Accounting for Bitcoin, Ethereum and their ETFs

Comprehensive Guide for Switzerland

The approval of Exchange-Traded Funds (ETFs) on spot Bitcoin and Ethereum by the U.S. Securities and Exchange Commission (SEC) underscores the global momentum towards mainstream acceptance of Bitcoin, Ethereum, and other cryptocurrencies. This approval not only signifies a crucial step for the broader financial market, but also resonates deeply with Switzerland's financial landscape, given its permissive regulatory environment for such investments.

This guidance focuses on the different accounting treatments for spot Bitcoin/Ethereum and Bitcoin/Ethereum ETFs under the common accounting standards applicable in Switzerland.

Swiss Code of Obligations (SCO)

Bitcoin and Ethereum
There is no specific accounting standard for Bitcoin or Ethereum under the Swiss Code of Obligations (SCO), but the Swiss Audit Manual (volume "Accounting and financial reporting") provides detailed guidance about the recognition and measurement of these cryptocurrencies. Under the SCO, holdings in Bitcoin or Ethereum may be classified as securities, inventories, or intangible assets.

Upon initial recognition, Bitcoin and Ethereum must generally be recognized at acquisition cost (Art. 960a para. 1 SCO). Transaction costs are typically expensed in the income statement, although they can be capitalized as part of the acquisition costs of the cryptocurrencies.

Subsequent measurement:
- **Securities:** holdings can be measured either at acquisition cost (lower of cost or market) or at market value. When measured at the lower of cost or market, a valuation adjustment is necessary if subsequent prices drop. Revaluation is only possible up to the acquisition cost. If the market value option is selected, market value increases above cost value are also recognized in the P&L, and setting up a fluctuation reserve is possible.

- **Inventory:** under the cost model, subsequent measurement might lead to a write-down to the net realizable value. Revaluation is only possible up to the acquisition cost. For determining the acquisition or production cost, standard accounting methods such as first-in-first-out (FIFO) or the weighted average method can be applied. Alternatively, valuation at market value (with changes in value recognized in the P&L) is also possible, except when inventories are consumed within the production process.

- **Intangible Assets:** under the cost model, holdings are not subject to any loss in value due to usage or age. However, "other losses in value" must be accounted for through value adjustments as per Art. 960a para. 3 SCO. These adjustments are recognized as soon as the market value drops below the acquisition cost or the current book value. A reversal of impairment losses is only possible up to acquisition cost. Alternatively, intangible assets may be measured at market value (with changes in value recognized in the P&L).

Bitcoin/Ethereum ETFs

Bitcoin and Ethereum ETFs, under Art. 960a para. 1 SCO, are initially recognized at acquisition cost. While brokerage and bank fees are usually expensed in the income statement, they may be capitalized as part of the acquisition cost. As ETFs are classified as securities, subsequent measurement is either at acquisition cost (or the lower of cost or market) or at market value. Unlike direct investments in Bitcoin or Ethereum, classification as intangible assets or inventory is not applicable for ETFs.

Swiss Accounting Standards for Banks

Bitcoin and Ethereum

For banks, FINMA distinguishes between cryptocurrencies (including Bitcoin and Ethereum) held on behalf of clients and those held for the bank's own account regarding accounting treatment.

- **Held on Behalf of Clients:** if cryptocurrencies held on behalf of clients cannot be segregated in the event of bankruptcy, they are recognized at fair value. If they can be segregated, they are treated as off-balance sheet items.

- **Held for Own Account:** cryptocurrencies are recognized in the trading book at fair value or as financial investments without the intention to trade at the lower of cost or market value. A reversal of impairment losses in the latter case is only possible up to acquisition cost.

Bitcoin/Ethereum ETFs

Investments in Bitcoin and Ethereum ETFs are treated similarly to other fund investments. If held for trading, they are recognized at fair value. Therefore, the accounting treatment may be identical to direct cryptocurrency investments, with trading book entries at fair value or financial investments at the lower of cost or market value.

International Financial Reporting Standards (IFRS)

Bitcoin and Ethereum

Under IFRS, when held for long-term business use and not for sale in the near future, cryptocurrencies are accounted for as non-current intangible assets under IAS 38. Upon initial recognition, they are measured at cost. Thereafter, entities may elect to use the cost model (carrying the asset at cost less impairment) or the revaluation model (revaluing the asset to its fair value at each reporting date, with changes in fair value above its cost value recognized in other comprehensive income, and below cost value in profit or loss) provided there is an active market for the respective cryptocurrency.

Cryptocurrencies should be treated as having an indefinite life under IAS 38, which means that they are not amortized but are subject to annual impairment testing. For cryptocurrencies held for sale in the ordinary course of business, IAS 2 Inventories applies, requiring measurement at the lower of cost and net realizable value, with changes in value recognized in profit or loss. If the entity acts as a broker-trader, inventories may be measured at fair value less costs to sell.

Bitcoin/Ethereum ETFs

Cryptocurrency funds, including Bitcoin and Ethereum ETFs, are generally subject to IFRS 9: Financial Instruments. The classification and measurement depend on the fund's structure and investment strategy.

A crucial step is the business model assessment, which is necessary to determine how the crypto assets are managed and the objective of holding them. If the crypto assets do not meet the SPPI (Solely Payments of Principal and Interest) criteria – typically the case for cryptocurrency funds – they must be measured at fair value through profit or loss.

Swiss GAAP FER

Bitcoin and Ethereum

Swiss GAAP FER is a true and fair view accounting standard leading to some significant different accounting treatment for cryptocurrencies than IFRS:

- **Intangible Assets:** cryptocurrencies could be classified as intangible assets if they meet certain capitalization criteria and material delimitation. However, due to mandatory depreciation for intangible assets and the lack of attributable revenue or cost, this classification is not appropriate.

- **Inventories:** if a company acts as a trader of cryptocurrencies, engages in mining with the intent to sell the mined cryptocurrencies later or uses cryptocurrencies as a resource for its services, they could be classified as inventories, measured at acquisition cost or the lower of cost and net realizable value.

- **Securities:** classifying cryptocurrencies as securities can be nuanced, as securities are typically financial instruments such as stocks or bonds. However, for accounting purposes, cryptocurrencies held for investment purposes may be treated similarly to financial instruments, given the economic substance of the investment.

  – **Short-term Holdings (Trading Securities):** cryptocurrencies held for short-term trading purposes can be classified as current assets and measured at fair value, with changes in fair value recognized in the income statement.

  – **Long-term Holdings (Investment Securities):** cryptocurrencies held as long-term investments should be classified as financial investments. They can be initially recognized at cost and subsequently measured at cost less any impairment losses, or at fair value, with changes in fair value recognized in the income statement. This approach aligns with the True and Fair View principle.

When classifying and valuing cryptocurrencies as securities, companies should ensure that their chosen approach reflects the economic reality of their use and complies with Swiss GAAP FER principles, taking into account the business model and the availability of quoted prices in an active market.

Bitcoin/Ethereum ETFs

Cryptocurrency funds under Swiss GAAP FER, in particular Bitcoin and Ethereum ETFs, do not fall under a specific FER standard. However, they are subject to the valuation framework outlined in FER 2. The measurement of the underlying crypto assets is similar to holdings of spot Bitcoin or Ethereum, depending on the intended holding period. Given the significant price fluctuations associated with Bitcoin and Ethereum ETFs, valuation at current market prices with changes in value recognized in the P&L is preferred under the true and fair view principle.

Conclusion

In conclusion, the accounting treatment of Bitcoin, Ethereum, and their respective ETFs varies significantly under different accounting frameworks in Switzerland. Each standard – Swiss Code of Obligations (SCO), Swiss Accounting Standards for Banks, International Financial Reporting Standards (IFRS), and Swiss GAAP FER – provides different guidelines based on the nature and purpose of the holdings.

The SEC's approval of Bitcoin and Ethereum ETFs marks a pivotal moment, offering new regulated investment vehicles and potentially increasing the mainstream adoption of cryptocurrencies. For companies, this development necessitates a keen understanding of the different accounting treatments to ensure compliance and accurate financial reporting. Understanding these nuances is crucial for making informed investment decisions and maintaining a true and fair view of the financial position in an evolving regulatory landscape.

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