Are Bitcoins Making Money Laundering Easier?

Bitcoins are sexy, but cash is still king.

By Katherine Mangu-Ward

Photo by Saul Loeb/AFP/Getty Images

*On Feb. 11, Future Tense—a partnership of **Slate**, the New America Foundation, and Arizona State University—will host an event on cryptocurrencies at the New America office in Washington, D.C. For more information and to watch the webcast, visit the New America website.*

A new protocol for keeping digital ledgers in a decentralized form doesn't exactly sound like the stuff of front-page headlines, dramatic press conferences, or televised congressional hearings. It barely sounds exciting enough to merit an afternoon breakout session at a conference of certified public accountants.

But despite its nerdy roots, Bitcoin, also sometimes referred to by the much sexier description "digital cryptocurrency," seems to have a way of grabbing attention. That's probably because you can't get too far into any discussion of Bitcoin before someone starts fretting about "money laundering" or talking about how absolutely everyone is buying drugs, guns, and who knows what else with this newfangled digital dough.

Schumer and others may be barking up the wrong series of tubes.

In 2011, New York Sen. Chuck Schumer, set the gold standard for anti-Bitcoin freakouts, calling Bitcoin "an online form of money laundering used to disguise the source of money, and to disguise who's both selling and buying the drug." Never one to opt for understatement or worry about technical details, Schumer also declared that bitcoin transactions on the nowshuttered Silk Road site—where people could indeed purchase illegal drugs with relative impunity, thanks to bitcoin and (more importantly) the anonymity-producing Tor network—were “more brazen than anything else by lightyears."

There have also been some high profile arrests of pleasingly scruffy-looking characters to keep interest piqued. Last week, BitInstant CEO Charlie Shrem was charged with money laundering. It looks like Shrem was working with Robert Faiella, whom he knew only by his username BTCKing, to help customers convert dollars to bitcoins for use on Silk Road. According to the Financial Crimes Enforcement Network (FinCEN), BitInstant is a payment company, so it is legally required to record and report information about its customers, particularly potentially shady dealings. Shrem, who was also on the board of the semi-official spokesorganization for the ownerless cryptocurrency, the Bitcoin Foundation, did no such reporting.

Similar money laundering charges shut down the shady sites Liberty Reserve and eGold last year. Operators of those sites argued that they should be exempt from money laundering laws since they were payment sites, not money transmitters. The feds thought otherwise.

It’s not just big dogs who have attracted the attention of federal regulators. Mike Caldwell had a small online business producing physical coins engraved with a private key that could be used to unlock digital Bitcoins. Late last year, he got an alarming letter from FinCEN and ceased operations. Apparently even his modest outfit fit the definition of a money transmitting firm, since he briefly held the actual value of his clients’ bitcoins during the process. He has since rejiggered his product to skip that step and hopes Casascius Coins will be back in business soon.

The Cato Institute’s Jim Harper told me in an email that money laundering “is a crime of pretty recent vintage, invented because other crimes like drug dealing have no complainants, which makes them hard to discover and prosecute.” He suggests we think of money laundering as the crime of "resisting the use of money for surveillance” and remain skeptical in the face of hysteria.

He’s right. Banks have been subject to some reporting requirements since the 1970s, but it wasn’t until 1986 that the Money Laundering Control Act made handling dirty money a criminal act. The laws are tricky, since they require anyone who handles money to develop theories about where that money came from and why their customers are moving their money in certain ways. But a quick survey of the “specified unlawful activities” that can throw off dirty money shows just what you’d expect—drug money looms large, suggesting that the laws are really about having something to throw at organized crime when other charges won’t stick.

So will the world’s criminals be turning to bitcoins to conceal their ill-gotten gains? One sign that Schumer and others may be barking up the wrong series of tubes is that the regulators themselves don’t seem terribly concerned about that prospect.

In November, the Senate’s Homeland Security and Governmental Affairs Committee held a hearing, at which regulators repeatedly rebuffed efforts by senators to suggest that they might need the legislature to give them more power. An unusual sight in Washington, to say the least.

FinCEN director Jennifer Shasky Calvery, who is more or less in charge of stopping money laundering in the United States, made a list of the reasons why "illicit actors" might like virtual currencies. Her list includes the fact bitcoin and other virtual currencies are "relatively simple for the user to navigate," "may have low fees," are "accessible across the globe with a simple Internet connection," "can be used both to store value and make international transfers of value," "is generally secure," feature "irrevocable transactions," and have "no administrator to maintain information on users."

Kind of sounds like an advertisement for Bitcoin, no? She acknowledged that many of these reasons are appealing to legit users as well and notes that not all innovation in money transmission is pernicious, citing online banking and prepaid debit cards as beneficial for a wide variety of users. She also expressed confidence that no new laws are needed to catch bad actors, even if they choose to do business in bitcoin.

Later in the same hearing, Edward Lowery, a special agent with the Secret Service, takes on the question with a hint of a smirk and a raised eyebrow. "High level international cybercriminals," he says of his experience, "have not by-and-large gravitated to the peer-to-peer cryptocurrency, such as Bitcoin." Instead, they prefer "centralized digital currency" that is based somewhere with looser regulations and lazier enforcement.

And as Shasky Calvery notes off the cuff during the question and answer portion of the hearing: "Cash is probably still the best medium for laundering money."

For now, regulators are being surprisingly restrained in their approach to bitcoin. As Cato's Harper notes, bitcoin may continue to be unappealing for criminals due to the public nature of the ledger—every bitcoin transaction is made public, albeit pseudonymously. "But even if it were" an effective tool for money laundering, he says, "you start to ask yourself: Are we going to forgo financial innovation and its massive consumer benefits—life, health, human welfare of all kinds—to prop up the drug war?"

Money laundering is the process of throwing needles into a haystack. The idea is to lose dirty cash in a jumble of legitimate transactions. About $8 billion worth of transactions were conducted in bitcoin from October 2012 to October 2013. During 2012, Bank of America processes $244.4 trillion in wire transfers and PayPal processed $145 billion. The bitcoin haystack just isn't big enough or messy enough to be a useful place to launder money right now. A better option: cash-heavy businesses, such as casinos or—yes—laundromats.

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