



ESA 2022 15

## EU financial regulators warn consumers on the risks of crypto-assets

The European Supervisory Authorities (EBA, ESMA and EIOPA – the ESAs) warn consumers that many crypto-assets are highly risky and speculative. These are not suited for most retail consumers as an investment or as a means of payment or exchange.

Consumers face the very real possibility of losing all their invested money if they buy these assets. Consumers should be alert to the risks of misleading advertisements, including via social media and influencers. Consumers should be particularly wary of promised fast or high returns, especially those that look too good to be true.

Consumers should be aware of the lack of recourse or protection available to them, as crypto-assets and related products and services typically fall outside existing protection under current EU financial services rules.

### THINGS YOU SHOULD KNOW AND CHECK

You should be aware of the specific risks of crypto-assets and related products and services and carefully weigh up whether the risks are acceptable given your own preferences and financial situation. These include the risk that:

- you may lose all the money you invest;
- prices can fall and rise quickly over short periods;
- you may fall victim to scams, fraud, operational errors or cyber attacks; and
- you are unlikely to have any rights to protection or compensation if things go wrong.

If you are thinking about buying crypto-assets or related products and services, you should ask yourself the following:

- can you afford to lose all the money you invest?
- are you ready to take on high risks to earn the advertised returns?
- do you understand the features of the crypto-asset or related products and services?
- are the firms/parties you are dealing with reputable?
- are the firms/parties you are dealing with blacklisted by the relevant national authorities?<sup>1</sup>
- are you able to protect effectively the devices you use for buying, storing or transferring crypto-assets, including your private keys?

### What are the key risks?

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<sup>1</sup> Please note that not being blacklisted is no guarantee that a firm/party is safe to engage with

- **Extreme price movements:** many crypto-assets are subject to sudden and extreme price movements and are speculative, because their price often relies solely on consumer demand (i.e., there may be no backing assets or other tangible value). You may lose a large amount or even all of the money invested. The extreme price movements also mean that many crypto-assets are unsuitable as a store of value, and as a means of exchange or payment;
- **Misleading information:** some crypto-assets and related products are aggressively advertised to the public, using marketing material and other information that may be unclear, incomplete, inaccurate or even purposefully misleading. For instance, advertisements via social media may be very short, with a focus on the potential gains but not the high risks involved. You should also beware of social media ‘influencers’ who typically have a financial incentive to market certain crypto-assets and related products and services and therefore may be biased in the communications they issue;
- **Absence of protection:** the majority of crypto-assets and the selling of products or services in relation to crypto-assets are unregulated in the EU.<sup>2</sup> In these cases you will not benefit from the rights and protections available to consumers for regulated financial services, such as complaints or recourse mechanisms;
- **Product complexity:** some products providing exposure to crypto-assets are very complex, sometimes with features that can increase the magnitude of losses in case of adverse price movements. These products, given their complexity, are not suitable for many consumers;
- **Fraud and malicious activities:** numerous fake crypto-assets and scams exist and you should be aware that their sole purpose is to deprive you of your money using different techniques, for example phishing;
- **Market manipulation, lack of price transparency and low liquidity:** how crypto-assets prices are determined and the execution of transactions at exchanges is often not transparent. The holding of certain crypto-assets is also highly concentrated, which may impact prices or liquidity. You may therefore not get a fair price or treatment when buying or selling crypto-assets, or not be able to sell your crypto-assets as quickly as you would want in the absence of a potential buyer. Cases of market manipulation have been reported on multiple occasions; and
- **Hacks, operational risks and security issues:** the distributed ledger technology underpinning crypto-assets can bear specific risks. Several issuers and service providers for crypto-assets, including crypto exchanges and wallet providers, have experienced cyber-attacks and severe operational problems. Many consumers have lost their crypto-assets or suffered losses due to such hacks and disruptions or because they have lost the private keys providing access to their assets.

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<sup>2</sup> Some Member States in the EU have implemented national rules to regulate certain crypto-assets and related products or services. In addition, providers of some types of crypto-asset services, including exchange services and custody services are required to be authorised or registered for the purposes of anti-money laundering and counter-terrorist financing. Please refer to the relevant competent authority for further details.

## Background information

This Warning is based on Article 9(3) of the founding Regulations of the ESAs.<sup>3</sup> It follows earlier warnings about the risks of buying/holding crypto-assets.<sup>4,5, 6</sup>

Crypto-assets can be defined as a digital representation of value or rights which may be transferred and stored electronically, using distributed ledger technology or similar technology.

The ESAs note growing consumer activity and interest in crypto-assets, including so-called virtual currencies and the emergence of new types of crypto-assets and related products and services, for instance so-called non-fungible tokens (NFTs), derivatives with crypto-assets as underlying, unit-linked life insurance policies with crypto assets as underlying and decentralised finance (DeFi) applications, that claim to generate high and/or fast returns. The ESAs are concerned that an increasing number of consumers are buying those assets with the expectation that they will earn a good return without realising the high risks involved.

In September 2020, the European Commission presented a legislative proposal for a regulation on markets in crypto-assets.<sup>7</sup> The proposal provides a comprehensive framework for the regulation and supervision of issuers and providers of services for crypto-assets with a view to protect consumers and the integrity and stability of the financial system. Consumers are however reminded that the proposal remains subject to the outcome of the co-legislative process.<sup>8</sup> Consumers will not currently benefit from any of the safeguards foreseen in that proposal until it is adopted and applies.

As at the date of this warning, there are more than 17,000 different crypto-assets, some of them being sometimes referred to as so-called 'virtual currencies' or digital 'coins' or 'tokens'.<sup>9</sup> The most prominent crypto-assets to-date include bitcoin and ether, which together represent about 60% of the total market capitalisation of crypto-assets. The energy consumption of some crypto-assets is high, e.g., from mining and validation processes, and consumers should be aware of their environmental impact.<sup>10</sup>

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<sup>3</sup> Regulation (EU) 2019/2175 of the European Parliament and of the Council of 18 December 2019 amending Regulation (EU) 1093/2010 establishing a European Supervisory Authority (European Banking Authority), OJ L 331, 15.12.2010, p. 12; Regulation (EU) 1094/2010 establishing a European Supervisory Authority (European Insurance and Occupational Pensions Authority), OJ L 331, 15.12.2010, p. 48; Regulation (EU) 1095/2010 establishing a European Supervisory Authority (European Securities and Markets Authority), OJ L 331, 15.12.2010, p. 84.

<sup>4</sup> EBA (2013), [Warning to consumers on virtual currencies](#), 12 December

<sup>5</sup> ESAs (2018), [ESAs warn consumers of risks in buying virtual currencies](#), 12 February

<sup>6</sup> ESMA (2021), [ESMA sees high risks for investors in non-regulated crypto-assets](#), 17 March.

<sup>7</sup> Proposal for a regulation of the European Parliament and of the Council on Markets in Crypto-assets, and amending Directive (EU) 2019/1937, COM/2020/593, 24/09/2020.

<sup>8</sup> [The ordinary legislative procedure - Consilium \(europa.eu\)](#)

<sup>9</sup> Source: Coinmarketcap.com, data as of 3 March 2022

<sup>10</sup> For further details, see for example Cambridge Centre for Alternative Finance (2022), '[Cambridge Bitcoin Electricity Consumption Index](#)'