

The Switch

Here's how Bitcoin charmed Washington

By **Timothy B. Lee** November 21, 2013

The pair of Bitcoin hearings held this week by Senate committees could have been a disaster for the Bitcoin community. After all, Bitcoin first came to mainstream attention in 2011 when Gawker [reported on Silk Road](#), an anonymous online marketplace that allowed users to purchase a wide variety of illegal drugs with Bitcoin. Sen. Chuck Schumer (D-N.Y.) [denounced the site](#) and suggested that Bitcoin was "an online form of money laundering." A few months ago, it would have been easy to imagine the first congressional hearings on Bitcoin being a prelude to a federal crackdown on the decentralized financial network.

But that's not what happened. Instead, the [hearings were lovefests](#). All three Obama administration officials who testified this week stressed that Bitcoin has legitimate uses and argued that no new regulations were needed to police illicit uses of the network. Most of the other witnesses echoed those sentiments.

That wasn't a coincidence. The cordial atmosphere of this week's hearings was the culmination of months of careful diplomacy by Bitcoin advocates. Since the spring, leaders of the Bitcoin community and sympathetic policy advocates have been engaging with federal regulators, lawmakers and other influential figures inside the beltway. The result: a near-unanimous consensus that the federal government needs to be careful to avoid hampering the growth of the world's first completely decentralized payment network.

A tough crowd

On the morning of June 13, several dozen well-dressed Washingtonians filed into the Carlucci Auditorium at the stately headquarters of the United States Institute of Peace. For many of the government officials in the room, this would be their first opportunity to meet senior figures in the Bitcoin community in the flesh. Panelists included lead Bitcoin developer Gavin Andressen and Patrick Murck, general counsel of the Bitcoin Foundation.

The way the event was framed didn't augur well for Bitcoin. One of the conference's two sponsors (along with Thompson Reuters) was the International Centre for Missing and Exploited Children. A major theme of the second panel was the use of bitcoins to purchase child pornography.

"Child pornography is like Bitcoin in some ways," said Andrew Oosterbaan, who prosecutes child pornography cases for the Justice Department. "It has intrinsic value to people who want it. The more valuable child pornography is the new child pornography. When you add an anonymous currency, you've taken individuals who are already incentivized to produce, given them a far more meaningful incentive to do so."

"Bitcoin is nothing like child pornography," a visibly angry Murck shot back. "If there was one instance of a child being abused because of Bitcoin, that's one too many. I'm a father, I think there's a special place in hell for people who do that."

But Murck also stressed that the Bitcoin community was willing to work with federal regulators to ensure that Bitcoin-based businesses complied with applicable laws. "I want to craft a sane regulatory environment," he said, urging federal regulators to "engage stakeholders. Don't have secret meetings. Have public meetings. We're all happy to live with the consequences of whatever rulemaking is open and transparent."

Murck would get his wish for engagement, though many of the meetings would be held behind closed doors. "We always intended that conference to be a launching point," says Ernie Allen, the president of the International Centre for Missing and Exploited Children and an organizer of the June conference. The gathering catalyzed the creation of a [task force](#) to consider how policymakers should respond to Bitcoin's emergence. It

is expected to issue its recommendations early next year.

Allen says that conversations among members of that task force have changed how he thinks about the online payment network. Allen now believes that premature regulation would be counterproductive.

"We are enthusiastic about the potential of virtual currencies and the digital economy," Allen said in his Monday testimony before the Senate Committee on Homeland Security and Governmental Affairs. Allen said he remained concerned about the use of the currency for exchanging child pornography, but he warned that "draconian" regulations could push Bitcoin enterprises underground and overseas, where it would be much harder to police for illicit uses.

The Senate studies Bitcoin

Staff on the Homeland Security Committee, which is chaired by Sen. Tom Carper (D-Del.), had been preparing for their Bitcoin hearing for several months. Committee staffers began to study the topic in earnest in April, when the value of one bitcoin spiked to \$266, generating a wave of media attention.

Over the summer, committee staff interviewed around 50 experts in industry, government, academic and nonprofit organizations to learn how the Bitcoin network worked and how it might affect the economy and law enforcement. Committee staffers talked to government agencies, bankers, and technologists. They also talked extensively to representatives of the Bitcoin Foundation.

The committee consulted with Dan Kaminsky, a well-known security expert who conducted an influential security analysis of the Bitcoin software in 2011. Staffers talked to Sarah Meiklejohn, a computer scientist at the University of California, San Diego, about whether Bitcoin is truly anonymous (it isn't). And they talked to Jerry Brito, a researcher at the Mercatus Center, a libertarian think tank. Brito testified at Monday's hearing.

In August, the committee sent a series of letters to federal agencies seeking their views on Bitcoin and other virtual currencies. Letters were sent to the Department of Homeland Security, the Treasury Department, the Federal Reserve, the Justice Department and other agencies with regulatory authority related to financial markets or online crime. The letters asked the agencies to provide details of any inquiries they had conducted into the virtual currencies, and to describe whether they had plans to regulate the currency in the future.

Meanwhile, representatives from the Bitcoin Foundation met with a number of executive branch officials at a closed-door meeting in August. "What the Bitcoin Foundation tried to stress is that Bitcoin is less useful for [illicit] purposes than other centralized virtual currencies," said Brito, who attended the meeting. Bitcoin advocates also stressed that excessive regulation in the United States would merely push more of the Bitcoin economy overseas, where U.S. regulators might not be able to reach it at all.

Those arguments seem to have made an impression, because government officials repeated many of them at this week's hearings. The Homeland Security Committee invited representatives of three federal agencies to testify before the committee this week. Jennifer Shasky Calvery represented the Financial Crimes Enforcement Network, which enforces the nation's laws against money laundering. Mythili Raman spoke on behalf of the Justice Department, whose enforcement activities have included the shuttering the Bitcoin-based drug marketplace Silk Road. And Edward Lowery spoke for the Secret Service, which (along with the Justice Department) was involved in shutting down e-Gold and Liberty Reserve, two virtual currencies that the government alleged had become vast money-laundering operations. Calvery also testified before the Senate Banking committee on Tuesday.

"Virtual currencies have yet to overtake more traditional methods to move funds internationally" for "criminal purposes," Calvery said. She pointed out that the Bitcoin network has processed only about \$8 billion worth of transactions over the last year, compared to an estimated \$1.6 trillion in "global criminal proceeds" in 2009. Clearly, the vast majority of those transactions are using some other financial network.

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"We are attuned to the criminal use" of Bitcoin, Raman said. But "there are many legitimate uses. These virtual currencies are not in and of themselves illegal."

Calvery agreed. "Innovation is a very important part of our economy," she said, cautioning that premature regulation could stifle Bitcoin innovation.

The personal touch

Regulators are busy people. They're more likely to pay attention to flesh-and-blood advocates than to anonymous Internet commenters. Murck and Andresen's trip to Washington proved to be crucial to building productive relationships with policymakers.

Calvery was a keynote speaker at the June conference. Murck and Calvery met in the speakers' room at the conference and had a conversation that would later lead to the closed-door August meeting between regulators and Bitcoin advocates. The day after the June conference, Murck was introduced to staffers on the Senate Homeland Security Committee, beginning a conversation that culminated in this week's hearings.

Murck says that not everyone in the Bitcoin community was happy about his engagement with Washington. The Bitcoin community has a strong libertarian streak, and many Bitcoin devotees worried that conversations with federal regulators could help to legitimize and encourage regulation.

But to the surprise of many, the Bitcoin advocates' charm offensive actually changed the minds of many D.C. insiders. Winning over Allen was a particular coup for the Bitcoin community. Allen's warnings against the dangers of premature regulation were particularly effective coming from a long-time activist against child pornography.

"Part of the effort was not just to address these issues from a law enforcement perspective, but to listen to the leaders of the Bitcoin movement," Allen said. And when he listened to them, he found some of their arguments to be surprisingly persuasive.

Disclosure: In 2012, while I was working as a freelance writer, the Mercatus Center paid me to contribute a chapter to a [book](#) on copyright policy that was edited by Jerry Brito. Details are available on my [disclosure page](#).