

Avoiding Bitcoin bubbles and cyber currency scams

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The surge of interest in cryptocurrencies is predicted to see investors getting their fingers burned as volatility continues and while the sector remains unregulated.

At the end of last week, Bitcoin was trading at just under US \$8,000, around half the \$19,000 peak it reached in November, and now Lloyds Bank has taken the step of blocking cryptocurrency purchases on its credit cards. While debit cards can still be used, the bank has moved to protect itself against possible losses if card holders are unable to settle their accounts following big drops in value.

It follows an announcement by Facebook last week that it would ban all advertisements for cryptocurrencies across its platforms, including Instagram, because they were too often associated with scams.

And while the Government has announced plans to apply anti-money laundering regulation to digital currency exchanges in the UK, as part of an EU-wide initiative to prevent criminal use while still enabling innovation, many of those involved in cryptocurrency trading are currently untraceable due to their being unregulated.

Cryptocurrencies have been around for the past decade and rely on blockchain technology, which is effectively a digital ledger shared and verified across innumerable computers worldwide, protected by complex cryptography to make it secure and resistant to fraud. The blockchain technology is expected to bring many benefits, and to play an increasingly important role in delivering greater security for cyber transactions and the transfer of money in future, for example in property transactions. But alongside, the digital currencies that have grown on the back of blockchain are often making

headlines for different reasons, with online and email scams proliferating.

Corporate partner, Veronica Hartley said: *“Bitcoin is the most well-known cryptocurrency and some people are calling the current situation a ‘Bitcoin Bubble’ after the phenomenal fluctuations in value seen over the past year. Perhaps because it is described as digital money, and called a ‘currency’, many people are approaching cryptocurrency as though it were like sterling, the euro or US dollar - legal tender determined by government – with an intrinsic value, where in fact it’s a high-risk gamble.”*

Growing out of cryptocurrencies are initial coin offerings, commonly abbreviated as ICOs, which are being used increasingly as an investment route, mainly by companies using blockchain technology. Here, companies raise funds by issuing tokens to investors instead of shares. The tokens are not the same as equity but can be traded with third parties and have a specific set of rules, which may include rights that are similar to holding shares. The rules are embedded in a so-called ‘smart contract’, which forms part of the token. The tokens provide security against the rules being broken, since if the smart contract is breached the funds can be returned to investors, but the volatility in the exchange rates and prices of cryptocurrencies makes ICOs inherently risky, for both investors and the new businesses themselves.

In addition, many ICOs come to the market with vague promises, and too often investors may come up against ICO campaigns that are fraudulent. Few will have the established brand offered by Telegram, one of the most high-profile ICOs, for their Gram cryptocurrency and encrypted messenger app, which is currently on ‘pre-sale’ to institutional investors. Telegram’s vision is for a system that enables instant payments across the globe using

cryptocurrency instead of state-backed currencies. Thanks to the founders' track record, the initial offering is said to be over-subscribed, with predictions that they may raise as much as \$1.2bn, making it by far the largest ICO to date.

Veronica added: *"Regulation and the law are playing catch up for now, and in view of the complexity surrounding such trading, it's worth taking professional advice before making an investment – whether buying bitcoin or any other digital currency, or when looking to get involved in investing in a new company through an initial coin offering."*



Note: This is not legal advice; it is intended to provide information of general interest about current legal issues.

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