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The Other Side of the Coin: The FEC's Move to Approve Cryptocurrency's Use and Deny Its Viability

Juliya Ziskina

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THE OTHER SIDE OF THE COIN: THE FEC’S MOVE TO
APPROVE CRYPTOCURRENCY’S USE AND
DENY ITS VIABILITY

Juliya Ziskina^{*}
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ABSTRACT

This Article examines the implications of the Federal Election Committee’s May 2014 advisory opinion on cryptocurrency’s viability within campaign finance regulation, and U.S. financial regulation more generally. Although the Commissioners sharply disagreed on whether Bitcoin is a cash or in-kind contribution, they voted unanimously to allow political committees to accept Bitcoin donations. Moreover, all the Commissioners agreed that Bitcoin donors must disclose their names, addresses, and occupations. While many view this decision as pushing Bitcoin and cryptocurrency further toward legitimacy, in actuality it undermines one of cryptocurrency’s distinct functionalities: pseudonymity. Paradoxically, while it approves the use of Bitcoin in campaign finance, the FEC ruling impairs cryptocurrency’s future within financial regulatory schemes.

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^{*} Juliya Ziskina, University of Washington School of Law, Class of 2016. Thank you to Tech Policy Lab Program Director Emily McReynolds and Professor Ryan Calo for their guidance and advice.

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INTRODUCTION

Cryptocurrency, particularly Bitcoin, has recently attracted significant media and regulatory attention. Cryptocurrencies rely on peer-to-peer networking, which limits the need for a central, controlling authority. An entire network of Bitcoin users authenticates transactions, rather than needing a government or bank to control the flow of this form of currency. This reduces the need for interaction with financial institutions. Cryptocurrencies appeal to those who would like to remain anonymous, as payments can be made without the exchange of any personal information.¹ It

¹ In a paper that established the fundamental concepts Bitcoin is built on, Satoshi Nakamoto, the “creator” of Bitcoin, recommended that Bitcoin users use a new address for each transaction to avoid the transactions being linked to a common owner. Satoshi Nakamoto, *Bitcoin: A Peer-to-Peer Electronic Cash System*, BITCOIN.ORG 1, 6, <http://Bitcoin.org/Bitcoin.pdf> (last visited June 13, 2015). Additionally, many Bitcoin users advocate for ways to increase anonymity. See *Anonymity*, BITCOIN SIMPLIFIED, <http://bitcoinsimplified.org/>

is important to note, however, that Bitcoin is not truly anonymous.² Although using Bitcoins does not necessarily require revealing any identifying information, all Bitcoin transactions are traced on the blockchain (a public ledger of all Bitcoin transactions).³ Researchers have highlighted methods to de-anonymize Bitcoin transactions.⁴ Accordingly, Bitcoin's algorithm is more accurately described as pseudonymous, although methods exist to increase (or even ensure) its anonymity.⁵

Since cryptocurrency first appeared in the marketplace in the 1990s, those responsible for monetary policy, payment systems operators, businesses, and consumers have grappled with understanding how cryptocurrency works. More challenging still is deciding the manner and the extent to which cryptocurrency should be regulated, particularly in an area where the role of money is already contentious: campaign finance.

The Federal Election Commission (FEC) approved Bitcoin contributions in a unanimous advisory opinion on May 8, 2014, but the opinion is only in response to a narrow question and arguably raises more questions than it answers.⁶ Additionally, soon after releasing the decision, the agency's six Commissioners offered divergent views on whether Bitcoin contributions must be capped at \$100 per election per donor, or whether candidates, political action committees, and parties may accept the currency in larger amounts.⁷

learn-more/anonymity (last visited May 2, 2015).

² Fergal Reid & Martin Harrigan, Ch. 1: An Analysis of Anonymity in the Bitcoin System 26 (May 7, 2012) (unpublished manuscript), *available at* <http://arxiv.org/pdf/1107.4524v2.pdf>.

³ *Id.*

⁴ See Alex Biryukov, Dmitry Khovratovich & Ivan Pustogarov, *Deanonymisation of Clients in Bitcoin P2P Network*, in CONFERENCE ON COMPUTER AND COMMUNICATIONS SECURITY (Nov. 2014), *available at* <http://hdl.handle.net/10993/18679>.

⁵ BITCOIN SIMPLIFIED, *supra* note 1.

⁶ FED. ELECTION COMM'N, ADVISORY OPINION 2014-02 (May 8, 2014), *available at* <http://saos.fec.gov/aodocs/2014-02.pdf> [hereinafter FEC ADVISORY OPINION].

⁷ This ambiguity hinges on whether the FEC defines Bitcoin donations as cash or in-kind contributions, a point on which the Commissioners offered conflicting statements after their unanimous vote. See Statement of Vice Chair

This Article first notes that the regulatory status of cryptocurrency does not hinge on the FEC's divergence, but rather on its agreement. All six Commissioners agreed that Bitcoin donors are subject to existing (if not more stringent)⁸ disclosure laws: they are required to provide names, addresses, and employment information with every donation. However, this requirement is at odds with one of the central ideas behind Bitcoin: pseudonymity.⁹ Coupled with previous U.S. regulatory pronouncements,¹⁰ the FEC opinion detracts from Bitcoin's viability within U.S. campaign finance regulations that prioritize disclosure and transparency.¹¹ Moreover, the FEC decision has far-reaching implications for not only Bitcoin, but also cryptocurrency in general. Bitcoin is currently the most widely used cryptocurrency, but the regulatory guidance can be extrapolated to apply to other current and future decentralized, pseudonymous, or anonymous virtual currencies.

Part I of this Article explains the background and technical details of cryptocurrency, with an emphasis on Bitcoin. It discusses the advantages and drawbacks, addressing its unique regulatory

Ann M. Ravel, Commissioner Steven T. Walther & Commissioner Ellen M. Weintraub, *Advisory Opinion 2014-02 (Make Your Laws, PAC, Inc.)*, FEDERAL ELECTION COMMISSION (May 8, 2014), <http://saos.fec.gov/aodocs/1256453.pdf> [hereinafter *Statement of Democratic Commissioners*]; Lee E. Goodman, *Statement of Chairman Lee E. Goodman on Advisory Opinion 2014-02 (Make Your Laws PAC)*, FEDERAL ELECTION COMMISSION (May 8, 2014), <http://saos.fec.gov/aodocs/1256452.pdf> [hereinafter *Statement of Chairman Goodman*].

⁸ *Id.* The advisory opinion also requires Bitcoin donors to verify that they are not foreign nationals.

⁹ As all transactions in the network are stored publicly in the blockchain, allowing anyone to inspect and analyze them, the system does not provide real anonymity but pseudonymity. See Malte Möser, Rainer Böhme & Dominic Breuker, *An Inquiry into Money Laundering Tools in the Bitcoin Ecosystem*, APWG eCRIME RESEARCHERS SUMMIT (2013).

¹⁰ See, e.g., I.R.S. Notice 14-21, 2014-16 I.R.B. 938, available at <http://www.irs.gov/pub/irs-drop/n-14-21.pdf>.

¹¹ CLYDE WILCOX, TRANSPARENCY AND DISCLOSURE IN POLITICAL FINANCE: LESSONS FROM THE UNITED STATES (June 2001) ("All sides of the campaign finance debate accept the disclosure requirement, and it is almost an article of faith in the U.S. that disclosure leads to a less corrupt campaign system.").

challenges in regards to campaign finance. Part II then discusses cryptocurrency in light of campaign finance by introducing the FEC's May 8, 2014 advisory opinion. Finally, Part III explores the implications of the advisory opinion and the Commissioners' public comments. This Article ultimately argues that the nature of cryptocurrency may not be reconcilable with the objective of transparency in campaign finance.

I. CURRENCY

A. Traditional Currency

Currency is broadly defined as “[t]okens used as money in a country.”¹² The Financial Crimes Enforcement Network (FinCEN) defines currency as “the coin and paper money of the United States or of any other country that [i] is designated as legal tender and that [ii] circulates and [iii] is customarily used and accepted as a medium of exchange in the country of issuance.”¹³ FinCEN terms these currencies as “real currencies.”¹⁴ In addition to these characteristics, relatively stable currency values are achieved by public trust in the continued rational government manipulation of the money supply,¹⁵ which are features that virtual currencies may lack.

B. Virtual Currency

Unlike real currencies, virtual currencies are online payment systems that may function as “real” currencies but are not issued or

¹² *Currency*, BUSINESSDICTIONARY.COM, <http://businessdictionary.com/definition/currency.html> (last visited May 2, 2015).

¹³ *Application of FinCEN's Regulations to Persons Administering, Exchanging, or Using Virtual Currencies*, DEP'T OF THE TREASURY FIN. CRIMES ENFORCEMENT NETWORK 1 (Mar. 18, 2013) (quoting 31 C.F.R. § 1010.100(m)), available at http://fincen.gov/statutes_regs/guidance/pdf/FIN-2013-G001.pdf [hereinafter *FinCEN Application*].

¹⁴ *Id.*

¹⁵ See Irena Asmundson & Ceyda Oner, *Back to Basics: What Is Money?*, INT'L MONETARY FUND (Sept. 2012), <http://www.imf.org/external/pubs/ft/fandd/2012/09/basics.htm>.

backed by a central government. Therefore, they do not have legal tender status in any jurisdiction,¹⁶ which means that they are not required to be accepted as forms of payment. According to the Government Accountability Office (GAO), “[a] virtual currency is, generally, a digital unit of exchange that is not backed by a government-issued legal tender. Virtual currencies can be used entirely within a [video game world], or can be used in lieu of a government-issued currency to purchase goods and services in the real economy.”¹⁷ In simplified terms, a virtual currency is one that is not administered or issued by a sovereign. For instance, the popular video game World of Warcraft has its own internal virtual currency that is separate from traditional, “real” currency.¹⁸

C. Cryptocurrency

Unlike virtual currencies that are associated with video game worlds, cryptocurrencies “function as a unique currency with [their] own free-floating exchange.”¹⁹ They are digital or virtual currencies that use cryptography for security and are difficult to counterfeit because of this security feature.²⁰ David Chaum, a computer scientist, started one of the first cryptocurrencies, known as DigiCash, in the early 1990s.²¹ He “obtained . . . digital currency patents in the 1980s related to ensuring anonymity using cryptography.”²² Although DigiCash ultimately failed,²³ the idea of

¹⁶ U.S. GOV’T ACCOUNTABILITY OFFICE, GAO-13-516, VIRTUAL ECONOMIES AND CURRENCIES: ADDITIONAL IRS GUIDANCE COULD REDUCE TAX COMPLIANCE RISKS 3 (2013), available at <http://www.gao.gov/assets/660/654620.pdf>.

¹⁷ *Id.*

¹⁸ *Currency*, WOWWIKI, <http://www.wowwiki.com/Currency> (last visited May 2, 2015).

¹⁹ David D. Stewart & Stephanie Soong Johnston, *Virtual Currency: A New Worry for Tax Administrators?*, 68 TAX NOTES INT’L 423, 423 (2012).

²⁰ *Definition of “Cryptocurrency”*, INVESTOPEDIA.COM, <http://www.investopedia.com/terms/c/cryptocurrency.asp> (last visited May 2, 2015).

²¹ David Chaum, *Blind Signatures for Untraceable Payments*, in ADVANCES IN CRYPTOLOGY: PROCEEDINGS OF CRYPTO 82 (1982).

²² *Id.*

²³ Jens-Ingo Brodesser, *FM Interviews: David Chaum*, FIRST MONDAY (July 1999), <http://firstmonday.org/ojs/index.php/fm/article/view/683/593>.

an anonymous (or pseudonymous) and cryptographic currency developed over the course of the 1990s. The idea flourished through a Cypherpunk electronic mailing list²⁴ that included individuals who “advocated the use of cryptography . . . for the protection of private individuals, against each other and against the government.”²⁵ The group’s members included prominent newsmakers, such as Wikileaks founder Julian Assange²⁶ and a co-founder of the Electronic Frontier Foundation (EFF), John Gilmore.²⁷ The list had a pronounced libertarian streak, opposing most regulation, advocating for privacy, and seeking to use cryptocurrencies to achieve these ends.²⁸ In line with their cypherpunk founders’ views, cryptocurrencies have the potential to challenge government supervision of monetary policy by the disruption of current payment systems and the avoidance of existing regulatory schemes.

At least a dozen cryptocurrencies in addition to Bitcoin currently exist. They include: (1) Litecoin, considered the “most valuable cryptocurrency after Bitcoin;” (2) PPCoin; (3) Dogecoin; (4) Freicoin; (5) Namecoin; (6) Terracoin; (7) Ripple; and (8) Feathercoin; among others.²⁹ Numerous other virtual currencies have failed, including Solidcoin, BBQcoin, Fairbrix, and Geist

²⁴ See CYPHERPUNKS, <http://www.cypherpunks.to> (last visited May 2, 2015) (“[C]ypherpunks.to is a center for research and development of cypherpunk projects such as remailers, anonymous peer-to-peer services, secure network tunnels, mobile voice encryption, untraceable electronic cash, and secure operating environments, etc.”).

²⁵ Sarah Jeong, *The Bitcoin Protocol as Law, and the Politics of a Stateless Currency* 9 (Harvard Law Sch., Working Paper, May 8, 2013), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2294124.

²⁶ JULIAN ASSANGE, CYPHERPUNKS 2012 (Julian Assange is known for his whistleblowing activities as the founder of Wikileaks); see also *Cypherpunks, Bitcoin & the Myth of Satoshi Nakamoto*, CYBER SALON (Sept. 5, 2013), <http://www.cybersalon.org/cypherpunk>.

²⁷ CYBER SALON, *supra* note 26.

²⁸ Reuben Grinberg, *Bitcoin: An Innovative Alternative Digital Currency*, 4 HASTINGS SCI. & TECH. L.J. 159, 162 (2012).

²⁹ Andrew R. Johnson, *From Bitcoin to Amazon Coins: A Guide to Virtual Currencies*, WALL ST. J. (May 31, 2013, 6:04 PM), <http://blogs.wsj.com/moneybeat/2013/05/from-bitcoin-to-amazon-coins-a-guide-to-virtual-currencies>.

Geld.³⁰ However, this Article has a focus on Bitcoin because Bitcoins currently represent the “world’s most widely used alternative currency”³¹ and are the subject of U.S. government regulatory discussions.³²

D. Bitcoin

Global, digital, and decentralized, Bitcoin is the currency of the Internet.³³ It is a digital currency system created to facilitate Internet commerce by using digital signatures and peer-to-peer technology to curtail the system’s need for trusted third parties, such as financial intermediaries and central banks.³⁴ No government, corporation, or commodity (such as gold) backs this system of currency. In this way, “currency . . . is exactly like religion. It’s based entirely on faith.”³⁵ Bitcoin is no exception.

The model proposed by Bitcoin is in many ways a response to some of the privacy and autonomy concerns surrounding our current financial system. Current money systems now increasingly come with monitoring of financial transactions which blocks financial anonymity.³⁶ Moreover, during the 2008 financial crisis, public confidence in financial institutions plummeted, and many

³⁰ Ian Steadman, *Wary of Bitcoin? A Guide to Some Other Cryptocurrencies*, ARS TECHNICA (May 11, 2013, 6:51 AM), <http://arstechnica.com/business/2013/05/wary-of-bitcoin-a-guide-to-some-other-cryptocurrencies>.

³¹ See, e.g., *In Brief*, COINBASE, <http://www.coinbase.com/about> (last visited May 2, 2015) (“Bitcoin is the world’s most widely used alternative currency with a total market cap of approximately \$5.3 billion. The bitcoin network is made up of thousands of computers run by individuals all over the world.”).

³² See, e.g., I.R.S. Notice 14-21, 2014-16 I.R.B. 938, available at <http://www.irs.gov/pub/irs-drop/n-14-21.pdf>.

³³ Christie Barakat, *Bitcoin: Currency or Commodity?*, ADWEEK.COM (Nov. 29, 2013, 3:57 PM), <http://www.adweek.com/socialtimes/bitcoin-currency-commodity/139043> (quoting the Reddit.com Bitcoin forum, r/Bitcoin, <http://www.reddit.com/r/bitcoin>).

³⁴ Nakamoto, *supra* note 1, at 1.

³⁵ Matthew Yeomans, *The Quest for a Global E-Currency*, CNN.COM (Sept. 28, 1999), <http://www.cnn.com/tech/computing/9909/28/global.e.currency.idg/index.html> (quoting Jack Weatherford, author of *The History of Money*).

³⁶ See Wilcox, *supra* note 11, at 2.

worried about a global financial failure. These turbulent circumstances led many people to fear the failure of government-controlled currencies and seek an alternative.³⁷

In 2009, the enigmatic Satoshi Nakamoto³⁸ effectuated the idea of a pseudonymous currency and developed Bitcoin, the world's first decentralized digital currency. Unlike fiat currencies, whose value is derived through regulation or law and underwritten by the state, Bitcoins have no intrinsic value and their only real value is based on supply and demand—what people are willing to trade for them.³⁹

1. How Cryptocurrency Works: The Bitcoin Example

Bitcoins are electronic files, similar to an mp3 or text file that can also be lost or destroyed.⁴⁰ They are stored either on a personal computer, or can be entrusted to an online service.⁴¹ Since the files are easily stored, they can also be easily sent.⁴² In order to send and accept Bitcoins, all transactions must be logged on a type of

³⁷ For instance, when Cyprus decided to confiscate money from citizens' deposit accounts to battle its growing debt, many turned to Bitcoin. The value of Bitcoin doubled around this time. See Paddy Hirsch, *What Just Happened in Cyprus? An Explainer*, MARKETPLACE (Mar. 25, 2013, 10:40 AM), <http://www.marketplace.org/topics/world/whiteboard/what-just-happened-cyprus-explainer>.

³⁸ "Satoshi Nakamoto" is most likely a pseudonym since his or her identity is unknown. Adrienne Jeffries, *Four Years and \$100 Million Later, Bitcoin's Mysterious Creator Remains Anonymous*, THE VERGE (May 6, 2013, 11:12 AM), <http://www.theverge.com/2013/5/6/4295028/report-satoshi-nakamoto>. Some have suggested that Nakamoto may not be a single person but instead a group of people. See also Benjamin Wallace, *The Rise and Fall of Bitcoin*, WIRED (Nov. 23, 2011, 2:52 PM), http://www.wired.com/magazine/2011/11/mf_bitcoin/all/1 (indicating that Nakamoto may be a team at Google or the National Security Agency).

³⁹ *Myths*, BITCOIN WIKI, <https://en.Bitcoin.it/wiki/Myths> (last visited May 2, 2015).

⁴⁰ Ogashi Tukafoto, *Bitcoin Mining for Fun and Net Loss*, SLACKATORY (Aug. 4, 2011, 10:00 AM), <http://slackatory.com/2011/08/Bitcoin-mining-fun-loss>.

⁴¹ *Id.*

⁴² *Id.*

public ledger.⁴³ This public ledger is a decentralized network operated and maintained by thousands of personal computers—similar to a peer-to-peer music-sharing service—rather than a central location.⁴⁴ Once another user on the network clears the transaction, the transaction is complete and the Bitcoins are transferred between users.⁴⁵

To secure transactions, Bitcoin relies on public key encryption, a system that uses digital keys to send and receive information.⁴⁶ It utilizes two keys: a public key known to anyone, and a private key known only to the recipient of the message.⁴⁷ The sender encrypts the document with a symmetric key then encrypts the symmetric key with the public key of the receiving computer.⁴⁸ The receiving computer uses its private key to decode the symmetric key.⁴⁹ It then uses the symmetric key to decode the document.⁵⁰ Together, the system then broadcasts all of the transactions associated with each public key to the whole Bitcoin community.⁵¹ A timestamp records the exact time of a transaction to prevent double spending.⁵² Through public key encryption, the Bitcoin system is able to maintain a secure payment system without the need for a third party. Accordingly, users are provided with pseudonymous transactions while still receiving public assurance that the transaction network is functioning and secure.

Bitcoins then enter the market through mining, a processor-intensive process that utilizes specific software.⁵³ Because the

⁴³ Barrett Sheridan, *Bitcoins: Currency of the Geeks*, BLOOMBERG BUSINESSWEEK (June 16, 2011, 5:00 PM), http://www.businessweek.com/magazine/content/11_26/b4234041554873.htm.

⁴⁴ *Id.*

⁴⁵ *Id.*

⁴⁶ *Bitcoin Address*, LEARN CRYPTOGRAPHY, <http://learncryptography.com/bitcoin-addresses> (last visited May 2, 2015).

⁴⁷ *Id.*

⁴⁸ *Id.*

⁴⁹ *Id.*

⁵⁰ *Id.*

⁵¹ Nakamoto, *supra* note 1, at 3.

⁵² *Id.*

⁵³ Mining is the process of adding transaction records to Bitcoin's public ledger of past transactions. This ledger of past transactions is called the blockchain, as it is a chain of blocks. The blockchain serves to confirm

process requires significant computing capacity, software users who mine Bitcoins are rewarded with Bitcoins.⁵⁴ However, the Bitcoin system limits the total number of Bitcoins in existence, which allows for Bitcoin mining.⁵⁵ Currently, Bitcoin miners receive twenty-five Bitcoins as a reward for every block⁵⁶ created, but over time this reward will decrease by fifty percent with every 210,000 created.⁵⁷ This gradual decrease in availability systematically limits the supply of Bitcoins; this ensures there will never be more than 21 million Bitcoins in circulation, which should occur around 2025.⁵⁸ As the supply of Bitcoin is automated, there is no room for a central bank to change the money supply.

In addition to using the mining process to obtain new Bitcoins, it is also possible to obtain Bitcoins from online exchanges, which are subject to the same rules as banks and financial institutions in the United States. Similar to traditional monetary exchange services that allow individuals and businesses to exchange one currency for another, there are online exchanges that allow the exchange of Bitcoin for national and transnational currencies (e.g., dollars, pounds, euros).⁵⁹ Bitcoins can also be purchased directly by finding someone who is willing to exchange Bitcoins for cash, usually done face-to-face and facilitated by websites similar to Craigslist.⁶⁰

transactions to the rest of the network as having taken place. *See How Bitcoin Mining Works*, COINDESK, <http://www.coindesk.com/information/how-Bitcoin-mining-works> (last updated Dec. 22, 2014).

⁵⁴ *Id.*

⁵⁵ COINDESK, *supra* note 53.

⁵⁶ A block is a unit of the code that comprises the blockchain. It is the record of transactions that have occurred since the last block was created and a confirmation of previous transactions. Each block links to the block before it, thus creating a full chain back to the original or “genesis” block. *Blocks*, BITCOIN WIKI, <https://en.Bitcoin.it/wiki/Blocks> (last visited May 2, 2015).

⁵⁷ *Id.*; *see also* COINDESK, *supra* note 53.

⁵⁸ *Controlled Supply*, BITCOIN WIKI, https://en.Bitcoin.it/wiki/Controlled_supply (last visited May 2, 2015).

⁵⁹ *Complete List of Bitcoin Exchanges*, PLANET BITCOIN, <http://planetbtc.com/complete-list-of-Bitcoin-exchanges> (last visited May 2, 2015).

⁶⁰ *See, e.g.*, LOCALBITCOINS.COM, <http://www.localbitcoins.com> (last visited May 2, 2015) (Website description states: “Buy and sell Bitcoins near you.”).

Once a person acquires Bitcoins, there are two main ways to store them: in an online wallet, or on a personal computer or removable media (such as a flash drive).⁶¹ An online wallet allows Bitcoin owners to store their Bitcoins in an online account managed by a third party.⁶² Alternatively, users can store them on their own computers, much like a personal digital wallet.⁶³ Either method carries risks; an online wallet may be subject to hacking, and a personal computer could become infected with a virus, suffer physical damage, or be stolen.⁶⁴ Other cryptocurrencies are functionally and analytically similar to Bitcoin in that they rely on cryptography.⁶⁵

2. Uses and Acceptance of Bitcoin and Other Cryptocurrencies

As with traditional currency, Bitcoin, and cryptocurrency in general, can be transferred in exchange for goods or services. In addition to some physical stores, there are hundreds, if not thousands, of online merchants that accept cryptocurrencies for goods like computer software or clothing, as well as services like graphic design, legal, and consulting services.⁶⁶ Moreover, cryptocurrency offers several unique benefits (or, perhaps, risks) distinct from traditional currency.

First, cryptocurrency dramatically reduces transaction fees. Its

⁶¹ See *Ways to Store Bitcoins*, BITCOIN WIKI, https://en.Bitcoin.it/wiki/Ways_to_store_Bitcoins (last visited May 2, 2015).

⁶² *Id.*

⁶³ *Id.*

⁶⁴ *Id.*

⁶⁵ See *generally Virtual Currency Schemes*, EUROPEAN CENTRAL BANK 21 (Oct. 2012), available at <http://www.ecb.europa.eu/pub/pdf/other/virtualcurrencyschemes201210en.pdf>. However, not all virtual currencies rely on cryptography. *Id.* For example, the online roleplaying game Second Life created by Linden Labs allows players to participate in a virtual economy based on Linden Dollars. Whereas Bitcoin lacks a central monetary authority, Second Life maintains control over its currency through a variety of mechanisms. Players who earn a profit selling virtual land and goods to other plays can convert Linden Dollars into real money. *Id.*

⁶⁶ *Real World Shops*, BITCOIN WIKI, https://en.Bitcoin.it/wiki/real_world_shops (last visited May 2, 2015); *Trade*, BITCOIN WIKI, https://en.Bitcoin.it/wiki/Ways_to_store_Bitcoins (last visited Nov. 1, 2014).

efficiency, gained through eliminating intermediaries, and low cost in comparison to legacy payment tools might be tempting for merchants, individuals, and business-to-business billing.⁶⁷ Bitcoin processors, for instance, charge only one percent to process Bitcoin transactions, compared to the two to three percent often paid by merchants for credit card processing.⁶⁸

Second, the unique benefits cryptocurrency offers are alluring to some users. Using the method described above, it is nearly impossible to create, for example, fraudulent Bitcoins.⁶⁹ They can also be carried, stored, and spent across national borders without a tracking or accountability mechanism.⁷⁰ Many are attracted to this global ease of use and transportability, as well as the elimination of potentially nefarious third parties.⁷¹ Simple convenience is also a relevant factor; Bitcoins can be easily transferred to anyone, anywhere in the world.⁷²

⁶⁷ John Heggstuen, *These Are The Five Main Reasons Bitcoin Is Beginning To Flourish As A Payment Technology*, BUSINESS INSIDER (June 2, 2014, 5:05 PM), <http://www.businessinsider.com/five-main-reasons-bitcoin-is-beginning-to-flourish-as-a-payment-technology-2014-5>.

⁶⁸ *Id.*

⁶⁹ See Joshua Davis, *The Crypto-Currency; Bitcoin and its Mysterious Inventor*, NEW YORKER (Oct. 11, 2011), available at <http://www.newyorker.com/magazine/2011/10/10/the-crypto-currency>.

⁷⁰ Heggstuen, *supra* note 67.

⁷¹ *Id.*

⁷² See generally, Press Release, Department of Justice, Acting Assistant Attorney General Mythili Raman Testifies Before the Senate Committee on Homeland Security and Governmental Affairs (Nov. 8, 2013), available at <http://www.justice.gov/criminal/pr/speeches/2013/crm-speech-131118.html>. Unfortunately, Bitcoin's distinctive factors also make cryptocurrency alluring for criminal purposes. As Attorney General Raman explains, "[S]ome criminals have exploited virtual currency systems because of the ability of those systems to conduct transfers quickly, securely, and often with a perceived higher level of anonymity than that afforded by traditional financial services. The irreversibility of many virtual currency transactions additionally appeals to a variety of criminals seeking to engage in illicit activity, as does their ability to send funds cross-border." Virtual currencies, due primarily to their anonymity, have been linked to facilitation of marketplaces for: assassins, attacks on businesses, exploiting children (including pornography), corporate espionage, counterfeit currencies, drugs, fake IDs and passports, high yield investment schemes (Ponzi schemes and other financial frauds), tax evasion, sexual exploitation, stolen credit cards and credit card numbers, and weapons. See also Laurence Trautman,

Finally, and most importantly, the pseudonymity that cryptocurrency offers appeals to many people.⁷³ Because, for instance, Bitcoins are transferred peer-to-peer without an intermediary, transacting in Bitcoins provides users with high levels of privacy because they remain pseudonymous.⁷⁴ The information recorded during a transaction is the digital address of the Bitcoins, not the user's identity or account information.

Over the past three years, Bitcoin has gradually captured the attention of consumers, retailers, and service providers, and it is now effectively functioning as a currency in the real world.⁷⁵ In fact, Bitcoin has been recognized for legal and tax purposes in Germany, making it the first country to take an official stance on the status of the online currency as "private money."⁷⁶ In the United States, a federal judge ruled that for purposes of securities regulation, Bitcoin is indeed "money."⁷⁷

Even so, it is fair to say that cryptocurrency is not going to cause government-backed currencies to become obsolete. But while the system's virtues, such as pseudonymity and lack of bank fees, may not matter much to the general consumer, it is possible to envision its usefulness in a variety of niche markets.⁷⁸ Where pseudonymity or anonymity is valuable and where persistently high inflation is problematic, it is possible that cryptocurrency could in fact flourish.

Virtual Currencies; Bitcoin & What Now After Liberty Reserve, Silk Road, and Mt. Gox?, 20 RICH. J.L. & TECH. 13 (2014).

⁷³ See Wilcox, *supra* note 11, at 2.

⁷⁴ See FAQ – Bitcoin, *What Are the Advantages of Bitcoin?*, BITCOIN PROJECT, <https://Bitcoin.org/en/faq#what-are-the-advantages-of-Bitcoin> (last visited May 2, 2015).

⁷⁵ See, e.g., *The Mysterious World of Bitcoin: Does It Have Staying Power?*, KNOWLEDGE@WHARTON AT WHARTON SCH. U. PA. (Apr. 24, 2013), <http://knowledge.wharton.upenn.edu/article/the-mysterious-world-of-Bitcoin-does-it-have-staying-power>.

⁷⁶ *Germany Recognizes Bitcoin as 'Private Money'*, RT (Aug. 18, 2013, 6:13 PM), <http://rt.com/news/Bitcoin-germany-recognize-currency-641>.

⁷⁷ Sec. and Exch. Comm'n v. Shavers, No. 4:13-CV-416, 2013 WL 4028182, at *2 (E.D. Tex. Aug. 6, 2013) ("Bitcoin is a currency or a form of money . . .").

⁷⁸ See Trautman, *supra* note 72, at 2.

II. CAMPAIGN FINANCE ENTERS THE AGE OF BITCOIN

The FEC is the latest federal regulatory agency that seemingly legitimized the use of cryptocurrency. After several months of debate, the FEC voted 6-0 to approve Advisory Opinion 2014-02 that allows federal political committees to accept Bitcoin contributions.⁷⁹ While the decision is not considered binding, it may be cited as relevant precedent, and it paves the way for the use of Bitcoins by any federal political committee. The FEC's ruling is significant because it weighs in on a number of questions that touch on the nature of Bitcoins and how they should be valued.⁸⁰

A. Summary of the FEC Advisory Opinion

The FEC decision comes in the form of guidance to the Make Your Laws PAC (MYL PAC). A PAC is a political action committee, a type of organization that pools campaign contributions from members and donates those funds to campaigns for or against candidates, ballot initiatives, or legislation. MYL PAC, a non-connected political committee that registered with the Commission in 2012, wished to accept contributions of up to a total of \$100 in Bitcoins for both its contribution and non-contribution accounts. In its advisory request, MYL PAC proposes to accept Bitcoins only through an online form on which the Bitcoin contributor, regardless of the proposed contribution amount, will have to provide his or her name, physical address, occupation, and employer.⁸¹

The FEC agreed that MYL PAC may accept up to \$100 worth of Bitcoins per election, per contributor. To this point, contributors “should value that contribution based on the market value of Bitcoins at the time the contribution is received.”⁸² If Bitcoin soars in value after the \$100 contribution is received, then bully for the

⁷⁹ *Id.*

⁸⁰ The question of how Bitcoins should be characterized—either as monetary or in-kind contributions—could have implications beyond the fairly narrow confines of election law.

⁸¹ FEC Advisory Opinion, *supra* note 6, at 2.

⁸² *Id.* at 6.

committee. Theoretically, \$100 worth of Bitcoins today could steadily appreciate to \$10,000 worth at the year's end.⁸³ A political committee could then find itself with \$10,000 worth of Bitcoins it could use. The FEC notes that "earnings (or losses) realized upon the sale of any Bitcoins . . . must be reported like other investment earnings or losses."⁸⁴

Moreover, the FEC decided that the sale of Bitcoins, and their conversion into dollars before being used, is legal.⁸⁵ Liquidated Bitcoin must be deposited, in dollar form, into a committee's campaign account within ten days of receiving it.⁸⁶ However, the FEC could not reach an agreement on whether political committees may directly purchase goods and services with Bitcoins. Essentially, the FEC is not authorizing committees to make purchases with actual Bitcoin, but it is not prohibiting them from doing so, either. Since the FEC did not rule on whether committees are allowed to directly spend Bitcoin on goods and services, it states in its ruling, "the Commission is not addressing how such purchases might be reported."⁸⁷ The advisory opinion also provides that purchasing goods or services with Bitcoins that a political committee has purchased with campaign cash is "not permissible under Commission regulations."⁸⁸

Most important in this context, Bitcoin contributions and contributors must be disclosed publicly, regardless of whether Bitcoin users want to remain pseudonymous. The FEC held that all contributors must provide their name, physical address, and employer, affirm that he or she owns the contributed Bitcoins, and that he or she is not a foreign national.⁸⁹

⁸³ See THE BITCOIN VOLATILITY INDEX, <https://btcevol.info> (last visited May 2, 2015). This website tracks the volatility of Bitcoin prices in U.S. dollars.

⁸⁴ FEC Advisory Opinion, *supra* note 6, at 8.

⁸⁵ *Id.* at 3.

⁸⁶ *Id.*

⁸⁷ *Id.* at 9.

⁸⁸ *Id.* at 7.

⁸⁹ *Id.* at 5.

B. How Much Bitcoin Can a PAC Actually Accept?

While the FEC's decision does provide some measure of guidance, it leaves open as many questions as it answers about Bitcoin, and cryptocurrency in general.

The question of whether Bitcoin is a monetary (gift of money) or in-kind (gift of goods or services) contribution is important in this context because if Bitcoins are money, then a political committee may only accept Bitcoin contributions up to \$100, according to federal elections law.⁹⁰ If Bitcoins are in-kind contributions, however, an individual could make a Bitcoin contribution valued up to \$2,600 per election to a federal candidate.⁹¹ The FEC's decision does not indicate whether committees may accept Bitcoin up to the federal limit on campaign contributions. It only addresses acceptance of \$100 worth of Bitcoins, largely because MYL PAC only asked to accept \$100 per election per person. As such, the FEC advisory opinion is narrow because it only responds to a specific question. Despite the opinion's limited scope, the Commissioners still contradicted one another's interpretation of it.

1. The Commissioners' Clash over Bitcoin Campaign Contribution Limits

Although the Commission voted unanimously, the Commissioners seem to disagree on what exactly they voted on. Commissioner Ellen Weintraub told the press that MYL PAC's self-imposed Bitcoin contribution limit of \$100 "was really important to us," and "[b]ecause the Commission only approved the acceptance of Bitcoin as specifically described in the request by Make Your Laws PAC, the decision does not permit contributions of more than \$100."⁹² Chairman Lee Goodman,

⁹⁰ Monetary contributions are limited to \$100 by statute and FEC regulation. See 2 U.S.C. 441g; 11 C.F.R. 110.4(c).

⁹¹ See *Candidate Committees*, FEC, <http://www.fec.gov/rad/candidates/FEC-ReportsAnalysisDivision-CandidateCommittees.shtml> (last visited May 2, 2015).

⁹² Matea Gold, *Federal Election Commission Approved Bitcoin Donations*

however, disagreed. He told the press that “the advisory opinion treats Bitcoin donations as in-kind contributions—not official currency—meaning that the only limits that apply are the federal caps on all forms of accepted donations,”⁹³ and “[t]his advisory opinion in no way established the outer limit.”⁹⁴

Later, the two groups of Commissioners issued separate statements. The three Democratic Commissioners explained that the advisory opinion treats Bitcoins like cash, meaning that Bitcoin contributions must be limited to \$100.⁹⁵ Chairman Goodman (Commissioners Hunter and Petersen did not join this statement) explained that the advisory opinion treats Bitcoins as in-kind contributions, which are not subject to the \$100 limit on cash contributions, and may be accepted in amounts up to the regular contribution limits.⁹⁶ The Commissioners’ divergence is particularly confounding in light of the text of the opinion, which refers to Bitcoin as an in-kind contribution for reporting purposes.⁹⁷ The only analogy to cash appears in the Democratic Commissioners’ separate Statement (“[B]itcoins are most like cash contributions . . .”).⁹⁸

to *Political Action Committees*, WASH. POST (May 8, 2014), <http://www.washingtonpost.com/blogs/post-politics/wp/2014/05/08/federal-election-commission-approves-Bitcoin-donations-to-political-committees>.

⁹³ *Id.* See also FEC, *supra* note 91.

⁹⁴ *Id.*

⁹⁵ *Statement of Democratic Commissioners, supra* note 7, at 1.

⁹⁶ *Statement of Chairman Goodman, supra* note 7, at 1.

⁹⁷ See FEC Advisory Opinion, *supra* note 6, at 8 (“Bitcoins share certain characteristics of contributions governed by two different regulatory reporting provisions: 11 C.F.R. § 104.13(a), which addresses the reporting of most *in-kind contributions*, and 11 C.F.R. § 104.13(b), which addresses the specific reporting of *in-kind contributions* that the committee receives to liquidate in a later reporting period. . . . The initial receipt of Bitcoins as contributions, regardless of subsequent disposition, should be reported like *in-kind contributions* described in 11 C.F.R. § 104.13(a) . . .”) (emphasis added).

⁹⁸ *Statement of Democratic Commissioners, supra* note 7, at 1.

III. IMPLICATIONS OF REGULATORY GUIDANCE ON THE FEDERAL STATUS OF CRYPTOCURRENCY

The FEC advisory opinion has significant implications for Bitcoin, and cryptocurrency more generally, outside the realm of campaign financing. First, the decision may not sit squarely with previous regulatory guidance, which damages the overall cohesion of fiscal regulation. Second, the FEC's treatment of Bitcoin further damages the potential for cryptocurrency to be embraced as a legitimate means of transaction in federal campaign finance.

A. The FEC's Advisory Opinion is Inconsistent with Other Federal Cryptocurrency Regulatory Schemes

Whether Bitcoins are characterized as monetary or in-kind contributions has implications beyond the fairly narrow confines of election law. Their characterization may create inconsistency in other regulatory schemes. Specifically, if the FEC does characterize Bitcoins as in-kind contributions analogous to stocks or commodities, this characterization may be inconsistent with the SEC's view of Bitcoin. For example, in *SEC v. Shavers*, the defendants moved to dismiss the complaint, in which the SEC accused Trendon T. Shavers of operating a Bitcoin-based Ponzi scheme, on the grounds that Bitcoins are not true currency and therefore the investments he solicited and accepted were not "investments of money" subject to federal securities regulation.⁹⁹ The SEC and the federal district court disagreed. In denying the motion, the court found that: "It is clear that Bitcoin can be used as money. It can be used to purchase goods or services Bitcoin is a currency or form of money, and investors wishing to invest in [Shavers' company] provided an investment of money."¹⁰⁰

Bitcoin characterized as an in-kind contribution could also create inconsistencies with the FinCEN March 18, 2013 guidance interpreting the status of virtual currency under the Bank Secrecy Act (B.S.A.) and the anti-money laundering (A.M.L.) rules

⁹⁹ Sec. and Exch. Comm'n v. Shavers, Case No. 4:13-CV-416 (E.D. Tex. Aug. 6, 2013).

¹⁰⁰ *Id.*

adopted under the B.S.A.¹⁰¹ FinCEN found that while decentralized virtual currencies lack legal tender status, they have many of the attributes of currency, and accordingly held that decentralized virtual currency should be treated like legal tender for purposes of A.M.L. regulation.¹⁰² That ruling could be clouded if the FEC advisory opinion is to mean that Bitcoins are not “money” as defined under its regulations.

While any individual federal agency’s guidelines are not binding on other federal agencies considering whether and how to regulate Bitcoins, it may certainly be cited as relevant precedent. An argument can be made that treating Bitcoin differently for different purposes makes sense. For instance, Bitcoin may be more like money than a security in the *Shavers* context, but it may be more like money for the concerns of money laundering and illegal activity. There may be policy advantages, but even so, disjointed opinions regarding the nature of Bitcoin create confusion about how cryptocurrency fits within overall fiscal regulation.

B. Cryptocurrency is Difficult to Reconcile with U.S. Financial Policy

At issue here is not what the Commissioners disagreed on, but on what they unequivocally agreed. The split between the Commissioners highlights a fundamental tension between safeguarding against illicit activity and promoting new, but perhaps risky, technology. Given Bitcoin’s pseudonymous nature, the Democratic Commissioners argue that “contributions of Bitcoins are most like cash contributions,” and regulators must impose strict disclosure requirements on cash because it “offers too facile a medium for unethical and illegal activities” due to “[i]ts untraceability and easy transferability.”¹⁰³ Although Chairman Goodman disagreed that Bitcoins are cash, he still noted the importance of committee requests for identifying information and

¹⁰¹ See *FinCEN Application*, *supra* note 13, at 1.

¹⁰² *Id.*

¹⁰³ *Statement of Democratic Commissioners*, *supra* note 7, at 1 (quoting 120 CONG. REC. 7832 (1974) (statement of Rep. Boland)).

that contributors self-identify.¹⁰⁴

The clearest implication of the FEC's guidance is that there will be no less regulation and scrutiny of entities transacting in Bitcoin and other cryptocurrencies. Despite Bitcoin's commitment to pseudonymity, all donors must list their names, addresses, and occupations before they can donate the digital currency to politicians in the United States. The FEC held that current campaign contribution laws apply, in that "the Commission requires committee treasurers to employ best efforts to obtain, maintain, and publicly report the name, address, occupation, and employer of each contributor who gives more than \$200 in a calendar year."¹⁰⁵ The Commissioners' unanimous agreement here indicates that cryptocurrency will likely not see any less stringent monitoring or disclosure regulation.

Despite this, many believe that the FEC cracked open the door of legal legitimacy in the American political system to cryptocurrency by voting unanimously to allow Bitcoin contributions.¹⁰⁶ After all, regardless of whether it is a cash or in-kind contribution, political committees are allowed to accept Bitcoin donations—the FEC agreed on that much.

Ironically, the FEC decision illustrates the exact opposite conclusion—cryptocurrency does not fit with campaign finance law. In its advisory opinion, FEC nullifies the fundamental precept of cryptocurrency: its pseudonymity. There is no central authority that the FEC can work with to discover the person behind a cryptocurrency transaction. Though everyone on the network can see the blockchain, all they see are public keys, which do not give information on the identity of the person behind that public key. This is the very core of cryptocurrency's functionality. While some users can choose to not be pseudonymous by associating personal data with a public key address, pseudonymity is the assumed default.

¹⁰⁴ *Statement of Chairman Goodman, supra* note 7, at 4.

¹⁰⁵ *Id.* (citing 2 U.S.C. § 432(i); 11 C.F.R. § 102.9(d)).

¹⁰⁶ *See, e.g.,* Matthew Heller, *FEC Decision Pushes Bitcoin Further Toward Legitimacy*, MINT PRESS NEWS (May 19, 2014), <http://www.mintpressnews.com/fec-decision-pushes-bitcoin-toward-legitimacy/190961>.

On the other side, financial transparency is one of the crucial tenets of campaign regulatory law.¹⁰⁷ Indeed, as recently as its 2010 decision in *Citizens United v. Federal Election Commission*, the Supreme Court recognized that campaign finance disclosure is a vital measure to “[enable] the electorate to make informed decisions and give proper weight to different speakers and messages.”¹⁰⁸ By its very nature, cryptocurrency shields its users from financial disclosure. While cryptocurrency has other unique draws in addition to pseudonymity—such as decentralization and low transaction costs—the fact remains that a part of its functionality is at odds with governmental and financial transparency.

The FEC decision follows similar consequences stemming from the U.S. Internal Revenue Service (IRS). In March 2014, the IRS stated that it would treat Bitcoin as a property payment for the purposes of taxation.¹⁰⁹ The guidance also indicates that Bitcoin transactions are subject to the same information reporting and withholding requirements as similar transactions in dollars.¹¹⁰ To the extent that Bitcoin’s success partly depends on its pseudonymity and on avoiding the burden of government regulation, this IRS guidance similarly undermines its unique characteristics.

Accordingly, perhaps the crucial takeaway from the FEC guidance lies not in its Commissioners’ dispute over what Bitcoin is, but rather what Bitcoin cannot be in elections: pseudonymous or anonymous. As such, despite its approval of Bitcoin donations, the FEC opinion is another implicit blow against users’ wish to remain unknown. Ultimately, U.S. fiscal regulations indicate that cryptocurrency is difficult to reconcile with the objective of financial disclosure and transparency.

¹⁰⁷ Wilcox, *supra* note 11, at 2. Also, famously, former Supreme Court Justice Louis Brandeis stated: “[S]unlight is . . . the best of disinfectants” for government. Louis D. Brandeis, *What Publicity Can Do*, OTHER PEOPLE’S MONEY AND HOW THE BANKERS USE IT 62 (Nat’l Home Library Found. 1933) (1914)).

¹⁰⁸ *Citizens United v. Fed. Election Comm’n*, 558 U.S. 310, 371 (2010).

¹⁰⁹ I.R.S. Notice 14-21, 2014-16 I.R.B. 938, *available at* <http://www.irs.gov/pub/irs-drop/n-14-21.pdf>.

¹¹⁰ *Id.*

CONCLUSION

While alternate currencies have offered some respite for those who desire some control in their financial medium, alternative currencies have still been controlled by a central authority and have generally been limited to a specific geographic area. Cryptocurrency, however, is a unique confluence of technology and demand, which allows it to function as a global, decentralized, alternative currency. The growing adoption of cryptocurrency indicates that it is here to stay. The pseudonymous and decentralized features that are widely praised in cryptocurrency are also regulators' largest concern with it. While the currency does have legitimate uses, it has gained notoriety from enabling illicit transactions. As a result, governmental agencies are taking note. On the whole, the FEC ruling is both an acknowledgment of cryptocurrency's growing popularity and a move to undermine its unique features.

