



*Commission de Surveillance  
du Secteur Financier*

## WARNING

### WARNING ON INITIAL COIN OFFERINGS (“ICOs”) AND TOKENS

**Raising funds from the public in the form of so-called initial coin offerings (“ICOs”) is not subject to a specific regulation and does not benefit from any guarantee or other form of regulatory protection. ICOs are highly speculative investments, associated with a certain number of risks, including a total loss of investment.**

#### Introduction

The Commission de Surveillance du Secteur Financier (CSSF) warns the public of the significant risks associated with ICOs. These forms of fundraising often use the appeal of new technologies and virtual currencies, or relating projects, to promote their activities with potential investors.

In this context, the CSSF recognises and stresses that the technology underlying these ICOs, the blockchain technology, may bring about certain benefits through its use in financial sector activities and in various innovative projects. Thus, the CSSF specifies that this warning only concerns fundraising through ICOs that use this technology, without questioning the technology itself.

ICOs are a form of fundraising from the public with the purpose of financing the launch of new virtual currencies or any sort of new projects.

In exchange for participating in the financing, the participant receives digital tokens issued by the initiator, which may, where applicable, grant certain rights to their holders. These rights are freely defined by the initiator and may take different forms, such as the provision of a service, a share in the capital of the company being formed, the right to a part of the profit or the right to receive a manufactured product. The appreciation of the tokens' value for a participant relates foremost to the rights, which are of a various nature (and which makes their evaluation difficult), together with the capacity of the counterparty to fulfil its commitments.

The technology used allows identifying and verifying the electronic address of the owner of a token at any time, in principle without the intervention of a third party. Issuances of tokens are sometimes structured so as to allow their exchange on specialised platforms.

#### How does an ICO take place?

Generally, an ICO is announced through the publication of a White Paper, and, where relevant, an executive summary. Typically, the White Paper describes, in a more or less detailed and commercial manner, the terms and conditions of the offer, the project at the origin of the fundraising, the duration of the offer, the token subscription and issue mechanism, as well as the rights attached to the token issued. In the absence of specific regulations governing its content, the White Paper may unfortunately take the appearance of a prospectus for an offer to the public.

The public may participate in the financing of the project for a period of time that has been predefined in the offer by making payments to the initiator in accordance with the requirements described in the White Paper. Besides payments in virtual currencies, the initiators of the projects accept more and more often fiat currencies in order to reach a wider public.

At the expiry of the offer, the tokens are created and distributed to the participants. Usually, these tokens can be kept in electronic wallets and structured so as to allow their trading on specialised platforms. Some tokens carry the right to the provision of a service, reductions on certain services or the acquisition of products, while others are structured so as to create rights close to those attached to shares of a company.

### **Risks associated with ICOs**

The CSSF stresses that ICOs can involve significant and often unforeseeable risks for professional investors as well as for consumers that participate in the initial call for financing or who invest in tokens on or through specialised platforms.

In particular, the CSSF considers that the major risks linked to ICOs are the following:

- Lack of protection

There are currently no specific regulations that apply to ICOs either at national or European level. Investments in ICOs do not enjoy any guarantee or other form of particular protection and are highly speculative.

- Success of the financed project

The projects financed by ICOs are usually in an early stage of development and based on business plans that have not been assessed independently. There is no guarantee that the projects will be developed or will have the expected success. As a consequence, it is impossible to anticipate if the tokens issued in consideration for the participation in the financing will have or can generate any value.

- Loss of capital

The capital invested in the financing itself or in the tokens generated through secondary markets is not guaranteed. As a consequence, the capital invested can be partially or totally lost depending on market developments. Also, there is no guarantee that the initiator is really able to fulfil its contractual obligations following the fundraising. In this context, the rights attached to the tokens may turn out to have no subsequent value.

- Historical rapid growth in value

Recent substantial upward fluctuations of a certain number of virtual currencies in a short lapse of time triggered a wave of euphoria which drove investments through ICOs. Many participants hope that past evolutions will repeat and that the value of their portfolio will grow exponentially. The impression of missing out may obscure the serious underlying risks. Participants should consider that past evolutions are not a guarantee for the future, and that fluctuations may also take the opposite direction, and that they could thereby lose everything.

- Risk of token theft

Specialised platforms and token storage systems may present vulnerabilities as regards their security, which can lead to risks of hacking and theft. Moreover, it cannot be excluded that tokens are seized or confiscated.

- Liquidity shortage

The tradability of the tokens on specialised platforms, if provided for, is conditional on sufficient liquidity, i.e. a sufficient number of tokens outstanding and the existence of a demand from third parties. As a consequence, holders of tokens may be unable to sell them, or only in adverse conditions.

- Volatility

Tokens can be subject to extreme price fluctuations and constitute a price bubble risk. The capital invested in tokens through participation in an ICO or via specialised service providers is not guaranteed and can, depending on price evolution, be partially or totally lost.

- Fraud and money laundering

The lack of regulation and supervision is likely to attract criminals that use ICOs in order to create fraudulent schemes or commit scams. Likewise, ICOs can be a means to carry out money-laundering or terrorist-financing transactions.

- Operational disruption

The technologies allowing the creation, transfer and safekeeping of tokens being particularly innovative, they can be vulnerable and, as a consequence, expose investors to lasting or temporary disruptions of systems, hacking attempts, problems relating to activity peaks, etc. As a consequence, investors are exposed to the risk of tokens being unavailable.

- Misleading information, lack of transparency and risk of price manipulation

White Papers are not subject to specific regulations and may contain incomplete or even misleading information as regards the description of the financed project and its economic potential, the applicable terms and conditions or the rights attached to the tokens issued and the charges levied. In the absence of a supervision performed by a public authority, the information disclosed by the initiator in the White Paper is not subject to any control or verification and could be inaccurate. Furthermore, the lack of regulated information on the amount of tokens issued, the amount of funds collected, the evolution of the rights attached to the tokens and the financial situation of the initiator, will not allow an investor or a potential purchaser to get an idea of the value or the possible liquidity of the token. This absence is also a breeding ground for value manipulations where trading takes place on specialised platforms.

- An investment which does not suit all types of investors and objectives

The risks associated with investments through ICOs mean that these investments are not appropriate for most of the consumers and under no circumstances for long-term projects such as retirement projects.

## **The CSSF recommends investors to be prudent in their acquisitions**

The CSSF advises interested investors to be extremely prudent and to ensure the reliability and soundness of the initiator by performing researches on the latter, in particular as regards the registered office, the legal form, the incorporation deed, the capital and the persons involved in the project, including the person and the home country of the account on which amounts in currency or virtual currency should be transferred. Where the initiator is a Luxembourg legal person, some of this information is available on the website of the Registre de Commerce et des Sociétés de Luxembourg ([www.rcsl.lu](http://www.rcsl.lu)).

Where the promotional documentation or the initiator's website mentions an authorisation, the CSSF strongly advises to refer to the website of the home State regulator in order to check if the initiator really holds the alleged authorisation, the extent of that authorisation or if the regulatory authority has already issued a warning to the public concerning the activities of the initiator concerned.

Moreover, the CSSF advises interested investors to ensure that they have fully understood the risks associated with the project and the return on their investment before making any investment whatsoever. If in doubt, the CSSF advises the interested investors to ask the initiator and to verify the answers received with independent sources.

The CSSF reminds that it is essential not to risk money one cannot afford to lose.

## **Information for entities under the prudential supervision of the CSSF**

As stated in the risk section above, the entities under the prudential supervision of the CSSF must take into account that investing in tokens through ICOs is not suitable to all kinds of investors and investment objectives. UCITS, UCIs addressing non-professional customers and pension funds are thus not allowed to invest directly or indirectly in virtual currencies.

## **Information for service providers and initiators of ICOs**

Despite the lack of specific regulations that applies to ICOs, the activities related thereto or implied through the creation of tokens, the collection and raising of funds may, depending on their characteristics, be subject to certain legal provisions in Luxembourg and thus to certain supervisory requirements. The CSSF will not hesitate to assess such fundraising activities by extending its analysis to the objectives pursued in order to assess whether it could be a scheme to circumvent or avoid financial sector regulations, notably the provisions of the Law of 10 July 2005 on prospectuses for securities and the Law of 5 April 1993 on the financial sector. The CSSF considers that for any fundraising, the initiators of such ICOs are required to establish anti-money laundering and terrorist financing procedures.

## **Warnings issued by European Supervisory Authorities**

- [https://www.esma.europa.eu/sites/default/files/library/esma50-157-828\\_ico\\_statement\\_firms.pdf](https://www.esma.europa.eu/sites/default/files/library/esma50-157-828_ico_statement_firms.pdf) ;
- [https://www.esma.europa.eu/sites/default/files/library/esma50-157-829\\_ico\\_statement\\_investors.pdf](https://www.esma.europa.eu/sites/default/files/library/esma50-157-829_ico_statement_investors.pdf).

Luxembourg, 14 March 2018