Vermonters should exercise caution with Cryptocurrencies

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01/29/2018 (All day)
For Immediate Release Monday, January 29, 2018

January 29, 2018 – With cryptocurrencies continuing to attract headlines, the Department of Financial Regulation ("DFR") reminds Vermont investors to be cautious about investments involving cryptocurrencies.

"The recent success of cryptocurrencies has drawn considerable interest from the investing public and the media, however, Vermonters should educate themselves about the risks associated with cryptocurrencies, including high volatility and limited oversight, before deciding to invest," said DFR Commissioner Michael Pieciak.

Cryptocurrencies are a medium of exchange that is created and stored electronically in the blockchain, a distributed public database that keeps a permanent record of digital transactions. Current common cryptocurrencies include Bitcoin, Ethereum and Litecoin. Unlike traditional currency, these alternatives have no physical form and typically are not backed by tangible assets. They are not insured or controlled by a central bank or other governmental authority, cannot always be exchanged for other commodities, and are currently subject to little or no regulation.

A survey of state and provincial securities regulators by the North American Securities Administrators Association (NASAA), of which DFR is a member, shows 94 percent believe cryptocurrencies involve a "high risk of fraud." Regulators also were unanimous in their view that more must be done to provide greater investor protection.

"Until this past year, the price of Bitcoin was relatively stable, but dramatic price increases and FOMO (the 'Fear Of Missing Out') have caused some investors to rush into an investment they may not fully understand," Pieciak said. "Cryptocurrencies may be a high-risk product with an unproven track record and high price volatility, and when combined with a high risk of fraud, investing in cryptocurrencies is not for the faint of heart."

Last month, NASAA identified Initial Coin Offerings (ICOs) and cryptocurrency-related investment products as emerging investor threats for 2018. Unlike an Initial Public Offering (IPO) when a company sells stocks to raise capital, an ICO typically sells "tokens" in order to fund a project, usually related to the blockchain. The token likely has no value at the time of purchase. Some tokens constitute, or may be exchangeable for, a new cryptocurrency to be launched by the project, while others entitle investors to a discount, or early rights to a product or service proposed to be offered by the project.

NASAA offers a short animated video to help investors understand the risks associated with ICOs and cryptocurrencies. Vermonters are encouraged to call (802-828-3420) or email (dfr.securitiesInfo@vermont.gov) DFR with questions relating to cryptocurrencies.

Common Cryptocurrency Concerns

Some common concerns investors should consider before investing in cryptocurrency:

The high volatility of cryptocurrency investments makes them unsuitable for most investors, especially those investing for long-term goals or retirement.

Cryptocurrency accounts are not insured by the Federal Deposit Insurance Corporation (FDIC) or National Credit Union Administration (NCUA), which insures bank and credit union deposits up to $250,000.

Cryptocurrency are subject to minimal regulatory oversight, susceptible to cybersecurity breaches or hacks, and there may be no recourse should the cryptocurrency disappear.

Investors in cryptocurrency are highly reliant upon unregulated companies, including some that may lack appropriate internal controls and may be more susceptible to fraud and theft than regulated financial institutions.

Investors will have to rely upon the strength of their own computer security systems, as well as security systems provided by third parties, to protect purchased cryptocurrencies from loss or theft.
Common Red Flags of Fraud

DFR also reminds investors to keep watch for these common red flags of investment fraud:

"Guaranteed" high investment returns. There is no such thing as guaranteed investment returns, and there is no guarantee that the cryptocurrency will increase in value. Be wary of anyone who promises a high rate of return with little or no risk.

Unsolicited offers. An unsolicited sales pitch may be part of a fraudulent investment scheme. Cryptocurrency investment opportunities are promoted aggressively through social media and craigslist. Be very wary of an unsolicited communication—meaning you didn't ask for it and don't know the sender—about an investment opportunity.

Sounds too good to be true. If the project sounds too good to be true, it probably is. Watch out for exaggerated claims about the project's future success.

Pressure to buy immediately. Take time to research an investment opportunity before handing over your money. Watch out for pressure to act fast or "get in on the ground floor" of a new tech trend. Unlicensed sellers. Many fraudulent investment schemes involve unlicensed individuals or unregistered firms. DFR can help investors research the background of those selling or advising the purchase of an investment. The Department can be reached at 802-828-3420, dfr.securitiesInfo@vermont.gov or through our website at dfr.gov.