

ISLE OF MAN

CONSUMER MATTERS

Safeguard your future



ICOs and cryptocurrency What's all the fuss about?

JARGON BUSTER

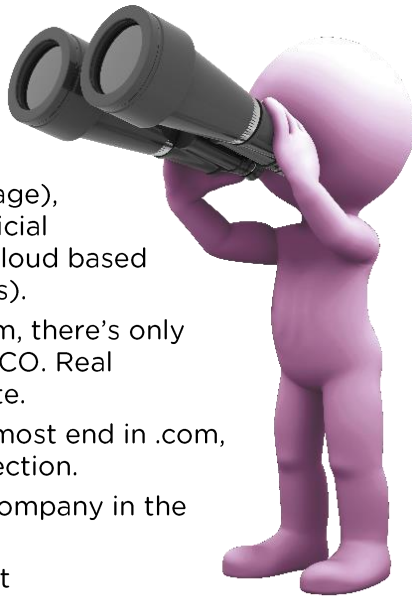
Initial Coin Offering ('ICO')	An ICO is similar to a company raising finance by an initial public offering ('IPO'); but traditional company law safeguards don't apply. ICOs can be used by start-up businesses who want to develop services or products. Participants receive coins/ tokens instead of shares. There is international debate about whether/ how to regulate ICOs.
Cryptocurrency	A digital, virtual currency designed to act as a medium of exchange which records its transactions on blockchain.
Blockchain	Software which records transactions (e.g. who owns cryptocurrency) using an internet based global distributed ledger over thousands of computers. There is no master ledger and transactions are verified on an ongoing basis. Each transaction is digitally signed to prevent tampering.
Coin or Token	Participants in an ICO are given coins or tokens on Blockchain. If a cryptocurrency or ICO is developed from scratch it's a coin. If it uses existing software, it's a token.
Asset Tokens	Asset tokens give a debt or equity claim against the entity issuing the token, e.g. a promise to share in future profits. These tokens are similar to equities, bonds or derivatives but are not normally subject to investment regulation.
Payment Tokens	Tokens used as a means of payment for goods or services or as a means of money or value transfer, now or in the future.
Utility Tokens	Tokens redeemable for specific purposes or for what the company is selling, e.g. memberships or discounts.
Hybrid Tokens	Tokens which combine payment/ utility/ asset rights.
Decentralised Currency	A national currency, like sterling, is controlled by a central bank. A decentralized currency doesn't have one person in control, e.g. anyone can mine Bitcoin. Instead of trusting a government to back currency, cryptocurrencies' value comes from network users trusting the network.
ICO and crypto exchanges	Online platform where customers can buy and sell coins and tokens using traditional payment or cryptocurrencies.
Pump and dump	A technique to raise interest in a venture so that existing participants (who are often insiders to the venture) can sell their coins or tokens at a significant profit.
IoMFA	The Isle of Man Financial Services Authority.

A Smart Investor investing in initial coin offerings, digital assets and other online investments:

- Understands the risks that are associated with initial coin offerings and crypto-assets in general and is careful in deciding whether to invest in these products
- Does not forget about the importance of due diligence when considering investments in online and digital environments
- Never invests based solely on a celebrity endorsement
- Knows that most legitimate firms do not allow their customers to use credit cards to make investments.
- Recognises the red flag warning signs of online investment fraud (see later).

Protect yourself:

- Only use the official wallet of the company to pay, it can always be found on the company website.
- Never send your email address on a Telegram group in a PM (Private Message), unless you are sure you're using an official admin contact. (Telegram is a secure cloud based messenger which is often used by ICOs).
- Don't fall for fake channels on Telegram, there's only one official Telegram group for every ICO. Real addresses are found on the ICO website.
- Pay attention to the website address, most end in .com, and check the https for a secure connection.
- If unsure, ask an administrator of the company in the telegram group.
- ALWAYS do your research. If you don't understand everything or you aren't 100% convinced it is legitimate, don't buy it.
- If it sounds too good to be true, it probably is!



Pros and Cons of an ICO

The companies that run ICOs are fundraising to produce a product, like a piece of software, a new cryptocurrency or an online service. Most companies run their ICOs very early in development, and ICOs can be run to generate interest in the company. As more interest is generated, tokens and coins increase in value. People then sell off their coins for a profit to others that are interested, which creates an incentive to spread the knowledge of the product around.



Positives

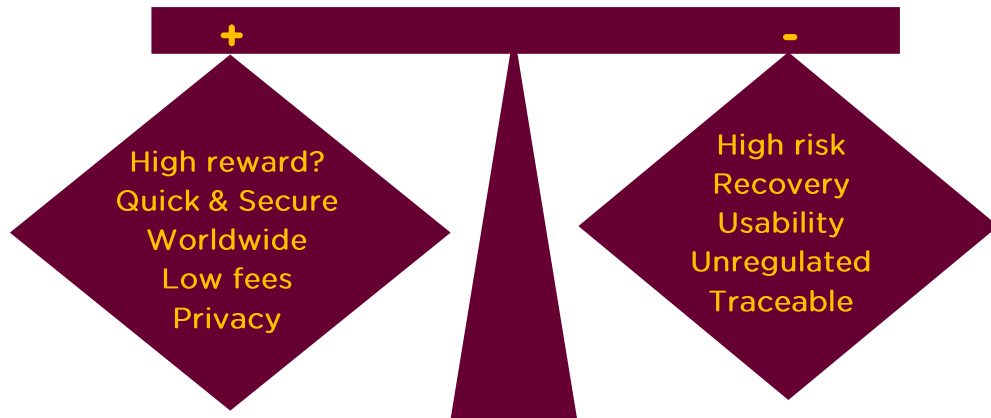
- **Potential for high reward:** ICOs can go up in value very quickly. If they do, you can take profits out easily through an ICO exchange (but this is not guaranteed).
- **Less susceptible to hackers:** ICO transactions are encrypted and recorded on blockchain. This means it is harder to intercept tokens.
- **Available to the public:** anyone can create an ICO or invest in one.
- **Privacy:** people participating in ICOs can remain pseudo-anonymous due to encryption (through individual identification codes) – but this means you don't know who you are dealing with.

Negatives

- **High Risk:** New ventures are more risky. If they don't develop their product/ service and find a market they will fail and any coin or token will have no value.
- **Open to fraud:** ICOs can be scams. Be aware of the red flags for ICO scams and do your homework.
- **Unregulated:** If ICOs aren't regulated and something goes wrong the regulator can't intervene, and consumer protections may not apply.
- **Uncertainty:** ICO's are not required to produce detailed information about their proposal (unlike IPOs).

Pros and Cons of a cryptocurrency

Cryptocurrency can be used as a medium of exchange or to store value; it is seen as secure because it is recorded on the blockchain.



Positives

- **Potential for high reward:** Since the cryptocurrency market is volatile it can give high rewards.
- **Quick and Secure:** Transactions are quick, permanent, and hard to fake, this eliminates a lot of the fraud.
- **Worldwide:** Available to people in countries that don't have access to financial services.
- **Low fees:** Cryptocurrency has low transaction costs compared to other digital payment methods like PayPal or traditional transfers like BACs.
- **Privacy:** pseudo-anonymous due to encryption (each person has an individual identification code ("key")).

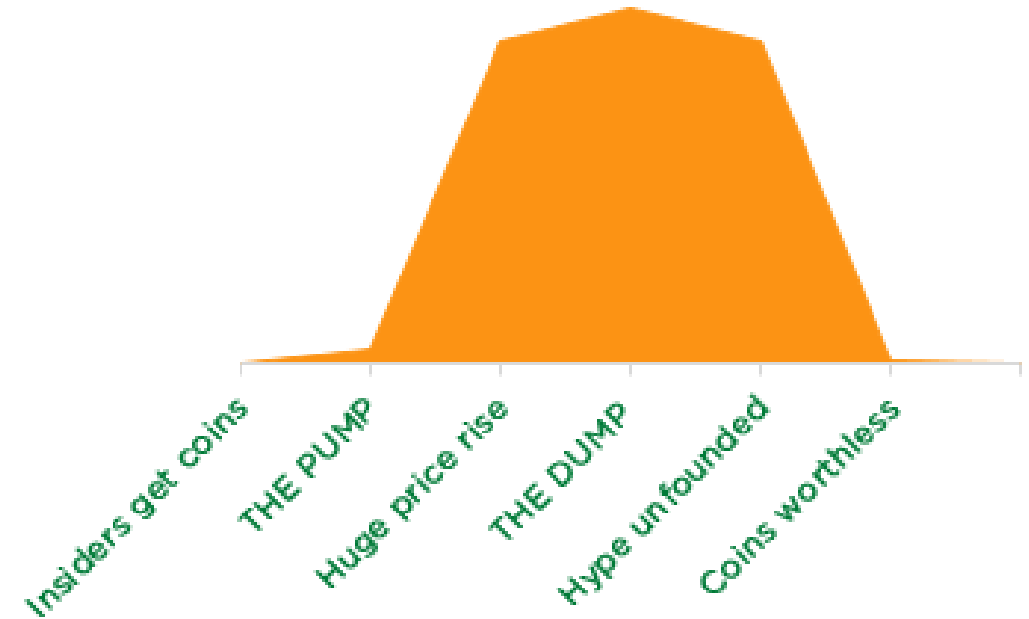
Negatives

- **High Risk:** Cryptocurrency is volatile; value can change wildly and quickly. In 2014 Bitcoin ranged between \$30 and \$1000 per coin.
- **Difficult to recover:** If something goes wrong with a transaction or you hold coins personally and lose your "key" you can't recover it.
- **Usability:** Cryptocurrency is only accepted by certain vendors and value fluctuates. The money saved in transaction costs could be negligible.
- **Unregulated:** if cryptocurrencies aren't regulated and something goes wrong the regulator can't intervene, and consumer protections may not apply.
- **Traceable** - Cryptocurrency is not anonymous; the public ledger details all activity.

What can go wrong?

A Smart Investor doesn't just consider the potential benefits of participating in a venture, they also consider what can go wrong.

Pump and Dump



A Pump and Dump scheme is a fraud where insiders manipulate coin prices so they can profit from your investment.

- An insider group will organise a mass purchase of coins (often very early and at a discount to the launch price).
- They then hype the venture (THE PUMP) and its prospects of huge rewards to raise public interest.
- The value of coins goes up sharply
- The insiders sell at a huge profit (THE DUMP).
- The hype was unfounded and coin values plummet meaning consumers lose their money.

Non existent offerings

It is very easy to make a fake website: stock photos can be taken from the internet and jargon can be used to confuse people. Do your research and make sure the opportunity is real.

Failed Business Models

There is always the chance that any project will not work due to a lack of planning, running out of money, lack of interest, or general incompetence. This could also mean you losing your money, either in a project that doesn't materialise, or on worthless coins or tokens, which were devalued due to a lack of interest.

Volatility

Cryptocurrencies and ICOs are volatile. In the past, Bitcoin has fluctuated by over 40% in one day. If you buy at the higher price and the price goes down so does the value of your coins.

The value of cryptocurrencies is only based on supply and demand. If users lose trust in a cryptocurrency there are no assets or central bank backing it.

Security of your records

Hackers will target cryptocurrencies and ICOs due to their value. Although the blockchain makes it difficult for a hacker to steal coins or currency whilst it is traded, a hacker can steal cryptocurrency that is sitting on your computer. Due to fraud, hacking and viruses, as many as 3 million bitcoins have been lost. As there is a 21 million bitcoin cap, this means that as much as 14% of the total supply has been lost.



Red flags for online investment fraud

- ❗ **Poor Grammar/ Spelling** can indicate a scam. Serious operations will take the time to make sure their proposals are professional.
- ❗ **Pressure/Sense of Urgency** - Many ICO websites include countdown clocks to create a sense of urgency around You are more likely to invest if the 'deal' is a limited time event.
- ❗ **No time frame on sales** - Serious ICOs will have a deadline on token sales as they need the funds to develop the software or business proposal detailed in their white paper
- ❗ **High/unrealistic returns and interest/ If it sounds too good to be true, it probably is**
- ❗ **Guarantees** - the performance of any new business is uncertain. Unsupported guarantees can attract unsuspecting investors
- ❗ **Claiming to be regulated** - typically ICOs and cryptocurrencies aren't regulated. On the IOM they are registered with the IoMFSA for anti money laundering oversight but aren't regulated. If it says it's regulated, check the regulator's website to make sure.
- ❗ **Vague whitepaper (or non-existent)** - Credible ventures will have a whitepaper which sets out what the company will do with the money it raises. The document will detail team members and co-founders and their backgrounds and give a primary address. Check that the address exists and is not a residential location.
- ❗ **Celebrity endorsements or impersonations** - Celebrities promote lots of things. Being promoted by a famous person doesn't guarantee that something is any good. The celebrity may not understand an ICO or cryptocurrency; do your own research and do not base your decision on celebrity endorsements.
- ❗ **Co-founders, team members and advisers - who are they, are they genuine and what is their background** If the information doesn't stack up this is a clear indicator of a scam.
- ❗ **Code repository** - Get someone with programming knowledge to check the repository code for an ICO. Red flags for poor coding, e.g. more than 50 lines of codes for a function, can indicate lack of expertise and/ or fraud.
- ❗ **Credit card payments** - The majority of licensed and registered investment firms don't accept credit cards for investments. If an ICO asks for a credit card payment take care.