

To the Point

SEC – Staff Accounting Bulletin

SEC staff issues guidance on obligations to safeguard crypto assets

When an entity is obligated to safeguard a platform user's crypto assets, the staff says it is appropriate for the entity to present a liability and a related asset measured at the fair value of the user's crypto assets.

What you need to know

- ▶ The SEC staff issued interpretive guidance regarding the accounting for obligations to safeguard the crypto assets that an entity holds for platform users.
- ▶ The staff believes these entities should present a liability for the obligation to safeguard the users' assets and should measure the liability at the fair value of those assets.
- ▶ The staff also believes that it would be appropriate for the entity to recognize an asset at the same time it recognizes a liability that is equal to the fair value of the crypto assets it is responsible for safeguarding. Both the asset and the liability should be measured at fair value at each subsequent reporting date.
- ▶ The SAB says the staff expects certain disclosures about these types of arrangements given the significant risks and uncertainties associated with holding crypto assets. The SAB also includes transition guidance to address how quickly the staff expects entities to apply the guidance.

Overview

The Securities and Exchange Commission (SEC or Commission) staff issued [Staff Accounting Bulletin \(SAB\) No. 121](#) to provide interpretive guidance regarding the accounting for obligations to safeguard the crypto assets¹ that an entity holds for platform users.

The SEC staff issued this guidance to address the recent increase in the number of entities that offer platform users the ability to transact in crypto assets. These entities also often provide services that obligate them or their agents to safeguard users' crypto assets, including holding the cryptographic key information that provides access to the assets on the distributed ledger or blockchain.

The staff believes that there are unique risks and uncertainties associated with these types of arrangements. These risks include technological risks (e.g., safeguarding the assets), legal risks (e.g., the lack of legal precedent for crypto assets) and regulatory risks (e.g., fewer regulatory requirements for holding crypto assets on behalf of platform users compared with those for arrangements to safeguard assets for third parties) that the staff believes could significantly impact an entity's operations and financial condition. The SAB provides recognition, measurement and disclosure guidance to enhance information about these risks provided to financial statement users.

SEC Commissioner Hester Peirce issued a [statement](#) in response to the SAB.

Key considerations

Recognition and measurement

When an entity² is responsible for safeguarding a user's crypto assets (including holding the cryptographic keys used to access those assets), the SEC staff believes the entity should present a liability on its balance sheet to reflect its obligation to safeguard the assets. The staff also believes it would be appropriate for the entity to recognize an asset that is separate and distinct from the user's crypto assets at the same time it recognizes the safeguarding liability, similar to an indemnification asset³ in a business combination.

The SAB states that the staff believes it would be appropriate for the entity to measure at initial recognition and each subsequent reporting date both the liability and the related asset at the fair value⁴ of the crypto assets held for its users. Further, the entity should evaluate whether any potential loss events (e.g., theft, loss or destruction of the cryptographic keys) affect the measurement of the asset.

Disclosure

Given the significant risks and uncertainties associated with safeguarding users' crypto assets, the SEC staff believes there are several financial statement disclosures that an entity should include in the notes to the financial statements, such as the nature and amount of crypto assets that the entity holds for its users, including a separate disclosure for each significant crypto asset, and any vulnerabilities that may arise as a result of any concentration in crypto assets.⁵

Because both the safeguarding liability and the related asset are measured at fair value, the SAB states that entities must also include the disclosures required by the fair value measurement guidance.⁶ Further, the accounting for the safeguarding liability and related asset should be disclosed in the footnotes.⁷ The staff believes that the disclosure should also include information about who is responsible for the record-keeping of the crypto assets, the holding of the cryptographic keys to access the crypto assets and safeguarding the assets from potential loss or theft.

The SAB states that there also may be other disclosures that are required outside of the financial statements under existing Commission rules, including the description of business, risk factors or management's discussion and analysis of financial condition and results of operations.⁸ The SEC staff provided the following examples of the types of items that may need to be disclosed:

- If material, the types of losses or obligations that could occur as a result of risks associated with holding crypto assets (e.g., the loss of platform users or customers, litigation, reputational damage and regulatory enforcement actions)
- The entity's assessment of legal ownership for the crypto assets held for platform users and whether those assets could be used to satisfy the entity's creditors in the event of bankruptcy
- The potential effect of loss, theft, compromise or any other form of unavailability of the cryptographic key information on the entity's business (e.g., the effect on its financial condition, operating results, cash flows)
- Mitigation steps that the entity has taken to address the risks associated with safeguarding the user's crypto assets (e.g., insurance policies held by the entity)

Transition

The SAB includes transition guidance for SEC registrants⁹ and certain other entities¹⁰ for applying the interpretive guidance. The transition guidance for these entities is included in the table below:

	SEC registrants	Other entities
Initial application	Apply to an entity's financial statements covering the first interim or annual period ending after 15 June 2022.	Apply to an entity's financial statements beginning with the next submission or filing with the SEC.
Transition method	Retrospective application as of the beginning of the fiscal year to which the interim or annual period relates. The effect of initial application should be reported in the carrying amounts of assets and liabilities as of the beginning of the annual period specified above.	If the filing includes a subsequent interim period that reflects this guidance, apply retrospectively as of the beginning of the most recent annual period ending before 15 June 2022. If the filing does not include a subsequent interim period that reflects this guidance, apply retrospectively to the beginning of the two most recent annual periods ending before 15 June 2022. The effect of initial application should be reported in the carrying amounts of assets and liabilities as of the beginning of the annual period specified above.
Disclosure	Entities should disclose the effects of the initial application of this guidance.	

Endnotes:

- ¹ The staff defined the term “crypto asset” to include a digital asset that is issued and/or transferred on a distributed ledger or blockchain using cryptography.
- ² References to “entity” are inclusive of both the entity and any agent acting on the entity’s behalf in safeguarding the platform users’ crypto assets.
- ³ For additional details on indemnification assets, refer to Accounting Standards Codification (ASC) 805, *Business Combinations*, and International Financial Reporting Standards (IFRS) 3 *Business Combinations*.
- ⁴ As defined in ASC 820, *Fair Value Measurement*, and in IFRS 13 *Fair Value Measurement*.
- ⁵ Entities should refer to the disclosure guidance in ASC 275, *Risks and Uncertainties*, or in International Accounting Standards (IAS) 1 *Presentation of Financial Statements*.
- ⁶ Entities should refer to the disclosure guidance in ASC 820 or IFRS 13.
- ⁷ Entities should refer to the disclosure guidance in ASC 235, *Notes to Financial Statements*, or in IAS 1.
- ⁸ Items 101, 105 and 303 of Regulation S-K, respectively.
- ⁹ SEC registrants include entities that file reports under Section 13(a) or Section 15(d) of the Exchange Act or entities required to file periodic and current reports in accordance with Rule 257(b) of Regulation A.
- ¹⁰ Other entities include, but are not limited to, entities conducting an initial registration of securities under the Securities Act or Exchange Act, entities conducting a securities offering under Regulation A, and private operating entities entering into a business combination transaction with a shell company, including a special purpose acquisition company.

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