Cryptocurrency
The challenge for accountants & auditors

Stephen Reyes – Partner, Deloitte Gibraltar
June 2018
The World has gone Crypto Crazy
Blockchain and cryptocurrency are disrupting commerce

Snapshot taken from CoinMarketCap.com on 24 May 2018
- 1,623 cryptocurrencies in issue
- Total Market Cap ~ $322B
- Went as high as ~$800B in Jan 18
- 23 have over $1B Market Cap
- 4 have over $10B Market Cap

Bitcoin         - $126B ADTV ~$6.5B
Ethereum       - $  56B ADTV ~$3B
Ripple          - $  24B ADTV ~ $0.5B
Bitcoin Cash - $  17B ADTV ~ $0.8B
Blockchain Technology

- Fundamentally an accounting technology
- Based on decentralized ledgers
- Each containing a complete copy of all transactions
- Across a peer to peer network
- No need for central authority or central clearing
- Uses “miners” to write blocks to the chain by solving complex algorithms

**Benefits**
- Increased transparency
- Accurate tracking
- Permanent Ledger
- Immutable
- Lower cost
- Business Continuity

**Potential applications**
- Cryptocurrency
- Financial services
- Sharing sensitive information
- Voting
- Asset tracking
- Online gaming
- Anything that requires certainty

**Concerns**
- Complex Technology
- Regulatory implications
- Implementation Challenges
- Sufficient expertise
- Competing platforms
- Energy Consumption
Smart Contract Functionality

- Key development in blockchain technology
- Piece of self-executing code that executes a transaction when a precondition occurs
- Precondition is determined by outside entities referred to as "oracles"

Benefits
- Speeds up business processes
- Reduces operational error
- Enhances enforcement
- Improves cost efficiency

Concerns
- Difficult to renegotiate or modify
- Errors/Unintended consequences
- Relies on Oracle
- Issues not tested in court
Features of an ICO

- Form of crowdfunding
- NOT an IPO – unlikely to give ownership rights
- Different types of token – utility, in-app currency, security, asset
- Details set out in a whitepaper and token purchase agreement
- Usually token issuer has few obligations, whitepaper actively sets out lack of obligations
- Token Value driven primarily by speculation
- Lack of regulation
Initial Coin Offerings - 2017

Cryptocurrency ICO Stats 2017

Total: $3,880,018,203

Total Number of ICOs: 210

Month | Total Raised
-------|------------------
Jan    | $15,358,276
Feb    | $25,460,157
Mar    | $18,660,713
Apr    | $81,427,029
May    | $381,012,458
Jun    | $916,537,695
Jul    | $417,281,712
Aug    | $305,866,448
Sep    | $562,534,541
Oct    | $489,713,046
Nov    | $118,768,558
Dec    | $1,069,822,902

Total raised are grouped by the ICO closing date and are raised using ETH exchange rate of that time. Data last updated on 23rd May 2018 17:34 UTC.

Top Ten ICOs of 2017

<table>
<thead>
<tr>
<th>Position</th>
<th>Project</th>
<th>Total Raised</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Hdac</td>
<td>$250,000,000</td>
</tr>
<tr>
<td>2</td>
<td>Filecoin</td>
<td>$257,000,000</td>
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<tr>
<td>3</td>
<td>EOS Stage 1</td>
<td>$185,000,000</td>
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<tr>
<td>4</td>
<td>Paragon</td>
<td>$183,157,275</td>
</tr>
<tr>
<td>5</td>
<td>Bancor</td>
<td>$153,000,000</td>
</tr>
<tr>
<td>6</td>
<td>Status</td>
<td>$90,000,000</td>
</tr>
<tr>
<td>7</td>
<td>BANKEX</td>
<td>$70,000,000</td>
</tr>
<tr>
<td>8</td>
<td>TanK</td>
<td>$64,000,000</td>
</tr>
<tr>
<td>9</td>
<td>Nebulas</td>
<td>$50,000,000</td>
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<tr>
<td>10</td>
<td>MobileCO</td>
<td>$53,069,235</td>
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Monthly Number of ICOs

<table>
<thead>
<tr>
<th>Month</th>
<th>Number of ICO</th>
</tr>
</thead>
<tbody>
<tr>
<td>Jan</td>
<td>7</td>
</tr>
<tr>
<td>Feb</td>
<td>6</td>
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<tr>
<td>Mar</td>
<td>5</td>
</tr>
<tr>
<td>Apr</td>
<td>15</td>
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<td>May</td>
<td>26</td>
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<td>Jun</td>
<td>21</td>
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<td>Jul</td>
<td>21</td>
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<td>Aug</td>
<td>21</td>
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<td>Sep</td>
<td>14</td>
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<tr>
<td>Oct</td>
<td>19</td>
</tr>
<tr>
<td>Nov</td>
<td>10</td>
</tr>
<tr>
<td>Dec</td>
<td>46</td>
</tr>
</tbody>
</table>

% of Funds Raised

- >100%: 23
- 50%-100%: 63
- <50%: 134
Initial Coin Offerings – 2018 (up to 20th May)

Cryptocurrency ICO Stats 2018

Total: $7,730,811,121
Total Number of ICOs: 326

<table>
<thead>
<tr>
<th>Month</th>
<th>Total Raised</th>
</tr>
</thead>
<tbody>
<tr>
<td>Jan</td>
<td>$1,639,465,335</td>
</tr>
<tr>
<td>Feb</td>
<td>$1,349,743,790</td>
</tr>
<tr>
<td>Mar</td>
<td>$2,944,345,007</td>
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<tr>
<td>Apr</td>
<td>$993,031,993</td>
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<tr>
<td>May</td>
<td>$545,036,696</td>
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<tr>
<td>Jun</td>
<td>$0</td>
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<td>Jul</td>
<td>$0</td>
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<td>Aug</td>
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<tr>
<td>1</td>
<td>Telegram (Pre-sale)</td>
<td>$1,700,000,000</td>
</tr>
<tr>
<td>2</td>
<td>Dragon</td>
<td>$330,000,000</td>
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<tr>
<td>3</td>
<td>Huobi Token</td>
<td>$300,000,000</td>
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<tr>
<td>4</td>
<td>Bancor</td>
<td>$150,949,194</td>
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<tr>
<td>5</td>
<td>Envision</td>
<td>$100,000,000</td>
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<tr>
<td>6</td>
<td>Ellastos</td>
<td>$94,100,000</td>
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<tr>
<td>7</td>
<td>Flashcoin</td>
<td>$72,000,000</td>
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<tr>
<td>8</td>
<td>Neuronation</td>
<td>$71,899,499</td>
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<tr>
<td>9</td>
<td>Zenpay</td>
<td>$62,100,000</td>
</tr>
<tr>
<td>10</td>
<td>Olympus Labs</td>
<td>$50,300,000</td>
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<td>Feb</td>
<td>51</td>
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<tr>
<td>Mar</td>
<td>53</td>
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<tr>
<td>Apr</td>
<td>106</td>
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<tr>
<td>May</td>
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<td>Jun</td>
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<td>Jul</td>
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- <50%: 131
PRE-ICO SALE IS LIVE

15% BONUS ENDS IN
14 : 22 : 20 : 57

DON'T MISS THIS EXCLUSIVE OPPORTUNITY TO PARTICIPATE IN HOWEYCOINS TRAVEL NETWORK NOW!

TOKEN SALE!

Learn More

ICO – HOWEYCOINS

If You Responded To An Investment Offer Like This, You Could Have Been Scammed – HoweyCoins Are Completely Fake!
DLT & ICO Regulation in Gibraltar

- Gibraltar a trailblazer in introducing regulation
- DLT regulation introduced on 1\textsuperscript{st} January 2018
- GFSC regulator
- Regulation is principles based
- Guidance issued on application of principles
- ICO regulation expected 2\textsuperscript{nd} Qtr 2018

**DLT Regulatory Principles**
1) Honesty and integrity
2) Customer interests
3) Financial resources
4) Management and Control
5) Protection of Client Assets
6) Corporate Governance
7) Systems and Control
8) AML & CTF
9) Business continuity

**ICO Regulations**
- Promotion, sale and distribution of tokens
- Operation of secondary market platforms trading in tokens
- Providing investment and ancillary services relating to tokens

**Regulatory Pillars**
- Consumer protection
- Protect Gibraltar’s reputation
- Economic Benefit
Issues for Accountants and Auditors

• Client takeon
• Accounting for cryptocurrencies or tokens held
• Accounting for issue of tokens
• Auditing issues
• The future of auditing
Issues for Accountants and Auditors – Client takeon

• Start Up
• Experience and expertise of management
• Lack of Corporate Governance structure
• Compliance with laws – AML/GDPR
• Regulatory Issues
• Feasibility of underlying business model
• Rationale for use of cryptocurrency/ICO
• Appropriate investor funding
• Reliability of Financials
• Customer interests
• Scope/risk of engagement
Issues for Accountants – Accounting for Cryptocurrencies

• Not a currency!
• Not cash or cash equivalent
• Not a financial instrument
• Usually not inventory
• Probably an intangible asset
  • Identifiable, non-monetary asset with no physical form

Intangible asset accounting treatment
Cost less impairment
If active market then FV with gains through OCI not P&L

• Fairer presentation is to FV and show gains through P&L but accounting standards do no allow that – need new specific accounting framework
Issues for Auditors – Holding cryptocurrencies

• Verifying existence and ownership
• Increased AML risk
• Valuation
• Post year end review - volatility
Issues for Accountants – ICO

- Revenue recognition
- Token creation and issue costs
- Issue of tokens to founders/employees/advisors
- Payment for products/services with tokens
- Taxation – management and control/PE
- Capitalisation of platform development
How will Blockchain impact the audit and assurance profession
If all transactions are available, do we need an auditor?

Recording a transaction is just one aspect
- Recorded transactions can still be illegal, entered into between connected parties, linked to offchain side agreement, incorrectly classified.
- What about completeness, estimates and accounting policies

New ways of auditing
- Real time auditing
- Audit automation & cognitive capability
- Data analytics

Additional assurance opportunities
- Smart contracts
- Architecture
Thank You