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Bitcoin is ripe for fraud and Ponzi schemes, warns SEC

Government agency cautions about the use of cryptocurrencies, saying they're more likely to be used by "fraudsters to perpetrate fraudulent investment schemes."

by Dara Kerr @darakerr / May 7, 2014 8:38 PM PDT

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Bitcoin

The US Securities and Exchange Commission issued an advisory Wednesday that warned investors to be wary of Bitcoin or other virtual-currency related investments.

While not advising investors to avoid Bitcoin altogether, the financial regulator did caution investors by saying the cryptocurrency is uninsured, unregulated, and volatile. But the SEC's chief concern was the risk of fraud.

"A new product, technology, or innovation – such as Bitcoin – has the potential to give rise to both frauds and high-risk investment opportunities," the agency's notice says. "Potential investors can be easily enticed with the promise of high returns in a new investment space and also may be less skeptical when assessing something novel, new and cutting-edge."

The government agency also pointed to another investor alert (PDF) it issued, which outlines the risks of Bitcoin in the context of Ponzi schemes. The SEC said that Ponzi scheme organizers often use the newest tech innovations for their scams.

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"Innovations and new technologies are often used by fraudsters to perpetrate fraudulent investment schemes," the agency said.

Additionally, the SEC said that investors who were able to cash in when the Bitcoin market was soaring are now more susceptible to being taking advantage of because of their unexpected increase in wealth. They are "attractive targets for fraudsters" and "promoters of high-risk investment opportunities," the SEC said.

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It's been a wild ride for Bitcoin over the past couple of years.

The virtual currency has become more accepted and grown exponentially – it went from \$2 per coin in 2011 to roughly \$1,000 per coin last fall. What's more, cryptocurrency ATMs have begun to pop up, some casinos have said they'd accept digital currency payments, Yelp started listing businesses that accept Bitcoin, and even eBay has begun allowing for limited sales of bitcoins on its US and UK sites.

Yet, the virtual currency has hit some rough patches. Besides coming up against hurdles from US, Japanese, and other regulators, the prominent Tokyo-based Bitcoin exchange Mt. Gox filed for bankruptcy earlier this year. The demise of the exchange came because hackers stole nearly \$500 million in

bitcoins through a weakness in the company's system. Bitcoin bank Flexcoin also had to shut down after being hacked.

Despite the SEC's concerns, the digital currency still has backing from several US government officials. US Rep. Jared Polis (D-Colo.) has publicly said that dollar bills are as equally vulnerable to instability, illicit activity, and forgery as Bitcoin. The congressman has also noted that dollars have been used extensively in drug trafficking and money laundering, not to mention tax fraud.

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