



Crypto firms build confidence through SOC 2 reporting

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Following the increase of adoption of digital assets, cryptocurrencies have become a popular alternative asset class in the global economy. In the latest report from Crypto.com, it was estimated that the total number of global crypto users has shot up to **295 million** users as of year end 2021. At the time of writing in February 2022, the total market cap of cryptocurrencies is estimated at around **USD2 trillion** and bitcoin.com statistics shows that the leading 13 crypto exchange platforms indeed custody for **USD156 billion** of cryptocurrencies as of 2 January 2022.

The leading 13 exchanges are Coinbase, Binance, Huobi Global, Kraken, Okex, Gemini, Bitfinex, Bittrex, Bitflyer, Coincheck, Bitstamp and Bybit.

However, since the regulation governing cryptocurrencies are still either not clear or even non-existent in many countries. There are still number of crypto exchanges are indeed not licensed anywhere or/and incorporated in offshore islands in order to be subject to less regulatory supervision.

Regardless, a reputable crypto exchange or custodian (wallet provider) or crypto service providers, they would significantly invest resources in their IT system and security. This is because the crypto firms have witnessed many security breaches and hacking events in the market. According the Hackernoon, over 60 major cryptocurrency hacks have occurred worldwide, with investors losing USD12.6 billion. Given the fact that there are many crypto exchanges which are unlicensed, as a client or user of these crypto firms, it becomes crucial to choose one with robust IT controls measures. When you are deciding to use a crypto exchanges platform to trade your cryptocurrencies or custody your cryptocurrencies with a custodian, the most common question is, "Is our information secured?" This is often followed by a more difficult question, "How do you know?" The SOC 2 certification then comes into play and it becomes the industry benchmark in these two years.

What is SOC2 certification?

The SOC 2 is a System and Organisation Controls report with an audit opinion issued by a certified public accountant over internal controls related to information technology. The report is prepared under the Trust Principles of Security, Availability, Integrity of processing, Confidentiality and Privacy.

A SOC 2 report can demonstrate to the recipient of the report the controls of the crypto firm in addressing security, availability, integrity of processing, confidentiality and privacy through this third-party assurance report.

As AICPA has provided the general criteria of effective design of controls under the Trust Principles, it would be the independent assessor's responsibility to identify what has been done by the crypto firm which meets those applicable criteria. Accordingly, the third-party assurance report helps crypto firms to build confidence in their service delivery processes and controls.

We see the increasing reliance on SOC 2 in the crypto space and becoming an industry benchmark. Your counterparties such as your customers, business partners, investors and global regulators will be asking a copy of the SOC 2 report to help their own due diligence work.

What is the scope of SOC 2 ?

Most organizations are familiar with both SOC 1 and SOC 2 reports. While SOC 1 reports cover internal controls on financial reporting (ICFR) and support customers' financial audit, SOC 2 reports focus on the controls that are relevant to the following Trust Services Criteria (TSC) which are established by the American Institute of Certified Public Accountants (AICPA):



Security

Information and systems are protected against unauthorized access (both physical and logical), unauthorized disclosure of information.



Availability

Information and systems are available for operation and use as committed and agreed. It refers to accessibility of system, products or services as the firm committed.



Processing integrity

System processing is complete, valid, accurate, timely, and authorized to meet the entity's objectives.



Confidentiality

Information designated as confidential is protected to meet the entity's objectives.



Privacy

Personal information is collected, used, retained, disclosed, and disposed of in conformity with entity's objectives.

Type 1 vs Type 2 report

A SOC 2 report has an option for a Type 1 or Type 2 report. A Type 1 report only covers the design and implementation of controls at a point in time (a snapshot), while a Type 2 covers both the design and operating effectiveness of controls for a period of time.

Both Type 1 and Type 2 report should be available to be distributed to existing or prospective customers and other stakeholders who have requirements and expectation on the firm's IT controls.

However, it is typical a sequence of journey from Type 1 to Type 2 report. For example, a crypto firm can start with Type 1 report at year one. It helps to engage the external stakeholders' confidence in the firm's commitment on IT system and cyber security. For those concerns and deficiencies being identified by independent assessors at Type 1 report, the crypto firm can remediate them accordingly before transitioning to Type 2 report which has a higher expectation standard.

What are the benefits of performing SOC 2 review

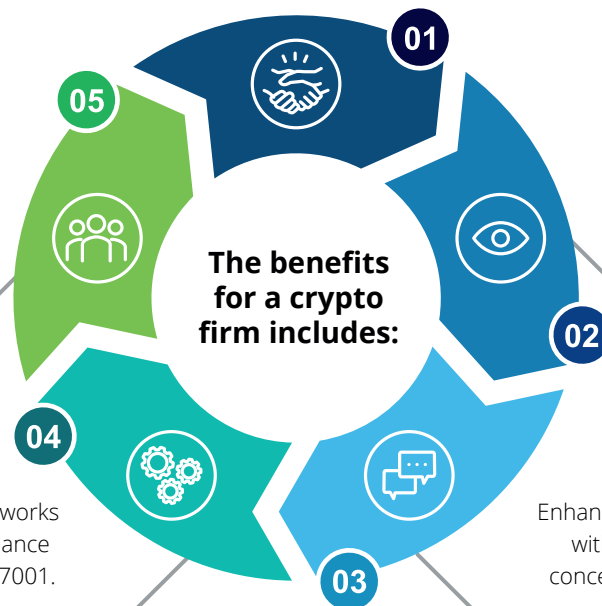
Building trust signal to clients in a time of increasing awareness around safety and security.

Attracting more partnership with institutional clients such as banks, fund managers, proprietary trading firms which generally have higher expectation and more demands on IT systems and security.

Gaining improved insight by senior management over risk, governance and internal controls.

Integrating with other frameworks over IT controls and governance such as Cobit and ISO/IEC 27001.

Enhancing efficiency for communication with local regulator in addressing concerns on IT security management.



The bottom line

It is important to remember that a crypto firm cannot outsource the risks around IT. It is the firm's obligation to protect the information of your business and your customers, even when they make use of SOC 2 report. A SOC 2 report will assist users by providing assurance over the controls in place at the crypto firms.

How Deloitte can help

Our experienced assurance teams stand ready to support your needs with a set of service offerings including:



Perform readiness assessment and advise the management the gap prior to the SOC 2 examination



Make recommendations on the improvement and enhancement of the control environment, system controls and IT security risk



Customize a SOC 2 report to meet client's need and be aligned to SOC framework

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