), or on any other matter in the DP not addressed by the above questions?

58. We think IFRS requirements should consider emerging issues, such as decentralized finance and non-fungible tokens as part of the third phase²¹ of the overall project.

Decentralized Finance (DeFi)

59. DeFi encompasses the provision of financial services through decentralized applications on the blockchain. DeFi uses open protocols that allow financial services to be programmatically combined in flexible ways.²⁰

60. DeFi comprises six service categories, being stablecoins, exchanges, credit markets, derivatives, insurance, and asset management.²² Of these DeFi service categories, we think that lending to exchanges, credit markets and derivatives are likely to pose accounting challenges. We highlighted the accounting concerns for stablecoins in our response to question 3.3. We are not aware of any DeFi exchanges that provide financial reporting under IFRS standards.

61. Most DeFi services incorporate token-based incentive structures for securing liquidity and the governance of the protocol. DeFi arrangements often require crypto-asset holders locking up their crypto-assets with the protocol's liquidity pool in order to receive payments that represent the yield generated on their locked assets. DeFi users borrowing crypto-assets from the protocol pay fees to access crypto-assets from the liquidity pool.

62. The following mechanisms for earning a yield or rewards are possible from a DeFi service²³:

- *Lock-up yields* – Crypto-asset holders earn interest for immobilizing crypto-assets in pools, where they serve as liquidity or collateral for the DeFi service. Under *Staking* arrangements Crypto-asset holders holding a crypto-asset which operates on a proof-of-stake protocol, may contribute their crypto-assets to a staking pool or directly stake their crypto-assets in return for earning rewards. Some projects award governance tokens to staking participants, which give holders a say in future changes and upgrades to that protocol.²⁴
- *Liquidation fees* – Crypto-asset holders act as market-makers and receive a fee based on a percentage of the value of under-collateralized, liquidated loans.
- *Liquidity mining* – Crypto-asset holders earn rewards in the form of tokens issued by the DeFi service itself usually in return for supplying crypto-asset pairs into liquidity pools.

63. DeFi credit service applications are an open source and non-custodial liquidity protocols for earning interest on deposits and borrowing assets. These applications usually operate via smart contracts on the blockchain.

²¹ Refer to our response to question 2.2 for our recommendation on a phased approach to the address the IFRS requirements for crypto-asset activities.

²² Source: DeFi Beyond the Hype: The Emerging World of Decentralized Finance; <https://wifpr.wharton.upenn.edu/wp-content/uploads/2021/05/DeFi-Beyond-the-Hype.pdf>

²³ Source: DeFi Beyond the Hype: The Emerging World of Decentralized Finance; <https://wifpr.wharton.upenn.edu/wp-content/uploads/2021/05/DeFi-Beyond-the-Hype.pdf>

²⁴ Source: <https://www.coinbase.com/learn/crypto-basics/what-is-staking>

64. We are not aware of any DeFi applications that provide financial reporting under IFRS Standards. The accounting considerations therefore arises from the perspective of lenders and borrowers that use DeFi applications and that report under IFRS Standards.
65. When lenders commit capital to DeFi credit services, they receive platform-native tokens representing an interest earning representation of their deposit in the form of a token (*interest earning token*). Borrowers accessing capital from the protocol are usually required to deposit collateral in excess of the value of borrowed before being able to access the capital required. Lenders and borrowers continue to maintain full custody over their crypto-assets and can liquidate their assets at any time. Credit terms under these arrangements can be complex. Furthermore, there are valuation challenges with the *interest earning token* which is also capable of being securitized and traded.
66. We think that opaque rights and obligations, complexity and unique terms applicable to DeFi lending arrangements may present accounting challenges. Furthermore, accounting challenges may also arise due to the enforceability, valuation, and the evaluation of whether the borrowing arrangements contain embedded derivatives. The stakeholders that we consulted told us that there is no clear guidance on how to account for staking rewards. For example, should an entity account for staking rewards as interest income or should it be accounted for as other income.
67. As DeFi matures and becomes less risky, we think that institutions holding large crypto-assets balances over the long term may look to earn a yield on their investments and take advantage of the lucrative yields offered by DeFi protocols. Moreover, the continued suppression of yields by central banks around the world may catalyze the mainstream adoption and use of DeFi protocols.

*Non-fungible tokens (NFTs)*²⁵

68. NFTs represent ownership of items in the tangible and intangible property domains that are not interchangeable for other items because of their unique properties. NFTs can only have one official owner at a particular point in time and are secured by the blockchain. The growth potential for NFTs is exponential since it provides the mechanism for the tokenization of all real-world assets. Furthermore, NFTs provide credence to the internet of things concept and could deliver cost efficiencies from being instantly transferable, storable, and permitting easy verification of ownership.
69. NFTs by their inherent design offers the potential to enhance or unlock liquidity for a wide range of non-native blockchain assets, such as real estate, collectibles, song files, customer loyalty points and artwork. NFTs also allow creators to retain ownership rights over their work and claim resale royalties directly via smart contract coding. Furthermore, NFTs also allow for fractional ownership to allow for greater liquidity of very high value items that would not be easy to liquidate.
70. With valuable assets such as artwork, real estate and cars being representable on the blockchain, this will allow for NFTs to serve as collateral in decentralized loans. Therefore, the interaction of DeFi and NFTs in several interesting ways is a strong possibility since both use the Ethereum blockchain infrastructure.
71. Although the NFT space is still an experimental and emerging space, the blockchain infrastructure already exists and some entities are already participating in these opportunities. For example, during our outreach, a stakeholder informed us of a company that was able to unlock liquidity through onboarding its real estate property as an NFT on the blockchain. Therefore, we think that the developments in the NFT markets should be closely monitored for any accounting challenges that may arise.

²⁵ Source: <https://ethereum.org/en/nft/>