



New SEC staff guidance spotlights crypto asset risks

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In a minute

On March 31, 2022, the Securities and Exchange Commission (SEC) released [Staff Accounting Bulletin No. 121 \(SAB 121\)](#) to provide accounting and disclosure guidance for entities involved with safeguarding crypto assets¹ on behalf of other parties.

A reporting entity within the scope of SAB 121 must record a liability for its obligation to safeguard crypto assets (safeguarding liability), which is both initially and subsequently measured at the fair value of the safeguarded crypto assets. The entity also would record a corresponding asset (safeguarding asset), measured on the same basis as the safeguarding liability.

SAB 121 also requires disclosure of the nature and amount of crypto assets being safeguarded, an entity's accounting policy for safeguarding activities, how the fair value of safeguarded crypto assets is determined, and potentially other information about risks and uncertainties arising from the entity's safeguarding activities.

SAB 121 is effective for financial statements covering the first interim or annual reporting period ending after June 15, 2022.

Entities can refer to this [SAB 121 decision tree](#) for help determining whether SAB 121 is applicable.

¹ SAB 121 defines a crypto asset as “a digital asset that is issued and/or transferred using distributed ledger or blockchain technology using cryptographic techniques.” This definition captures a wide variety of digital asset types, including cryptocurrencies (such as bitcoin and ether), stablecoins (such as USD Coin), and non-fungible tokens.

Breaking it down

The SEC staff released Staff Accounting Bulletin No. 121 (SAB 121) on March 31, 2022, to share its views on the accounting for entities that “have obligations to safeguard” crypto assets. Given the “unique risks and uncertainties” – including technological, legal, and regulatory risks and uncertainties – of safeguarding crypto assets that can significantly affect an entity’s operations and financial condition, the SEC staff believes the guidance in SAB 121 will enhance the information provided to investors and other users of financial statements.



Who does SAB 121 apply to?

Broadly speaking, SAB 121 applies to both issuer entities and entities with submitted or filed registration statements reporting under U.S. GAAP or International Financial Reporting Standards (IFRS). SAB 121 also applies to entities that are submitting or filing an offering statement and to private operating companies whose financial statements are included in filings with the SEC in connection with a business combination involving a shell company, including a special purpose acquisition company.

More directly, the accounting and disclosure guidance applies to those entities that safeguard crypto assets on behalf of other parties, including maintaining the cryptographic key information (private key information) necessary to access the crypto assets.



Crowe observation: Based on discussions with the SEC staff, the primary focus of SAB 121 is on the safeguarding of crypto assets. Importantly, SAB 121 does not reference contractual obligations. As a result, entities could be within the scope of the guidance if an implied or constructive safeguarding obligation is present. Furthermore, contractual language limiting an entity's liability for the loss or theft of crypto assets might not necessarily preclude an entity from being subject to SAB 121.

Examples of arrangements that might give rise to an obligation to safeguard crypto assets include:



**Custody
arrangements**



**Wallet
services**



**Collateral
agreements**



**Trading
platforms**

For further guidance in determining if SAB 121 would apply, entities can refer to this [SAB 121 decision tree](#).

What is the impact of SAB 121?

The SEC staff believes entities that have obligations to safeguard the crypto assets of others should recognize a safeguarding liability and an accompanying safeguarding asset at the fair value of the crypto assets held for others. The following table summarizes the SEC staff's views on the recognition, measurement, and disclosure requirements affected entities are expected to follow.

SAB 121 recognition, measurement, and disclosure requirements

Topic	SEC staff views
Recognition and measurement	<ul style="list-style-type: none">• An entity must recognize a liability to reflect its obligation to safeguard crypto assets on behalf of others. The liability is measured both initially and subsequently at the fair value of the underlying crypto assets.• An entity must recognize a corresponding asset – which SAB 121 refers to as similar in nature to an indemnification asset² – at the same time the liability is recognized. The asset is measured on the same basis as the liability.



Crowe observation: SAB 121 does not address how changes in the fair value of the safeguarding liability and safeguarding asset should be reflected in an entity's income statement. However, the guidance does suggest that the measurement of the safeguarding asset may differ from the measurement of the safeguarding liability due to "potential loss events, such as theft."

² SAB 121 explains that the safeguarding asset recognized is separate and distinct from the crypto assets being safeguarded.

Topic	SEC staff views
Financial statement disclosure	<p>An entity must disclose the following information in the notes to its financial statements:</p> <ul style="list-style-type: none"> • The nature and amount of each crypto asset the entity safeguards on behalf of others, with separate disclosure for each significant crypto asset. • Vulnerabilities the entity has due to any concentrations in safeguarding activities (see ASC 275-10-50, IAS 1). • Fair value measurement disclosures for the safeguarding asset and safeguarding liability (see ASC 820-10-50, IFRS 13). • The accounting policy used to account for the safeguarding liabilities and corresponding assets (see ASC 235-10-50, IAS 1). • The effects of the initial application of SAB 121 (see ASC 250-10-50). <p>In connection with these disclosures, an entity should consider disclosing a description of who (for example, the entity, its agent, or another third party) holds the private key information, who maintains the internal recordkeeping, and who is obligated to secure the crypto assets and protect them from loss or theft.</p>
Disclosure outside the financial statements	<p>Disclosures an entity might need to provide outside the financial statements include the following:</p> <ul style="list-style-type: none"> • Qualitative information regarding significant risks and uncertainties should be included within the description of the business, risk factors, or management’s discussion and analysis of financial condition and results of operation.³ • When material, a description of the types of loss or additional obligations that could occur and the potential impact that the destruction, loss, theft, compromise, or unavailability of the private key information would have to the entity’s ongoing business, financial condition, operating results, and cash flows. In addition, if material, any risk mitigation steps in place should be described (for example, insurance coverage directly related to the crypto assets held for others). • A discussion of the legal ownership of the crypto assets, including whether they would be available to satisfy general creditor claims in the event of bankruptcy.

Source: Crowe analysis

³ Refer to Items 101, 105, and 303 of Regulation S-K.



When is SAB 121 effective, and what are the transition provisions?

Public entities

A public entity must apply SAB 121 in its first interim or annual period ending after June 15, 2022, retrospectively to the beginning of the fiscal year to which the interim or annual period relates, which means SAB 121 applies to a calendar year public entity's second quarter 2022 Form 10-Q filing.

Other entities

SAB 121 applies retrospectively to other entities' next submission or filing (for example, an initial or amended registration statement, proxy statement, or Form 1-A) with the SEC to either:

1) The beginning of the two most recent annual periods ending before June 15, 2022, if no subsequent interim period is included in the submission or filing.

Example:

A calendar year-end entity submits a registration statement in 2022 that includes financial statements as of and for the fiscal years ended Dec. 31, 2021, and 2020 (that is, the subsequent interim period ended March 31, 2022, is not presented in the filing). Both the 2021 and 2020 annual periods should reflect the application of SAB 121.

2) The beginning of the most recent annual period ending before June 15, 2022, and the subsequent interim period presented in the submission or filing.

Example:

A calendar year-end entity submits a registration statement in 2023 that includes financial statements as of and for the fiscal year ended Dec. 31, 2021, and as of and for the nine months ended Sept. 30, 2022. The entity should apply SAB 121 as of and for the fiscal year ended Dec. 31, 2021, and to the subsequent interim period ended Sept. 30, 2022.⁴

All entities

For all entities, the financial statements should reflect the initial application of SAB 121 in the carrying amounts of assets and liabilities as of the beginning of the applicable annual period(s) with clear disclosure of the effects of the initial application.

⁴ Derived from footnote 14 of SAB 121.



SAB 121 decision tree

This decision tree can help entities determine if SAB 121's accounting and disclosure guidance applies to them.

Significant judgment might be required to conclude on the applicability of SAB 121, and consultation with the SEC's Office of the Chief Accountant is encouraged.

STEP 1

Is your entity subject to Staff Accounting Bulletins issued by the SEC?⁵

Yes

Proceed to Step 2

No

SAB 121 does not apply

However, if a reporting entity that is not subject to Staff Accounting Bulletins issued by the SEC elects to apply such guidance, proceed to Step 2.

STEP 2

Is your entity involved, directly or indirectly, with the safeguarding of crypto assets for a third party?

Yes

Proceed to Step 3

No

SAB 121 does not apply



Crowe observation: According to SAB 121, the obligation of safeguarding includes 1) securing the crypto assets and the associated private key information and 2) protecting them from loss, theft, or other misuse. When determining whether an entity safeguards crypto assets, the entity also must consider any agent(s) acting on the entity's behalf or the involvement of third parties.

Entities that are only indirectly involved in the safeguarding of the crypto assets of others will need to carefully consider their level of involvement and the customer's perception of involvement in safeguarding activities to determine if SAB 121 applies. From discussions with the SEC staff, we understand that multiple entities could fall within the scope of SAB 121 for the same safeguarded assets (for example, introducing entity with a subcustodial arrangement). Consultation with an accounting adviser might be necessary.

⁵ This question includes public entities, entities whose financial statements are filed with the SEC under Rule 3-09 and Rule 3-05 of the *Securities and Exchange Act of 1934*, and private companies involved in special purpose acquisition company transactions.

STEP 3

Does your entity control the underlying crypto assets and, therefore, recognize the crypto assets on its statement of financial position?



Crowe observation: Prior to applying SAB 121, an entity should determine whether it controls the underlying crypto asset. This assessment is made using the relevant accounting framework depending on the nature of the crypto asset involved (for example, an intangible asset or financial asset).

Question 10 of the American Institute of CPAs' [Accounting for and Auditing of Digital Assets practice aid](#) provides a framework an entity could consider using for assessing control.

Yes

SAB 121 does not apply

No

Proceed to Step 4

STEP 4

Does your entity or one of its agents maintain cryptographic key information (such as private key information) to independently transact in the safeguarded crypto assets?



Crowe observation: When an entity (including its agents) cannot unilaterally transact in the safeguarded crypto assets, it might still be subject to SAB 121 depending on its level of involvement with and customers' perceptions of the entity's involvement with the safeguarded digital assets.

Factors an entity might consider in its analysis include (but are not limited to) the following:

- Contractual rights and obligations.
- Customers' perception of who is responsible for safeguarding.
- The entity's involvement in record keeping of safeguarded assets.
- The entity's involvement in a customer's ability to access the safeguarded assets.

Yes

SAB 121 applies

No

SAB 121 might not apply



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