

What to know when
preparing for the auditing of
digital assets



Today's presenters



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Summary of Practice Aid

The AICPA Digital Assets Working Group has recently included nonauthoritative guidance for auditors to consider regarding accepting or continuing audit engagements in the digital assets ecosystem under generally accepted auditing standards (GAAS).

Overview

- Brief description of what guide does and does not cover

Auditor Skill Sets and Competencies

- Skills an audit firm is required to have in order to conduct an appropriate audit

Management Skill Sets and Competencies

- Skills a client is required to have in order to be an audit candidate

Management Integrity and Overall Business Strategy

- Corporate environment and tone at the top

Processes and Controls (incl. Information Technology)

- Processes and controls around digital assets



Overview

The AICPA *Client Acceptance and Continuance* practice aid was created to help guide audit firms and their clients on issues related to the acceptance and continuance of audit relationships. While the practice aid does not focus on ethical or independence considerations, these topics are still extremely important.

Independence Threats Auditors Consider

Self-review threat: Audit team member does not appropriately evaluate the results of a previous judgment

Management participation threat: Audit team member assumes the role of management or performs management responsibilities

Advocacy threat: Audit team member promotes a client's interests or position to the point their independence is compromised

As with any audit, auditors will seek to mitigate these threats. Digital asset engagements have unique complexities that may introduce new or different compliance risks for auditors. Clients can help auditors address these and other threats by ensuring they have the appropriate industry knowledge, technical skill sets, processes, and controls.



Auditor Skill Sets and Competencies

Firms are required to evaluate their personnel's competence, capabilities, resources, and availability of the engagement team prior to acceptance or continuance to mitigate the risk of accepting an engagement it is not capable of effectively performing.

Key Components for an Auditor

- Current industry experience
- Understanding of digital assets
- Understanding of how digital assets are being used in the specific client situation



Auditor Skill Sets and Competencies (cont.)

The digital assets ecosystem is evolving rapidly; it is important for the auditor to understand the level of effort necessary to gain the knowledge about the ecosystem (or relevant parts thereof) needed to make a reasoned client acceptance and continuance determination and competently perform the audit.

Auditor Challenges Specific to Digital Assets

- Staying apprised of regulatory, industry, technological, or financial reporting developments
- Recruiting, developing, and retaining talent
- Appropriately directing, supervising, and reviewing work performed
- Adapting to new/different risks as the ecosystem evolves
- Ongoing updates of training curricula



Management Skill Sets and Competencies

Auditors are required to obtain an agreement wherein management acknowledges its responsibility for the preparation and fair presentation of financial statements, the design, implementation, and maintenance of internal controls, and providing the auditor access to all relevant information and persons necessary to obtain audit evidence.

Management Challenges Specific to Digital Assets

- Appropriate maintenance of books and records and digital asset security
- Identification of unique risks in the space and designing and implementing internal controls to respond to such risks, incl. maintaining appropriate support for transactions and applying the appropriate financial reporting framework
- Over-reliance on the auditor
- Identification of applicable laws and regulations or areas of evolving laws and regulations
- Have access to or ability to identify the need for specialists, e.g. competent legal counsel, IT specialists, fund administrators



Management Skill Sets and Competencies (cont.)

The client acceptance or continuance process may be more involved than typically performed for other new or continuing engagements.

General Inquiries Management can Expect from an Auditor

- Management's prior experience in the digital asset space
- Management's understanding of the applicable regulatory environment
- How books and records are maintained, i.e. independent of or directly from the blockchain / 3rd party
- Engagement of specialists / accounting consultants as needed, incl. the effective review of such work
- Management's understanding of how the applicable financial reporting framework is applied to its operations
- Processes in place for the proper recognition, derecognition, measurement, classification, and tracking of digital assets



Management Integrity & Business Strategy

Company culture is defined by the tone at the top. Auditors seek to only associate with clients who they believe to have integrity. A culture of integrity begins with an entity's leadership who direct the objectives and strategies.

Challenges Specific to Digital Assets

- Pseudo-anonymous nature of a digital asset transaction could make KYC and AML challenging
- Easily accessible markets make the digital asset industry attractive to “bad actors”
- Management may not have sufficient understanding of their own business strategy

Management's Process to Address Challenges

- Outline plan for current and future involvement with digital assets
- Defined process for customer onboarding and related party identification
- Transaction monitoring procedures
- Appropriate third-party services are being used



Processes and Controls

A precondition of any audit is the client's ability to prepare and take responsibility for the fair presentation of the financial statements, as well as design, implementation, and maintenance of effective internal controls over financial reporting.

Process and Control Challenges Specific to Digital Assets

- Lack of third-parties who provide audit evidence related to transactions
- Related party risk due to pseudo-anonymous nature of a blockchain
- Tracking transactions both on and off chain
- Reconciliation between blockchain and financial statements
- Potential changes to current IT infrastructure
- Transactions issued on the blockchain are append only
- Involvement with digital asset custodians



Processes and Controls (cont.)

Management's Procedures to Reduce Risk Specific to Digital Assets

- Private key management
- Implement processes and controls around digital asset management
- Ensure control operators have sufficient understanding of digital assets
- Hire outside specialist to fill any knowledge around proper process implementation
- Create robust training program
- Hire service organizations for complex processes (wallet organization & key management)
- Create due diligence process when transacting in new assets
- Develop disaster recovery procedures



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