Digital assets risk disclosure

This risk disclosure on digital assets (hereinafter "Risk Disclosure") provides a general overview of certain risk factors (hereinafter the "Risk Factors") associated with digital assets, as defined in the "Digital assets" fact sheet, in connection with the services provided by Zuger Kantonalbank (hereinafter the "Bank") to the client (hereinafter the "Client"). The risks may entail the complete loss or a reduction in the value of the digital assets.

1. Introduction

1.1. This Risk Disclosure includes a non-exhaustive, indicative list of possible risks and does in no way disclose or explain all risks in connection with investments in digital assets. This Risk Disclosure supplements the contractual documentation between the Client and the Bank, and shall be read and construed in conjunction with the Basic Client Contract and the General Terms and Conditions. In no way shall this Risk Disclosure serve as a substitute for any kind of professional advice.

1.2. As the Bank does not provide any advice regarding digital assets, the Client and/or any person interested in investing in digital assets is strongly recommended to seek professional advice prior to making any investment decision.

1.3. The Client is advised to consult the risk disclosures issued by all third parties involved, such as the issuers of a digital asset or other third parties involved in the transactions relating to digital assets, as may be contained in particular in

- prospectuses, key information documents or
- fact sheets and white papers relating to a particular digital asset or category of digital asset.

1.4. Furthermore, this Risk Disclosure does not discuss any matters of taxation or other legal matters in any jurisdiction relating to investments in and transactions of digital assets. The Client is advised to obtain appropriate legal and/or tax advice on their own behalf.

1.5. The Client confirms that they have received and acknowledged the brochure "Risks Involved in Trading Financial Instruments" of the Swiss Bankers Association and that they agree with its content.

2. General risks associated with digital assets

2.1. Digital assets may incorporate several financial and non-financial rights, claims and/or assets, including rights and obligations not typically comprised by (traditional) financial market instruments. The Client must ensure they understand the rights and obligations comprised by the digital assets in question prior to any investment decision.

2.2. Where the aim of the Client primarily is to sell the acquired digital assets at a profit and only subsidiarily, if at all, making use of the underlying rights comprised by the digital assets, such underlying rights may be of little or no benefit at all for the Client. This might be the case where digital assets grant their holders the right to request the performance of services (e.g. access to a platform), the right to the supply of goods or where digital assets serve as means of payment. The fair value of digital assets may consequently be extremely difficult to assess and may ultimately prove to be much lower than anticipated.

2.3. The value of digital assets results primarily from the rights incorporated therein. It is at the sole discretion of the Bank and the custodian banks it has appointed to cease or limit the execution of such rights. Consequently, the Client may not be able to exercise such rights and the potential benefits of the digital assets may be limited as long as the Client holds such digital assets. For example, the Client may be unable to seize opportunities, e.g. to repurchase the digital assets and/or pay for products and/or services of the issuer or of third parties.

2.4. The technical functionalities of digital assets (e.g. the ability to transfer them, to create new digital assets, the number of decimals up to which a digital asset may be traded, etc.) depend on the smart contract for the digital asset in question. Smart contracts are based on sophisticated computer codes, and their interaction with the respective distributed ledger network is very complex. Therefore, Clients should ensure they understand the functioning of the relevant smart contract prior to investing in any particular digital asset.

2.5. There is no guarantee for a bug-free execution of smart contracts or the distributed ledger network it operates on. The rules and protocols of a distributed ledger network and/or the digital asset issuer may reserve the right to amend the code of the smart contract at any time, without prior notice and at their sole discretion. Depending on the rights and obligations defined in the smart contract, issuers have considerable discretion to manage their digital assets. For example, issuers may decide to cancel the digital assets and replace them with other forms of evidence such as paper certificates. Such changes to the code of the smart contract are entirely beyond the Bank's control and out of the Bank's sphere of influence. The Bank is not obliged to provide alternative solutions to such changes, e.g. storage services for any digital asset, paper certificates or other products replacing digital assets.

2.6. Digital assets may not be listed on a security exchange and therefore its issuers may not be subject to the rules applicable to listed companies. Consequently, issuers of digital assets are not subject to investor protection rules, such as the duty of transparency and the equal treatment of investors. In particular, issuers may not be required to disclose, provide or publish relevant documentation related to digital assets which may lead to disadvantages for the Client and their digital assets.

2.7 Private keys can be used to manage digital assets, and corresponding controls must be in place. If the private keys are not carefully stored and secured, this could mean that access to and control of the digital assets is restricted or even lost. If this risk materialises, it could entail the complete loss of the digital assets.

3. Technology risks

3.1. The digital ledger technology (hereinafter "DLT") on which the digital assets are based is still at an early stage of development and best practices are still to be determined and implemented. DLT will most likely be subject to significant technological changes and/or innovations in the future. Such technological changes and advances, for example in digital encryption or quantum computing, are entirely beyond the Bank's control and that of the custodian banks it has appointed, may pose a risk to the security of digital assets and, if exploited, lead to theft, loss of units or reduction in value (including reduction to zero) of the Client's digital assets. In addition, alternative technologies to certain digital assets could be established, making them less relevant or even obsolete. Digital assets which are traded on a distributed ledger that becomes less relevant or obsolete could negatively affect the price and the liquidity of the digital assets.

3.2. Due to the particular characteristics of digital assets (e.g. [i] they only exist virtually on a computer network, [ii] transactions on a distributed ledger are mainly done anonymously, [iii] they are irreversible and final, and the ability to modify the history of transactions is computationally negligibly small), they make an attractive target for fraud, theft and cyber-attacks. Various tactics have been developed respectively identified that are designed to steal digital assets or disrupt the underlying DLT. Such attempts can cause loss or at least scepticism about the long-term future of digital assets, prevent the adoption of digital assets, and increase the volatility and illiquidity of the digital assets in question. Furthermore, if the Client initiates or requests a transfer of digital assets using an incorrect digital ledger address, it will be impossible to identify the recipient and reverse the transaction. This risk also applies if the Client attempts to transfer digital assets using an incorrect digital ledger address.

3.3. Due to technical restrictions, it may be possible that fractions or a certain minimum balance of digital assets cannot be transferred to other wallets. This may be applicable for certain protocols of digital assets and is typically related to the "gas price" required to execute a transaction or to technical minimum balance requirements. The Client acknowledges that any potential remaining digital assets will remain with the Bank without any further claims and rights to them.

3.4. Since there is no supervisory body (e.g. a governmental authority or a central bank) overseeing the development of DLT, the functioning of distributed ledgers, as well as further improvements in the way they function (e.g. ability to increase the number of transactions, reduce the processing time or the transaction fees, implement security updates, etc.), relies on the collaboration and consensus of various stakeholders, among others, developers enhancing the open-source software related to cryptocurrencies or miners facilitating the processing of transactions. Any disagreement among stakeholders (e.g. developers and miners) may result in a hard fork. A hard fork is an open-source software upgrade that is not downward compatible. Hard forks or potential hard forks may lead to the instability of the distributed ledger concerned, and may limit the ability to process transactions and lead to an increase in the transaction fees. The Bank excludes any and all liability for losses or damage relating to, arising out of or resulting from a hard fork. The Client hereby agrees to indemnify, defend and hold harmless the Bank and its respective directors, officers and employees, and all successors and assigns of any of the foregoing, from and against any and all claims arising out of or resulting from a hard fork.

3.5. Hard or soft forks on a distributed ledger may lead to the creation of a new or competing kind of digital asset, and may adversely affect the functionality, convertibility or transferability or result in a full or partial loss of units or reduction (including reduction to zero) in the value of the digital assets.

3.6. The Bank is unable to foresee all upcoming hard forks. The Client shall find out about the particularities of and keep up to date with potential upcoming hard forks and their impact on the digital assets. It is at the sole discretion of the bank and its cooperation partner to support one, both or no chain(s) resulting from the hard fork.

3.7. The functioning of digital assets is based on open-source software. Developers of such open-source software are not appointed or controlled by the Bank or the custodian banks it has appointed. Open-source software code is freely accessible and may be copied, used and legally modified at any time. Conversely, developers may cease developing the open-source software at a critical point in time when a security update and/or modification to the software is required. Open-source software is therefore generally exposed to vulnerabilities, programming errors and threats from fraud, theft and cyber-attacks.

3.8. A digital asset may under certain circumstances show characteristics of centrally issued financial instruments, for example in case of a concentration of ownership of issued/pre-mined units with the issuer, or network functions such as node operation or transaction validation with one single party or several parties, irrespective of whether such parties are directly involved or not. This may result in potentially detrimental effects on the Client's digital assets and/or on parties other than those directly impacting such concentration of ownership or network functions.

3.9. In the unlikely event of a significant disruption to a distributed ledger network, the services in connection with such distributed ledger network may be ceased and action may be taken to ensure business continuity.

3.10. The execution of transactions in digital assets on a blockchain or other distributed ledger may be subject to delays, e.g. due to third parties/nodes using evolving technology and other processes for the verification of the transaction. Furthermore, an increasing number of transactions coupled with the inability to implement changes to DLT may result in a slower transaction processing time and/or a substantial increase in the transaction fees paid to miners of cryptocurrencies for facilitating the processing of digital asset transactions. This may limit the ability to process transactions quickly, and consequently cause significant delays, during which the value of the digital asset may fluctuate significantly, or which may otherwise result in loss or damage and/or lead to an increase in the fees and costs.

3.11. Digital assets only exist virtually on a computer network and have no physical equivalent. Determining a value for digital assets is difficult, as the value depends on the expectation and trust that digital assets can be used e.g. for future payment transactions, as a medium of exchange or for other purposes. Persistently high volatility, changes and advances in technology, fraud, theft, cyber-attacks and regulatory changes may prevent the establishment of digital assets as an accepted long-term medium of exchange, potentially rendering digital assets worthless.

4. Legal and regulatory provisions

4.1. The legal and regulatory framework governing digital assets is in formation and constant development in Switzerland, and is imposed globally by various regulatory authorities (e.g. concerning anti-money laundering, securities law taxation, consumer protection or the characterisation of specific digital asset classes). Changes to the legal and regulatory framework and related measures by regulators or other governmental authorities may affect e.g. the transferability or convertibility of the Client's digital assets and potentially result in the illegality of digital assets and in a full or partial loss of or reduction in value (including reduction to zero) thereof.

4.2. The classification of a particular digital asset as a cryptocurrency or another kind of digital asset, such as a security or other financial instrument, remains at the sole and full discretion of the Bank. This classification made by the Bank is valid for the business relationship between the Client and the Bank and may differ from the classification imposed by relevant authorities or other involved and competent third parties in any jurisdiction at any given point in time. This may result in differing rights and obligations of the Client in respect of their digital assets in various jurisdictions over time, e.g. legal and regulatory duties, tax obligations or other requirements, the non-compliance with which may result in measures and sanctions including criminal liability, or which may otherwise affect the legal position of the Client or the value, transferability or convertibility of the relevant digital assets.

4.3. The issuers of digital assets or other involved parties may become subject to regulatory investigations, injunctions or other measures which may impact the transferability or convertibility of the Client's digital assets or may restrict or prohibit the Client from holding or transacting digital assets.

4.4. The legal effectiveness of the underlying rights of digital assets may be subject to differing regulation in the relevant jurisdictions, including in particular the jurisdiction of the issuer and of the Client. The tokenisation of assets or of the anticipated underlying rights and obligations and/or its transfer to the Client may not be legally effective and, consequently, would potentially result in a full or partial loss of units or reduction of value (including reduction to zero) thereof.

5. Digital assets in the event of bankruptcy

5.1. The Client's digital assets held in custody by one of the custodian banks appointed by the Bank must be considered "deposited assets" in accordance with the Swiss Banking Act, in order to segregate the Client's digital assets held in custody by the appointed custodian bank in the event of bankruptcy. The qualification of the Client's digital assets as "deposited assets" and consequently the segregation of the digital assets may have severe consequences for the Client. If the digital assets are not segregated, they will fall into the bankruptcy estate of the appointed custodian bank, where the Bank will be treated as a creditor of the custodian bank and will compete with other creditors. Although the Client or the Bank may in certain cases benefit from the depositor protection scheme under Swiss law, not all (and perhaps none) of the digital assets will be eligible for protection under the depositor protection scheme. Conversely, if the digital assets are segregated they will not fall into the bankruptcy estate of the custodian bank appointed by the Bank and must be returned to the Bank and subsequently the Client under Swiss law. Furthermore, investments in crypto currencies are not considered segregated assets within the meaning of the Collective Investment Schemes Act (CISA).

5.2. In case of a bankruptcy event affecting a custodian bank appointed by the Bank, the corresponding processing of the impacted and segregated digital assets may lead to a delay in the transfer of the Client's digital assets to the respective wallet outside the appointed custodian bank's environment.

5.3. The Bank and the custodian banks it has appointed may involve sub-custodians for the purposes of depositing digital assets. A bankruptcy event of such sub-custodian(s) may also impact the Client's digital assets. The Client is aware that such bankruptcy event of the sub-custodian(s) is subject to the laws and regulations applicable to the sub-custodian (which may not necessarily be Swiss law) and that a change in such laws may lead to a lack of segregation of the digital assets which consequently leads to a significantly more difficult retrieval of the Client's digital assets. In such a case, the Bank (i) shall not be held liable for any losses directly or indirectly caused by the insolvency or bankruptcy event of the respective sub-custodian, and (ii) may assign to the Client for the return of the digital assets (or the reimbursement of their counter value) any claims to the extent such claim exists and can be freely assigned to the Client.

6. Risks related to market volatility

6.1. The value of digital assets may be subject to significant changes, even on an intra-day basis, as the trading thereof is perceived to be highly speculative and its volatility significantly high. Investments in digital assets are susceptible to irrational bubbles or loss of confidence, with the potential to result in a collapse in demand relative to supply, e.g. because of unexpected changes imposed by the software developers, the creation of alternative digital assets, or a deflationary or inflationary spiral. Confidence might also collapse due to technical reasons, e.g. if significant amounts of digital assets are lost or in the event of a successful cyber-attack preventing the settlement of a digital assets transaction.

6.2. The trend in the value of digital assets is unpredictable and may be impacted by several factors, e.g. changes and improvements in technology, fraud, theft, cyber-attacks and regulatory changes, potentially resulting in a full or partial loss of the Client's digital assets. Digital assets, in contrast to traditional financial instruments, lack historical fair values allowing a reliable assessment of volatility.

6.3. The execution and settlement of transactions in digital assets may be dependent on the particularities of the relevant distributed ledger or on the participation of third parties on the relevant network, in particular on the availability of miners or other processing entities. Delays or failures to execute or settle transactions may potentially result in losses or other adverse effects. In addition, trading platforms and systems in digital assets and their participants may be unregulated or subject to limited regulation and may not provide the same or similar safeguards as applicable to traditional financial instruments, e.g. safeguards concerning market manipulation, information asymmetry, transparency or insider trading.

6.4. Since there is no supervisory body (e.g. a governmental authority or a central bank) supervising digital assets, there is no authority or institution which may intervene and stabilise the value of digital assets and/or prevent or mitigate irrational price developments.

6.5. A single distributed ledger may be used as a channel for the execution of digital asset transactions. Consequently, such a channel may be the sole source of liquidity for the trading of digital assets, resulting in a higher illiquidity risk. The market for the relevant digital assets may experience periods of decreased liquidity or even periods of illiquidity. A lower liquidity may result in very rapid and irrational price developments, in wider spreads and/or in higher rejection rates. Insufficient liquidity in the market may lead to the Bank's inability to provide prices for the Client to trade digital assets or execute any transactions. The Client's ability to trade digital assets, to compare the prices of digital assets and/or liquidate their positions may consequently be limited.

6.6. The single distributed ledger used as a channel as described in 6.5 may constitute a trading venue that the appointed custodian bank itself operates. In the event that such a trading venue experiences interruptions or other errors limiting the operation of such venue, and if the appointed custodian bank is otherwise unable to find a suitable solution (another market, trading venue or counterparty to trade digital assets with), the Client may not be able to trade their digital assets for a certain period of time or even permanently.

7. Data protection

7.1. Clients should be aware that any transfer or transaction of digital assets may be recorded on the respective public distributed ledger and may therefore be visible to the public.

7.2. Distributed ledgers on which digital assets are issued and/or recorded are neither the property of the Bank nor the appointed custodian bank, nor does the Bank and/or the appointed custodian bank have any control over such distributed ledgers. The Client acknowledges that the information available on such networks may be exploited or misused by third parties.