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MARKETSCURRENCIESCRYPTOCURRENCY

FTX Disclosed Related-Party Transactions but Didn't Name Names

Lack of detail in financial statements echoes past scandals including Enron



Sam Bankman-Fried last July in the Bahamas, the offshore tax haven where FTX Trading was based.

PHOTO: ROBYN DAMIANOS FOR THE WALL STREET JOURNAL

By *Jonathan Weil* [+](#)

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The saga of Sam Bankman-Fried's bankrupt crypto empire isn't just about collapsing tokens, missing billions and sunny offshore tax havens. There were also red flags in its books.

At the core of FTX Trading Ltd.'s financial statements was a series of related-party transactions. But the company didn't say who those parties were.

On its balance sheet, the largest asset as of Dec. 31 was a "related party receivable" valued at \$1.2 billion, or 44% of its assets. Its liabilities included a \$362 million "related party payable."

FTX Trading last year paid \$250 million, or 25% of its revenue, to an unnamed related party for "software royalties," as previously reported by The Wall Street Journal, which viewed the documents. As a closely held company, FTX Trading didn't disclose its financial statements publicly, though they were shared with investors.

In a footnote to the financial statements, the company said its “primary shareholder is also the primary shareholder of several related entities which do business with the company.” It didn’t say who the related parties were for any specific transaction it disclosed.

The standard accounting rules for disclosing related-party transactions are vague and have long been considered a weakness in the system. There is no clear-cut rule requiring companies to disclose the players in a related-party transaction. The rules do say, “If necessary to the understanding of the relationship, the name of the related party shall be disclosed.”

Jack Ciesielski, founder of the asset manager R.G. Associates in Towson, Md., and a member of the Financial Accounting Standards Board’s Emerging Issues Task Force, said: “I think it’s a hole that needs to be fixed.” He added: “The auditors would have to know who the related party is. Why not just put that in there? How hard can it be? By keeping it purposely opaque it’s defeating the purposes of the footnote.”

FTX’s new chief executive, John J. Ray, said in a bankruptcy-court filing on Thursday that the company’s financial information wasn’t trustworthy and that it was controlled by “a very small group of inexperienced, unsophisticated and potentially compromised individuals.”

Mr. Bankman-Fried and several other former executives of FTX didn’t respond to requests for comment.

The lack of detail echoes past scandals. Enron Corp., in its 1999 financial reports, didn’t disclose that its related-party transactions involved its chief financial officer, Andrew Fastow, only describing the person as a senior officer of Enron. The energy-trading company eventually did identify Mr. Fastow in connection with the transactions. That information helped set its downfall in motion.

Unlike Enron, the FTX empire wasn’t a public company. And FTX Trading, based in the Bahamas and incorporated in Antigua, was just one of more than 100 companies in Mr. Bankman-Fried’s network of holdings. FTX Trading said in its report that it followed U.S. generally accepted accounting principles, and it hired an outside auditor, Prager Metis CPAs LLC, which vouched for its books.

Prager Metis, in an email, said that “we stand behind our audit opinion” for FTX Trading and that “all disclosures were presented in accordance with GAAP.” The firm said it was “only the

auditor for the financial statements of FTX Trading Ltd.” and not other FTX-related companies.

In the footnote, FTX Trading described the \$1.2 billion related-party receivable as “an intercompany account with these related entities to facilitate certain corporate transactions” as part of its “treasury management arrangements.” It said that had been paid down to \$600 million sometime earlier this year, but it provided few other details about it.

A disclosure for another set of transactions described certain “currency management” activities. It said “these related companies also entered into an ‘FTX equity-for-FTT Crypto’ option agreement” in connection with FTX Trading’s 2020 purchase of a majority stake in a company called Blockfolio Inc. FTT is a digital coin created by FTX.

FTX Trading paid \$84 million, largely with a \$79 million IOU that was denominated in FTT. The \$79 million liability represented FTX Trading’s obligation to deliver 20 million FTT tokens, based on their value at the time. FTX said it planned to pay for the acquisition gradually over two years.

While the disclosure was complex, the point was to let FTX Trading swap its own equity for the FTT tokens that it would use to pay for Blockfolio. In exchange for the FTT tokens, FTX Trading planned to issue 32.5 million shares and pay \$1 million in cash; the disclosure didn’t name the recipient. By comparison, FTX Trading had 390.5 million shares outstanding.

The swap resulted in a liability and a receivable, both of which FTX Trading “marked to market based on the quoted price for the FTT tokens.” The value of FTT soared, and by the end of 2021 the receivable was up to \$497 million. The collapse of FTT was central to FTX’s own swift demise.

Since last week’s collapse, details of loans to FTX principals have begun trickling out in bankruptcy-court filings. Mr. Ray, in his declaration, said there was \$4.1 billion of outstanding loans by Alameda Research to related parties as of Sept. 30, including \$1 billion to Mr. Bankman-Fried. Alameda, which Mr. Bankman-Fried founded and owned, is the trading company that borrowed FTX customers’ money to help meet its own liabilities. Its troubles helped lead to FTX’s bankruptcy.

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