Digital Asset Risk Assessment: A New Paradigm in Risk Management
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The digital asset marketplace has erupted in the past year. Financial institutions are gaining confidence in the transformative role that digital assets will play in the future due to the vast growth of the cryptocurrency market, along with the emergence of other non-state digital assets like non-fungible tokens (NFTs) and the adoption of central bank digital currencies (CBDCs). According to Deloitte’s 2021 Blockchain survey, FSI pioneers are in near unanimity that digital assets will be very or somewhat important to their industry in the next 24 months. As of August 2021, over 55% of the world’s largest banks are investing in the digital asset and blockchain market, with several of the world’s largest financial institutions announcing the expansion of their offerings to include digital asset services like trading and custody. Such adoption uncovers unique risks for emerging disruptors, tokenized businesses, digital asset exchanges, crypto natives, traditional financial services, and other organizations using the technology or investing in blockchain-based assets.

Anticipating digital assets regulatory policies

Digital assets represent a new paradigm in risk management. As the concept of digital asset risk assessment develops, it should remain anchored to the foundation of traditional risk assessments, while acknowledging the idiosyncratic characteristics of digital asset products and services. Key regulatory bodies have expressed concerns that the risks posed by digital assets could lead to systemic and financial impacts on consumers and the overall economy. However, these regulators are also aware of the opportunity to shape policy moving forward. On March 9, 2022, the White House released an executive order on ensuring responsible development of digital assets, detailing policy across six major priorities: consumer and investor protection, financial stability, illicit finance, US leadership in the global financial system, and economic competitiveness, financial inclusion, and responsible innovation. Regulators plan to address these concerns within the context of their respective oversight mandates with specific requirements around safety and soundness, consumer protection, and market integrity. Additionally, the European Union is in the process of drafting a new text that aims to regulate digital assets that are not currently covered elsewhere; the goal of which is to harmonize European law on the matter and provide a framework that elevates the status of these new instruments. There is an expectation of implementation by the end of 2024, granting new powers to European authorities on the topic.

In addition to the adherence of new policy, regulators expect that firms will establish or enhance their risk and control frameworks and conduct risk assessments specific to the characteristics of the underlying products and technologies. This is highlighted in the Office of the Comptroller of the Currency’s (OCC) Interpretive Letter 1176, which outlines the requirement of firms to have adequate controls in place before taking part in digital asset activities. Regulatory bodies like the OCC are trying to identify the cryptocurrency activities that banks are conducting presently and in the future. Deloitte’s recent whitepaper compares the OCC’s and the Federal Deposit Insurance Corporation’s (FDIC) recently announced cryptocurrency notification protocols which aim to better understand and supervise

Example key risk areas

- Security breaches
- Fraud
- Compliance with applicable laws
- Market manipulation
- Conflicts of interest
- Quality of market surveillance
- Anti-money laundering (AML) procedures
- Complexities with forked and airdropped DAs
- Insolvency
- Allocation across client accounts
Considerations for digital asset risk assessment

- Classification of digital assets
- Key management
- Protocol updates/
forks
- Regulatory requirements
- Transaction monitoring
- Threat monitoring
- Know your customer
- Performance
- Trade execution & settlement
- Trading venues
- Governance
- Network congestion

banks’ plans to assess the risks associated with operating in the cryptocurrency space. Overall, engaging with digital assets requires active management across a wide spectrum of risks and the leverage of core safety and soundness playbooks to meet the expectations of regulators. One of Deloitte’s industry-leading offerings is a digital asset risk assessment tool designed to help organizations mitigate digital asset specific risks while safely engaging in the marketplace.

Deloitte’s digital asset risk assessment tool
Leveraging our blockchain-related experience, we have developed a broad risk assessment tool comprised of more than 250 unique blockchain and digital asset targeted risks. The tool provides a baseline view of risk applicability across many of the emerging service offerings in the digital asset marketplace, taking into consideration the nuanced and evolving development of digital asset products, such as cryptocurrencies versus CBDCs. It is important to note that this tool, along with any risk assessment tool, is to be viewed as an accelerator rather than a blanket or universal solution. With approximately 500 professionals in the US and 1,500 more throughout the Deloitte Touche Tohmatsu Limited network of member firms having served on blockchain and digital asset engagements in over 50 countries, our experienced team works closely with executive stakeholders to fully understand the specific service offering and product scope of their operating model before conducting the risk assessment. Our systematic waterfall approach pivots on the applicable digital asset risk areas to drive a risk-based assessment which integrates with existing controls and assists in developing a prioritized remediation plan targeted to establish a robust risk and control framework for digital asset activity. Deloitte’s digital asset risk assessment methodology provides visibility into nuanced digital asset risks while ensuring mitigating controls are in place and appropriately aligned to risk appetite. In the fast-paced digital asset marketplace, the risk assessment tool can save an average of two months in a risk assessment lifecycle, while providing confidence in navigating the rapidly evolving landscape. If you are interested in learning more about Deloitte’s Blockchain and Digital Assets Practice and our digital asset risk assessment tool, please contact our team.

About Deloitte’s Blockchain and Digital Assets Practice
At Deloitte, our people work globally with clients, regulators, and policy makers to understand how blockchain and digital assets are changing the face of business and government today. New ecosystems are developing blockchain-based infrastructure and solutions to create innovative business models and disrupt traditional ones. This is occurring in every industry and in most jurisdictions globally. Our deep business acumen and global industry-leading, risk and financial advisory services help organizations across industries achieve their blockchain and digital asset aspirations. Reach out to our leaders to discuss harnessing the momentum of blockchain and digital assets, prioritizing initiatives, and managing the opportunities and challenges associated with blockchain adoption effort.
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Endnotes

1. Blockchain survey (deloitte.com)
2. Blockdata | Blockchain companies invested in by top 100 banks
6. Actual time savings are based on individual facts and circumstances