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Comment on AOR 2013-15

September 16, 2013

BY HAND DELIVERY

Shawn Woodhead Werth
Office of the Commission Secretary
Federal Election Commission
999 E Street, NW
Washington, DC 20463

Re: Comments on Advisory Opinion Request 2013-15 (Conservative Action Fund)

Dear Secretary Werth:

The Bitcoin Foundation very much appreciates the opportunity to provide these comments on the Conservative Action Fund PAC's ("CAF") Advisory Opinion Request (the "Request") filed with the Federal Election Commission ("FEC" or "the Commission") on August 15, 2013. As detailed below, the Bitcoin Foundation is the primary advocacy voice for the growing community of bitcoin users and developers, and thus hopes that its perspective will be of value to the Commission as it considers the Request.

The Request presents the Commission with two basic questions: (1) whether federal political contributions can be accepted in the form of bitcoins, and (2) if so, if they should be treated as monetary or in-kind contributions under the Commission's regulations. As to the first question, the Bitcoin Foundation agrees with CAF that the Commission should confirm that bitcoins can be used to make contributions. As another federal agency has recognized, bitcoins are a digital currency[1] that act as a substitute for legal tender, and can be used to buy and sell goods and services. While bitcoins may be novel in that they are digital in nature, the issues raised by accepting bitcoin political contributions are fundamentally no different than other forms of contributions that the Commission has previously approved.

[1] Bitcoins are often referred to as "virtual currency." The Bitcoin Foundation prefers the term "digital currency."

As to the second question, the Bitcoin Foundation agrees with CAF that the Commission should refrain from preemptively categorizing contributions made in bitcoins as either monetary or in-kind in nature, and instead should allow the recipient to categorize individual contributions as appropriate under the Commission's rules. The Commission should do so not only because – as CAF points out – bitcoins have aspects of both types of contributions under the Commission's rules, but also for a broader policy reason. Bitcoins, and the network that underlies them, are still very much in their infancy, and users and developers are just beginning to explore the ways in which they can be used. At the same time, various federal regulatory agencies with potential jurisdiction are at the very early stages of considering whether and how to classify and regulate bitcoins.[2] The Commission should avoid any possibility of stifling innovation or prejudicing other agencies by ruling on a point that it does not need to reach.

STATEMENT OF INTEREST

The Bitcoin Foundation is an advocacy-focused association dedicated to serving the business, technology, government relations, and public affairs needs of the Bitcoin community. The Foundation's members include many of the major companies and other entrepreneurs in the Bitcoin industry. The Bitcoin Foundation, a not-for-profit institution, seeks to broaden the use of Bitcoin, protect the integrity of the Bitcoin protocol, and promote its use through technological investment in the Bitcoin infrastructure, public education, and initiatives in law and policy.

BITCOIN BACKGROUND

I. BITCOIN IS A DECENTRALIZED, OPEN-SOURCE, PEER-TO PEER-NETWORK

Bitcoin was invented in 2008 as a peer-to-peer payment system for use in online transactions. Bitcoin is revolutionary in that, unlike any prior payment system, Bitcoin is not administered by any central authority, i.e. there is no middleman between the sender/buyer and the receiver/seller as there is with, say, PayPal or a traditional payment card. (Bitcoin is thus referred to as a "decentralized" digital currency.)

Instead, the Bitcoin transaction network consists of computers around the world running the Bitcoin open-source software containing the network protocol for administering Bitcoin network transactions. That software can be downloaded by any Bitcoin user (or anyone else for that matter), and any computer running the software can join the network. Each computer on the network also maintains a copy of a universal ledger that contains the history of every Bitcoin transaction ever made.

[2] As discussed below, Bitcoin is still very much in its infancy, and has enormous potential to drive innovation in financial and other sectors. The Bitcoin Foundation thus believes that regulators in general must approach the regulation of Bitcoin cautiously so as to avoid stifling its development.

As explained in more detail below, the computers on the Bitcoin network collectively verify every Bitcoin transaction, and ensure that no Bitcoin user can spend value that he or she does not have, or that has already been spent. Once a transaction is verified, it is included in a new "block" of transactions that is permanently added to the ledger collectively maintained by all the computers on the network (which is, for this reason, referred to as the "block chain"). The addition of the new transaction block to the block chain serves to confirm that the included transactions took place and, by virtue of the time-stamp included along with the block, when they took place. Each new block added to the block chain contains all of the verified transactions that took place since the addition of the prior block.

II. How a Bitcoin Transaction Works

Any Bitcoin user can transact directly with any other Bitcoin user. To utilize the Bitcoin network, a user needs a Bitcoin address. While any Bitcoin user can generate an address using the Bitcoin open-source software, in practice, many users have accounts with one or more Bitcoin service providers and store bitcoins at addresses provided through their accounts. A Bitcoin address takes the form of a cryptographic "public key," a string of numbers and letters roughly 33 digits long. Each public key has a matching "private key," known only to the user, and protected by a password or other means of authentication.

To initiate a transaction, the user sends a message to the other computers on the network announcing the transfer of a certain value in bitcoins[3] from the user's public key to the recipient's public key. The sending user's private key is used to "sign" the transactions. The private key is mathematically paired with the public key, and through a standard cryptographic process of the sort used to secure website connections, every computer on the network can verify that the transaction is signed with the correct private key.[4] The private key signature thus serves to confirm that the transaction originated with, and was approved by, the actual owner of the originating public key, and therefore that the transaction is valid. While this process sounds complicated, it is handled automatically and transparently to users through the Bitcoin software. From the user's perspective, sending bitcoins to someone else is no more difficult or arcane than sending funds using PayPal or other traditional payment systems.

[3] As discussed below, a distinction should be made between the network and protocol over which transactions are made on the one hand, and the unit of digital currency that can be sent or received over that network/protocol on the other hand. By the convention adopted here, "Bitcoin," when capitalized, refers to the network/protocol, and lower-cased "bitcoin" refers to the unit of digital currency.

[4] By using the cryptographic process, any computer on the network can compute whether the private key is correct, without ever knowing the private key.

Each active computer on the Bitcoin network receives a copy of the transaction message. This serves to notify every other user on the network that the owner of the receiving public key is the new owner of the bitcoins sent by the sending public key (assuming that the transaction bears the correct private key signature that proves that it is genuine). At this point, the transaction has been completed and is irreversible.[5]

It is not, however, accepted as a verified transaction until it is included in a block of transactions added to the block chain. Like the verification of private keys, the process of grouping transactions into blocks involves a cryptographic process that serves to confirm the validity of the block. Once a block is created, it is broadcast to the network, and the other computers on the network can confirm the so-called "proof of work" required to create the block. Only at that point is the block added to the block chain. Each new block added to the block chain contains a "hash"—a unique identifier—of the previous block that links the blocks and serves to confirm the previous block. Since no central authority controls the Bitcoin network, a consensus process is used to ensure that a common, current block chain always exists that constitutes a universally accepted record of all Bitcoin network transactions. Each computer on the network continuously updates its copy of the block chain to keep it current.

The process of finding the proof of work necessary to create transaction blocks is, by design, computationally very intensive, and requires considerable computing power so as to ensure that only valid blocks are added to the network. In order to incentivize users to expend the necessary computing power, each new block added to the block chain contains a transaction that rewards its creator with new bitcoins. The process of verifying transactions is thus also the mechanism by which new bitcoins are added to the network. (This process is referred to as "mining," and the users who choose to expend computing power to do so are referred to as "miners."[6])

In order to ensure that a constant flow of new bitcoins are added to the network, the difficulty of the proof of work necessary to create each new block is steadily and automatically adjusted, such that blocks are created at a constant rate of one new block roughly every ten minutes. At the same time, the number of bitcoins that can ever be mined is capped at 21 million.[7] To

[5] That the transaction is irreversible does not mean that the bitcoins in question cannot be returned to the sending public key. It just means that the sender cannot withdraw the transaction. The recipient is always free to reverse the transaction by initiating a transaction that sends the bitcoins back to the sender. In the campaign contribution context, this means that recipients can return contributions where necessary or appropriate, such as to comply with donor identification or contribution limit requirements.

[6] The analogy to mining is inexact. Gold miners unearth existing gold, whereas the bitcoin mining process results in the creation of new bitcoins.

[7] The 21 million cap on the number of bitcoins that can be mined is an arbitrarily chosen limit built into the protocol. To accommodate this limit, each bitcoin is subdivided down to eight decimal places, forming 100 million smaller units called "satoshis."

accomplish this, the number of bitcoins awarded for each new block is periodically halved.[8] The last bitcoins to be created this way will be created in approximately the year 2140.

While miners obtain newly-created bitcoins, the vast majority of Bitcoin users do not engage in mining, and therefore must acquire bitcoins from other sources. Some users acquire bitcoins directly from miners. In other instances, users obtain bitcoins from other users in exchange for goods or services, as many stores, restaurants, charities, and online businesses now accept bitcoins. Other users obtain bitcoins by buying or trading for them via one of the numerous exchanges and other service providers that perform those functions.

III. How Bitcoins Are Valued

Bitcoins are an intangible asset—they exist only in the form of the record of ownership maintained in the block chain. Their value is not tied to the scarcity of a physical resource (like gold), or to their issuance by some recognized central authority (like legal tender). Rather, they have value because users recognize them as a useful way of exchanging value, and have adopted them for that purpose. The limited supply of bitcoins, the increasing computational power required to add new bitcoins to circulation, the growing base of users, and their perceived strengths and weaknesses relative to other forms of value all factor into their value. Several leading exchanges maintain exchange rates that express the prices at which bitcoins trade relative to the dollar and certain other national currencies.

IV. The Advantages of Bitcoin Over Other Transaction Systems

The decentralized, open-source nature of Bitcoin gives it several advantages over other transaction systems. First, by eliminating the middleman, Bitcoin eliminates the cost and friction inherent in other transaction systems, making Bitcoin transactions nearly instantaneous and free or nearly free. Not only does this offer the promise of dramatically reducing the cost of existing forms of transactions such as overseas remittances, but it also enables new types of transactions like micro-payments.

Second, because every Bitcoin transaction is included in the block chain, the public details of the transaction can be viewed by any Bitcoin user or anyone else running the Bitcoin open-source software. Although Bitcoin transactions are "private" in the sense that there are no names attached to the public keys recorded in the block chain, all transactions associated with any given public key may easily be viewed and analyzed. This provides an unprecedented level of transparency to financial transactions. As we discuss below, this transparency is one of the features of the Bitcoin network that makes it ideally suited for political contributions.

[8] The reward started at 50 bitcoins and is halved every four years. Once the 21 million cap is reached, miners will be rewarded for creating blocks through small transaction fees.

Third, Bitcoin is highly protective of individual freedom. While the public details of every transaction are included in the block chain, Bitcoin users can choose whether to reveal their identity when engaging in transactions. Thus, unlike other financial transaction systems, Bitcoin puts privacy back in the hands of users, letting them determine the level of privacy they wish to maintain for a particular transaction. In instances where users have the legitimate need or desire to protect their identify, such as when paying for mental health services, they can do so. At the same time, where disclosure of personal information is necessary or appropriate (such as in connection with a contribution in an amount for which identification of the donor is required), the user is free to provide such information.

Finally, scholars view the Bitcoin protocol as a stimulus for financial innovation.[9] While the Bitcoin protocol is currently used almost exclusively for transactions in bitcoin digital currency, the Bitcoin network/protocol's neutral, open-source nature lends itself to numerous other uses. Since, bitcoins are, at their core, only a record of the history of ownership of a particular unit of value, they can be adopted as indicators of ownership interests in other assets as well. For example, bitcoins could be used to designate and transfer ownership in stocks, intellectual property, or ownership shares in a business entity. Moreover, other protocols can be added on top of the Bitcoin protocol to extend its functionality much like email protocols were built to extend the functionality of more basic Internet protocols. Examples of add-on protocols that have already been proposed or created include digital notary functionality to prove document ownership and authenticity, and a protocol for encrypted communications.

DISCUSSION

I. POLITICAL COMMITTEES SHOULD BE ABLE TO ACCEPT BITCOIN CONTRIBUTIONS

The threshold question presented by CAF's Advisory Opinion Request is whether donors should be permitted to make contributions to political committees in the form of bitcoins. The Commission should answer this question in the affirmative. Bitcoin donations fall squarely within the definition of permissible contributions pursuant to federal statute, and there is no statutory basis for disallowing them. The collection of donor information relating to bitcoin contributions is no more challenging than other forms of payment already approved by the Commission, such as electronic transfers and contribution by text messaging. Indeed, given the transparency of transactions on the Bitcoin network, bitcoins are ideally suited to use for contributions.

[9] *See generally* Jerry Brito & Andrea Castillo, *Bitcoin: A Primer for Policymakers* (Mercatus Center, 2013), available at http://mercatus.org/sites/default/files/Brito_BitcoinPrimer_embargoed.pdf.

A. *Bitcoins Are a Thing of Value and Are Thus Contributable*

The Federal Election Campaign Act ("FECA") (2 U.S.C. §431 *et seq.*) permits an individual to contribute (and a committee or candidate to accept) a "gift, subscription, loan, advance, or deposit of money or anything of value . . . for the purpose of influencing any election for Federal office." 2 U.S.C. §431(8)(A)(i). *See also* 11 C.F.R. §100.52(a) (defining "contribution" and "money"); 11 C.F.R. §104.13(b) (providing for the accounting of contributions in non-monetary forms). "Money" is defined as "currency of the United States or of any foreign nation, checks, money orders, or any other negotiable instruments payable on demand." 11 C.F.R. §100.52(a). "Anything of value" is broadly construed. It includes, but is not limited to, such items as stocks, bonds, art objects, other commodities, and services. *See e.g.* 2 U.S.C. §441b(b)(2); 11 C.F.R. §104.13(b); 11 C.F.R. §114.1(a)(1); Adv. Op. 1989-6 (June 1, 1989) (permitting contributions in the form of stocks); Adv. Op. 1982-8 (June 18, 1982) (permitting contributions in the form bartering credit units).

At least one other federal government agency has already recognized digital currencies such as bitcoin as "ha[ving] an equivalent value in real currency, or act[ing] as a substitute for real currency." In its March 18, 2013 Guidance, the Financial Crimes Enforcement Network ("FinCEN")[10] addressed the status of digital currencies like bitcoin[11] under the Bank Secrecy Act and its implementing regulations. *See Application of FinCEN's Regulations to Persons Administering, Exchanging, or Using Virtual Currencies*, FIN-2013-G001 (Mar. 18, 2013) ("Guidance"). FinCEN began by noting that its regulations define "currency" as "coin and paper money of the United States or 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." Guidance at 1 (citing 31 C.F.R. §1010.100(m)). FinCEN then went on to say that "'virtual' currency is a medium of exchange that operates like currency in some environments, but does not have all the attributes of real currency. In particular, virtual currency does not have legal tender status in any jurisdiction." *Id.* In other words, digital currencies like bitcoin can function in the same manner as "real" currency, despite lacking legal tender status.[12]

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[10] FinCEN is a bureau of the Treasury Department. It is responsible for anti-money laundering enforcement under the Bank Secrecy Act.

[11] In particular, the Guidance addressed the status of what it termed "convertible virtual currencies," which FinCEN characterized as "either ha[ving] an equivalent value in real currency or act[ing] as a substitute for real currency [i.e. legal tender]." Guidance at 1. The Guidance makes clear that decentralized digital currencies like bitcoins are convertible virtual currencies within the meaning of the Guidance. *See* Guidance at 5 (describing convertible virtual currency as "a de-centralized virtual currency (1) that has no central repository and no single administrator, and (2) that persons may obtain by their own computing or manufacturing effort").

[12] FinCEN's Guidance makes clear that bitcoins are not subject to the limitation on currency contributions set forth by 2 U.S.C. §441g, which applies only to "currencies of the United States or currency of any foreign country," i.e. to legal tender.

B. Contribution in Bitcoins Should be Treated no Different From Other Contributions Made Online or by Text Message

The Commission has previously sanctioned the collection of contributions in forms traditionally associated with reduced identifying information when donors are required to provide identifying information, and when there is an electronic record of that information available in connection with the donation transaction. Under the approach proposed by CAF, donations would be processed by online service providers, which will collect a donor's name, address, occupation, and employer name prior to a donor's submission of a contribution. (Alternatively, committees could develop their own information collection systems and accept donations in this same manner on their own behalf.) Donations can be rejected where donors do not enter the personal and employment information necessary to comply with applicable requirements. The collection of Bitcoin contributions is no different in this regard than the collection of contributions online or by text message.

For instance, the Commission approved of the use of the internet to collect contributions via "credit cards, electronic fund transfers and potentially other electronic means," so long as a complete and reliable "paper trail" confirming the legality of the contributions was created and maintained. Adv. Op. 1995-9 (Apr. 21, 1995). Of particular concern was whether committees could adequately ensure that contributions from prohibited sources (i.e. foreign nationals, those who had already exceeded the permissible donation limits, etc.) were not made or accepted, given the "unique global nature of the Internet and the unrestricted access to [] Web site[s]." The Commission answered this question in the affirmative, conditioned on the implementation of security procedures which required donors to enter their personal and financial information and attest to their qualifications to contribute. If donors checked "no" to any of the attestations, or left them blank, they would be advised that federal law prohibited contributions from individuals who did not meet those qualifications.

This approach was further developed in Adv. Op. 1999-09 (June 10, 1999), wherein the Commission approved the expansion of federal fund matching provisions to contributions collected online, so long as committees independently undertook the collection of relevant identifying and qualifying information. Under this procedure, the website would include a conspicuous disclaimer informing donors of the FECA's source restrictions and contribution limits, and donors would be required to complete an electronic form providing detailed personal information (including name and address), and attesting to the fact that they meet all of the FECA's requirements. (Donors entering intended contributions exceeding $200 would also be required to list their employers and occupations.) If donors opted not to provide any of the requested information, or failed to check any of the attestation boxes, the contribution would be rejected. The donor would then need to provide corrected or missing information, or the entire

transaction would be cancelled. Information regarding contributions that were approved for processing would then be entered into a database of the committee's donors to be checked against existing donor names and amounts. If the contribution appeared to be excessive, the committee was to either seek a timely reattribution, or refund the excessive portion. *See also* Adv. Op. 1999-36 (Jan. 14, 2000) (approving of similar voluntary information gathering measures for electronic checks).

The rationale behind these decisions is that, even though online contributions – unlike paper checks – do not by nature include donor information, online "screening procedures would allow the Committee to verify the identity of those who contribute via credit card with the same degree of confidence that political committees generally accept checks via direct mail and other forms of solicitation that are consistent with Commission regulations." Adv. Op. 1999-09 (quoting Adv. Op. 1999-03 (Mar. 18, 1999)). *See also* Adv. Op. 1999-36 (noting that screening procedures that would allow a committee "to submit evidence that 'the contributor has affirmed that the contribution is from personal funds and not from funds otherwise prohibited by law'" would bring electronic contributions within the ambit of those eligible for federal matching).

This same rationale led the Commission, in Adv. Op. 2012-30 (Sept. 4, 2012), to permit contributions by text message in all legal amounts once donors provided their names and addresses. Like many forms of online contribution, contributions by text messaging do not inherently contain a donor's name or address. *See* Adv. Op. 2012-17 (June 11, 2012). However, the Commission, in Adv. Op. 2012-30, permitted the acceptance of contributions via text message above the $50/month and $200/year or election cycle limits established in Adv. Op. 2012-17, once donors voluntarily submitted proper identifying information.[13]

Under CAFs' proposal, the acceptance of bitcoin contributions by federal political committees would integrate both elements the Commission has previously required for online and text messaging contributions. First, there would be an online screening system to ensure that prohibited sources do not contribute, and to ensure that donor identifying information is collected before a contribution is made. This will serve to ensure compliance with applicable donation limits and prohibitions on accepting contributions from certain classes of donors.

Second, bitcoin contributions, by their very nature, are uniquely transparent; not only is an online trail produced, but it is available to the public. The fact of, time of, and amount of each and every transaction from one public key to another occurring in the Bitcoin network is automatically recorded in the public block chain, and this record is maintained indefinitely. Because each transaction may be traced in the system to the sending and receiving public keys, other contributions made by the same donor may be identified and aggregated for accounting

[13] Bitcoin donations should also be permitted to be made without supplying personal information subject to similar limits.

purposes. Like email addresses, moreover, individual Bitcoin public addresses may be traced to IP addresses and thereby located geographically.[14]

Given the ability to screen online for prohibited sources and collect donor information, and given the traceable nature of bitcoin contributions, there is no legal basis for precluding bitcoin contributions to federal political committees. Accordingly, the Commission should follow its own long-standing policy of interpreting the FECA "in a manner consistent with contemporary technological innovations" (Adv. Op. 1999-9 (June 10, 1999)), and permit political committees to accept contributions in the form of bitcoins.

II. THERE IS NO NEED TO CATEGORIZE BITCOIN CONTRIBUTIONS AS "MONETARY" OR "IN-KIND"

The Bitcoin Foundation also agrees with CAF that bitcoin donations demonstrate characteristics of both monetary and in-kind contributions, and therefore that committees receiving bitcoin donations should be left free to determine, on an individualized basis, whether to ascribe to them monetary or in-kind treatment.

As noted above, the FECA provides that donations may be made in the form of "money or anything of value." 2 U.S.C. §431(8)(A)(i). "Money" contributions might include those made in the form of "currency of the United States or of any foreign nation, checks, money orders, or any other negotiable instruments payable on demand." 11 C.F.R. §100.52(a). Other non-monetary items of value, including stocks, bonds, art objects, other commodities, and services, are considered "in-kind" contributions. *See e.g.* 2 U.S.C. §441b(b)(2); 11 C.F.R. §104.13(b); 11 C.F.R. §114.1(a)(1); Adv. Op.- 1989-6; Adv. Op. 1982-8. Although, like money, in-kind donations "function as a medium of exchange," the value of in-kind donations "can be determined with certainty only when they are exchanged . . . they need not first be converted into cash in order to secure goods or services."

The Bitcoin Foundation submits that the Commission has already determined, in another context, the issue of the classification of assets that may be either/both monetary or in-kind, and that no further action or opinion on the part of the Commission is thus required. *See* Adv. Op. 1980-125 (Nov. 21, 1980). In Adv. Op. 1980-125, the Commission was presented with the question of whether a committee was required to account for a donation of silver dollars as monetary or in kind. Noting that there "[wa]s nothing in either the [FECA] or the regulations which state[d] how a contribution made in the form of currency [wa]s to be valued," the Commission concluded that "the value put upon a contribution of currency, which ha[d] the potential to be treated as either a contribution of money or an in-kind contribution with a different value, [wa]s to be

[14] By contrast, no record of transmission is generated when tangible currency changes hands, making Bitcoin far superior to cash for contribution purposes.

determined by the manner in which the currency [wa]s treated." The Commission explained that, if the committee opted to deposit the silver dollars or use them to make expenditures, they should be treated as a monetary donation. Conversely, if the committee opted to dispose of the silver through the commodities market, the donation should be valued according to in-kind principles. Because the coins could reasonably be used in either manner without violating election law, the Commission wisely deferred to the decision of the recipient in determining the use that best served the purposes of the campaign. The Bitcoin Foundation sees no reason to deviate from this opinion in the case of bitcoin contributions.

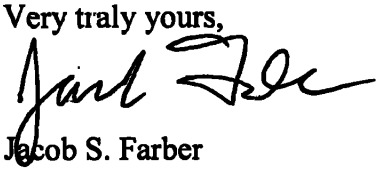
There is an additional reason why bitcoin transactions should not be preemptively categorized as either monetary or in-kind. While, as discussed above, the Bitcoin protocol is currently used mainly for bitcoin digital currency transactions, as a neutral, open-source protocol, its potential uses are nearly limitless. The use of bitcoins as the indicia of, and to transfer ownership in other classes of assets is already being explored, as are entirely new ways of using the Bitcoin protocol. The Commission should not risk curtailing that innovation by categorizing Bitcoin while it is still in its infancy.

Moreover, a ruling on whether bitcoin contributions must necessarily be classified as monetary or in-kind risks prejudicing the ongoing consideration of the regulatory status of Bitcoin and digital currencies in general by other federal agencies. In addition to FinCEN, agencies such as the SEC and the Commodities Futures Trading Commission, have either addressed bitcoin-related questions or have said they are considering whether they have jurisdiction over Bitcoin. Since the Commission need not rule on how bitcoins should be categorized, it should avoid the risk of muddying the consideration of Bitcoin by other federal agencies.

CONCLUSION

For the foregoing reasons, the Bitcoin Foundation urges the Commission to conclude both that bitcoins can be used to make contributions, and that bitcoin recipients should be permitted to categorize individual contributions as monetary or in-kind at their discretion.

Very truly yours,



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