ISRAEL SECURITIES AUTHORITY

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Warning to Investors Regarding Cryptocurrency Investments

The Israel Securities Authority (ISA) warns the investor public of the dangers of investing in cryptocurrencies. Such investments may be made in various ways: by purchasing popular cryptocurrencies such as Bitcoin, by purchasing cryptocurrencies in ICOs (Initial Coin Offerings), or by investing in other ways in companies who are active in the fied of cryptocurrencies. All these types of investments carry heavy risks for investors, including a tangible risk of loss of the entire investment amount. The ISA urges investors who are considering putting their money in this field, either directly or indirectly, to read this warning carefully before making a decision.

Why one should be careful before investing in cryptocurrencies?

Cryptocurrencies are issued on the basis of new Distributed Ledger Technology. Some believe that this technology is expected to develop into a true innovation for entrepreneurs, investors, and the economy as a whole. Currently, however, this area is subject to multiple risks that differ in both degree and nature from conventional traditional capital market risks. The risks of investing in cryptocurrencies include:

- **Market risks**, such as development of a bubble (artificially inflated prices), extreme price volatility, and low liquidity that limits investor's ability to redeem his/her investment.
- **Operational risks**, such as risks of fraud and trading manipulations on unregulated and unreliable trading platforms, and the risk that funds originating in cryptocurrency will not be accepted for deposit in the banking system.
- **Information security (cybersecurity) risks**, such as loss or theft of personal keys (passwords) to digital wallets that offer access to cryptocurrencies. Cyber-attacks against unregulated trading platforms and digital wallets are a common occurrence.
- **Regulatory risks**, where future regulation of cryptocurrencies' operations may lead to significant implications for companies in this field, in some cases to the extent of preventing their continued operations.

Investors who choose to put their money, either directly or indirectly, in cryptocurrencies investments face a high probability that one or more of these risks will materialize, causing investors to lose their investment entirely.

Should cryptocurrencies investors be concerned of fraud?

The answer is yes. New technologies typically create new opportunities, but also attract parties that wish to exploit these opportunities to enrich themselves at the expense of innocent customers. Cryptocurrency fraud can lead to the loss of one's entire investment, and since the operations in this field are largely unregulated, the risk of fraud is greater than usual. Here are some typical warning signs of fraud:

- Promise of a high or consistent return is an empty promise. Investors should beware of individuals who offer high or consistent returns with little or no risk.
- Unsolicited offers may be part of a scam. Investors should exercise extreme caution when receiving unsolicited offers from unfamiliar individuals or offers that are not part of regulated services that they typically receive.
- If the offer sounds too good to be true, it probably is. The greater the chances of large profits, the greater the risk.
- A pressure to act quickly should alert that the offer may be a scam. Investors should not be seduced into making investments quickly and should properly study each investment offer. Generally, after you transfer your money, there is no going back.
- If the party making the investment offer is not a regulated entity, its operations are extremely risk, and may even be illegal. Investors should be aware of investing in unregulated entities.

What should a person who is considering a cryptocurrencies investment take into account?

In view of the multiple risks involved, investors should exercise extreme caution before deciding on an investment in cryptocurrencies. Here are some important factors that investors should examine before making such a decision:

<u>ICOs</u>

- Initial Coin Offerings by ventures seeking to raise capital might be considered a public offering of securities. In this case, the ICO must conform to the Securities Law and is subject to the publication of a prospectus. If the ICO is not made according to a prospectus, investors should inquire into the reason for this absence, and be careful about participating in illegal capital raising.
- Use of investors' funds – How do the entrepreneurs intend to use investors' money, and what are the declared goals of the issue? Do investors have access to a well-

developed business plan that is easily read and understood? Are investors' funds property protected, and will the funds raised by the entrepreneurs be used only for the goals stated in the business plan and not for any other goals?

- The rights that the cryptocurrency confers - What rights does the cryptocurrency confer? Are they unambiguous and clearly defined?
- The ability to sell the cryptocurrency on a regulated secondary market – Is there a secondary market for the cryptocurrency? Can investors freely sell the cryptocurrency? Can investors re-sell the cryptocurrency to the issuing company for a refund? Remember that different mechanisms for creating and deleting currencies on demand include various restrictions that affect the price and scale of permitted transactions, among other things. Cryptocurrencies are not substitutes for genuine liquidity.
- Information transparency – Have the issuers disclosed information about the operations and the individuals behind them? For example, did issuers make disclosures about the scope and goals of the capital raising, the entrepreneurs' background and personal experience, the number of tokens that was or is expected to be sold, or the business or technological concept?

<u>Direct Investments in common cryptocurrencies</u>

Even investments in the better known cryptocurrencies such as Bitcoin involve multiple risks. Investors should also take into consideration the following risks:

- Extent of security and exposure to cyber risks – Digital wallets, especially those operated by third parties such as trading platforms, are vulnerable to fraud, theft, hacking, and technical malfunctions. Investors should exercise extreme care in selecting the service providers they use to trade in or hold their cryptocurrencies. Investors should confirm that these service providers are large regulated entities that follow strict control procedures that protect their customers' money.
- Volatility and risk of losing the entire investment – The field of cryptocurrencies is characterized by extreme fluctuations in prices, rising and falling by hundreds and thousands of percent in a short time. Frequent changes in the prices of these cryptocurrencies may constitute a significant risk for investors, who must be prepared to lose a substantial portion or all of their investment in a short time, even if investors have studied all the other factors listed above.
- Reliability and robustness of the trading platforms and risks of fraud and scams – Most of the world's trading platforms that function as secondary markets for cryptocurrencies are not regulated. This lack of regulation creates adverse effects

of lack of transparency or fairness in trading, such as manipulations in quoted prices and pump-and-dump schemes. Investors should maintain a skeptical and suspicious attitude toward the information that these platforms present about themselves and their trading data. Investors should take into account that the financial strength and managerial quality of these platforms has not been vetted, and investors may find it difficult to recover their funds in the event of a theft, fraud, or collapse of a trading platform.

- Converting cryptocurrency into New Israeli Shekels (NIS) or other national currency - In addition to investors' concerns of liquidity, investors may encounter substantial problems in an effort to realize their investments and convert them into other currency. Conversion may entail high costs and delays in the transfer of funds between all the parties involved. Investors may find it difficult to redeem cryptocurrency investments. Furthermore, investors may find it difficult to track funds transferred in cryptocurrency or deposit such funds into the banking system, due to anti-money laundering and terrorism financing restrictions, among other things.

Indirect investments in cryptocurrencies

The risks of direct investments in cryptocurrencies (through an ICO or a secondary market) also apply to investments in private and public companies that intend to enter this field. Investors must be aware that the risks described above may apply to companies that plan to operate in the field of cryptocurrencies. Such risks raise doubts regarding the true economic value of these companies and the appropriate pricing of their securities. Investors who choose to invest in such companies should be aware that such investments are extremely high-risk investments compared to other capital market investments, and entails a tangible risk of loss of one's investment, including the loss of the entire invested amount.