



Federal Reserve Bank
of San Francisco

Crypto and Accounting Implications

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Your presenters today




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The views expressed in this presentation are our own and do not necessarily reflect those of the Federal Reserve Bank of San Francisco or the Federal Reserve Board of Governors.



Today's key take-aways

Growing demand among consumers

Retail interest in crypto expected to persist; strong interest in purchasing from banks

Current accounting classification for crypto is complicated

Most crypto is treated as intangible assets; stablecoins differ

Accounting treatment will shape how crypto is integrated into the banking system

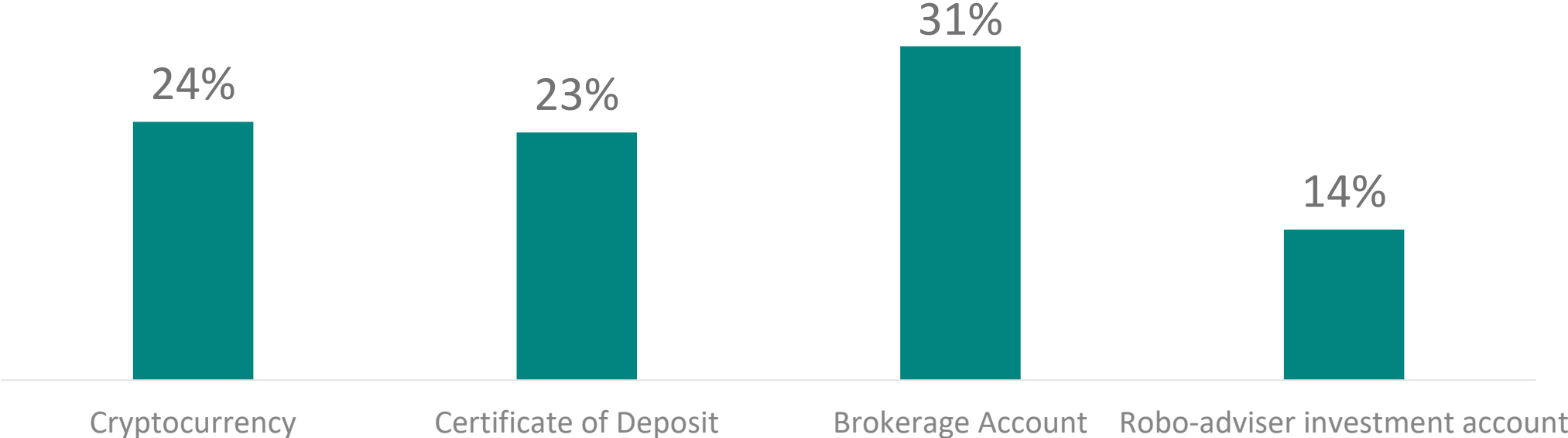
Capital treatment of crypto on bank balance sheet still being debated



Nearly 1 in 4 American households own cryptocurrency

Cryptocurrency ownership is outpacing consumption of popular financial services

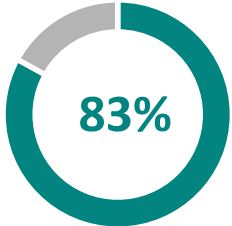
% ownership among US households surveyed Dec 2021



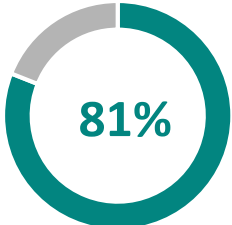
Source: Q1 2022 The State of Consumer Banking & Payments by Morning Consult



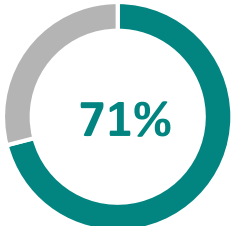
Most current crypto holders want to buy & hold crypto with their banks



Would be interested in earning interest in Bitcoin on an account such as savings, money market, or CD



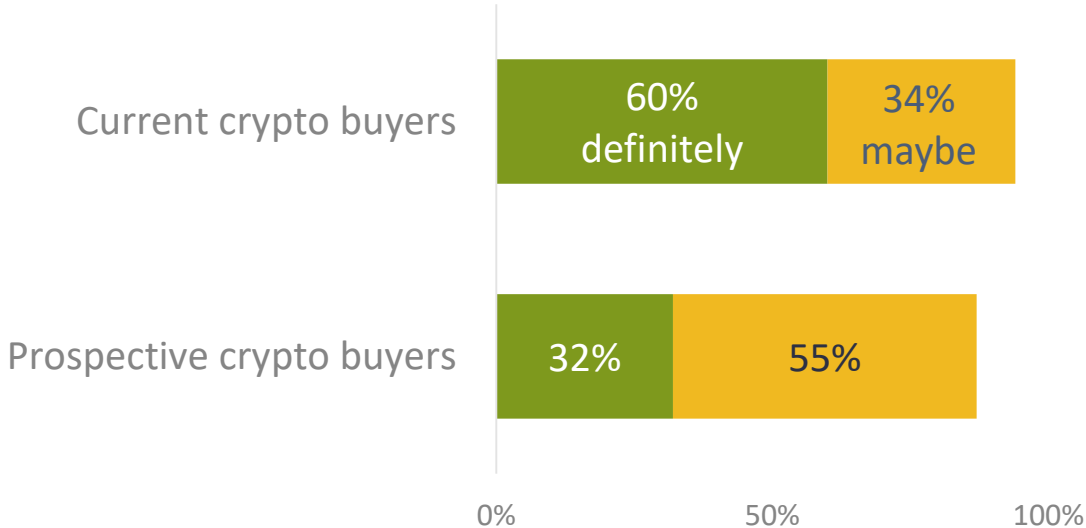
Would be interested in buying Bitcoin through my bank



As a Bitcoin holder, I would switch my primary bank to a bank that offered Bitcoin-related products

Source: NYDIG Survey: Bitcoin and Banking, January 2021 [Link](#)

If your bank gave you the ability to invest in cryptocurrencies, how likely would you be to use it?

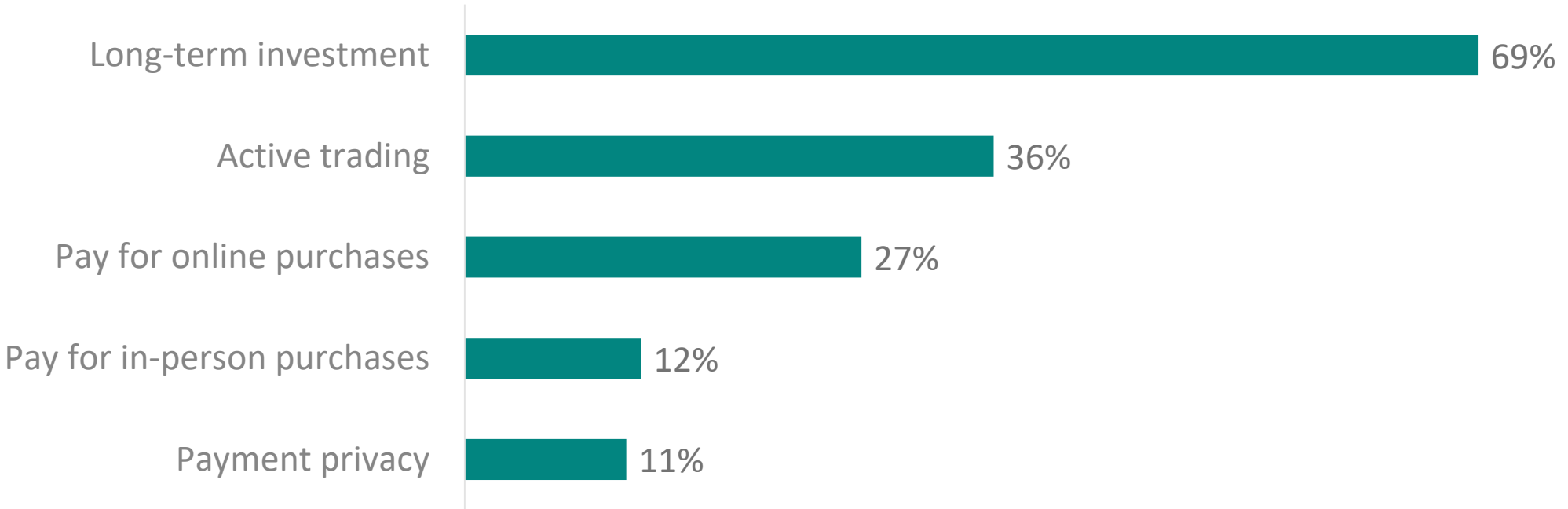


Source: Cornerstone Advisors Survey, December 2020



They are largely motivated by long-term price appreciation

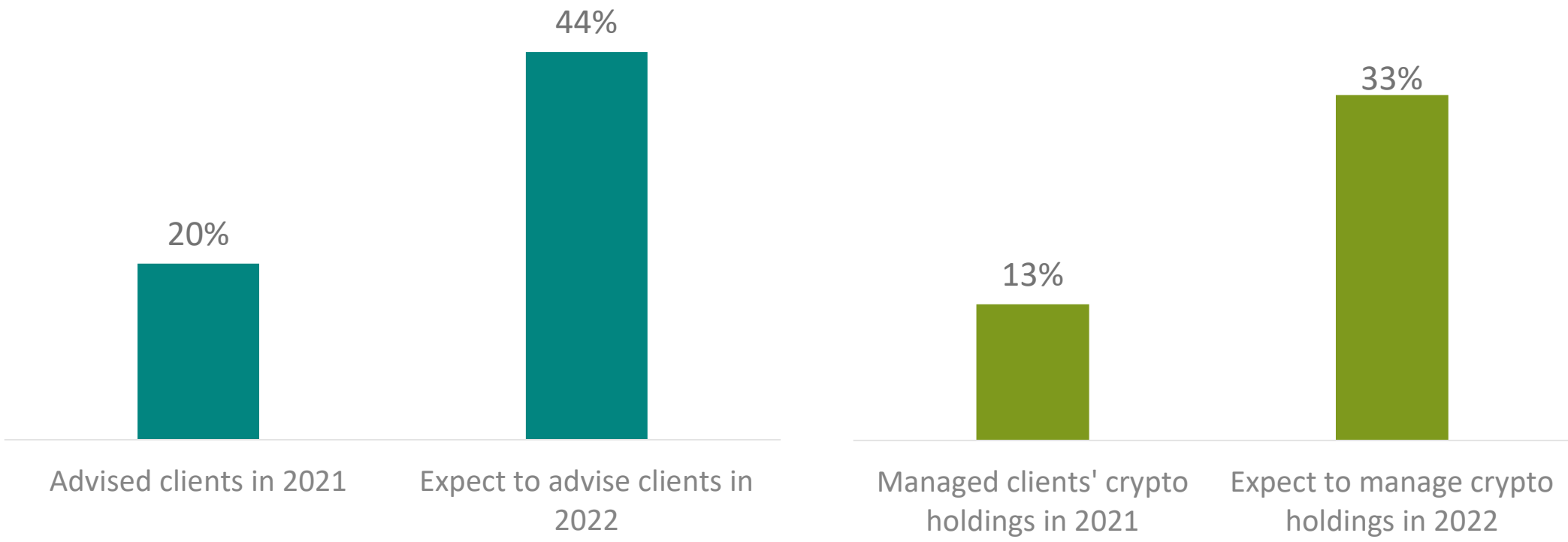
Reported reasons for buying cryptocurrencies



Source: Gemini 2021 The State of U.S. Crypto Report



Financial advisors are preparing for a surge in client interest this year



Source: "Flexibility, Fear and Fortitude: Finance Faces the Future" report by Arizent, compiled from research conducted October 2021





What are the challenges for crypto in banking?

Need for greater clarity

2022 Cryptoasset Roadmap Developed by Federal Reserve, FDIC, and OCC

Greater clarity on legal permissibility, safety & soundness expectations, consumer protection and compliance related to:

- Crypto-asset safekeeping and traditional custody services
- Ancillary custody services
- Facilitation of customer purchases and sales of cryptoassets
- Loans collateralized by cryptoassets
- Issuance and distribution of stablecoins
- Activities involving the holding of crypto-assets on balance sheet

Source: Joint Statement on Crypto-Asset Policy Sprint Initiative and Next Steps released November 23, 2021



GAAP treats most crypto on balance sheet as intangible assets

Balance sheet classification	Meet GAAP definition?	Rationale
Cash and cash equivalents	No	Not legal tender and not backed by a sovereign government
Financial instruments	No	Not cash or an ownership interest in an entity, and do not represent the contractual rights to receive cash or another financial instrument
Inventories	No	Not tangible, and therefore do not meet definition of inventory
Intangible assets	Yes	Assets that lack physical substance and do not fall within scope of other classifications

Stablecoins are different

What is the accounting treatment?

Absent complicating features, many are expected to be financial instruments, for which the fair value option is available. Other classifications are possible under various structures (derivative, debt, equity, receivable, etc).

Must consider specific facts and circumstances:

- Purpose
- Legal form
- Rights and obligations of the holder
- Issuing entity
- Stability mechanism
- Redemption features
- Collateralization
- Credit or liquidity risks

For most stablecoins, 1 unit ~ 1 US dollar



Accounting challenges for banks holding crypto on balance sheet

Indefinite-life intangible assets

- Initially measured at cost
- Impairment recognized for observed decreases in price (lowest observed)
- Subsequent increases in fair value not recognized until sale of the asset
- NO FAIR VALUE OPTION

Exceptions

- Crypto assets held by an entity that applies industry-specific guidance provided in ASC 940 (broker-dealers) or ASC 946 (investment companies) able to account for at fair value



Fair value considerations

Fair value, liquidity, and leveling

- Fair value = price that would be received to sell an asset in an orderly transaction between market participants at the measurement date
- Fair value hierarchy gives priority to quoted prices in active markets (Level 1) and lowest priority to unobservable inputs (Level 3)

Understand the source and reliability of pricing data

- Time stamping convention
- Crypto to USD versus Crypto to Stablecoin volume
- Regulated versus unregulated exchanges
- Potential for wash sales



Should crypto be on-balance sheet if held as a custodian or collateral?

Official Answer: It depends. Consider:

- Specific terms of the arrangement
- Applicable laws and regulations
- Legal ownership of the assets
- Who has control?

Unofficial Answer: Probably not for banks, but more complicated than traditional assets:

- Novel functionality, storage, and terms
- Talk to your accountants and lawyers
- More analysis and documentation may be needed to support the accounting treatment
- An on-balance sheet conclusion would result in an accompanying liability that may have an embedded derivative



What about capital treatment of
crypto?

Capital considerations

Goodwill and Intangibles historically excluded from regulatory capital due to the high level of uncertainty to realize value from these assets, especially under adverse financial conditions.

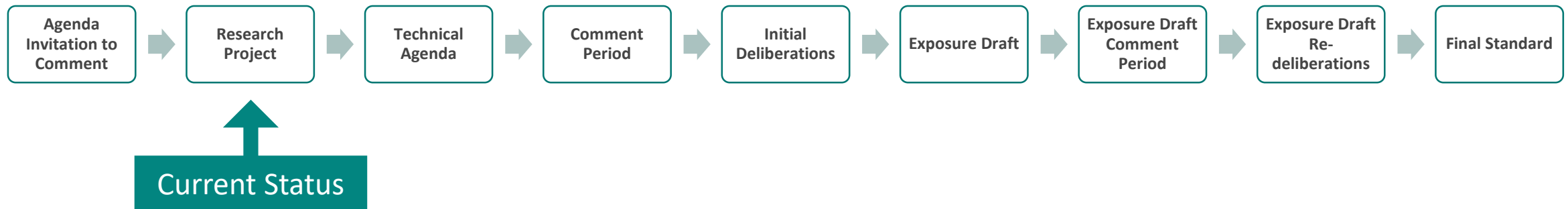
Basel Committee on Banking Supervision: Consultative Document

Group 1a: tokenized traditional assets	Treated equivalent to the traditional assets, if they have the same legal rights as direct ownership. Not met if they first need to be redeemed or converted.
Group 1b: cryptoassets with stabilization mechanisms	Risk-weight based on risk from holding the underlying traditional asset AND default risk of the issuer/redeemer.
Group 2: other non-intangibles (e.g., cryptoasset ETFs, derivatives, etc.)	Simple and conservative: 1250% risk weight. Similar in effect to deduction of the asset from capital but can also be applied to short positions.
Other considerations	Pillar 1 operational risk add-on charge for all Group 1 exposures?



Is the accounting treatment set in stone? Not necessarily

Accounting Standard Setting



- Agenda comment period has concluded
- Research project added: Accounting for and disclosure of a subset of exchange-traded digital assets and exchange-traded commodities

Sydney Smith (1771 – 1845)

English wit, writer, and Anglican cleric.



“We shall generally find that the triangular person *has* got into the square hole, the oblong *into* the triangular, and a square person *has* squeezed himself into the round hole. The officer and the office, the doer and the thing done, seldom fit so exactly that we can say they were made for each other.”

Questions?