

TREASURY EXECUTIVE MINUTE

Minute No. 20140052

15 January 2014

Minister for Small Business

cc: Treasurer
Assistant Treasurer

BITCOIN AND ILLICIT TRANSACTIONS

Timing: Your office requested this brief by COB Wednesday.

Recommendation:

- That you note this brief requested by your office on the use of Bitcoin as a virtual currency and the draft letter to respond to s47F (Attached).

Noted

Signature:/...../2014

KEY POINTS

- s47F
- Bitcoin differs from a traditional electronic payment system in that it does not require a third-party intermediary such as a bank. Rather, Bitcoin operates through a decentralised peer-to-peer network with participants communicating directly with each other. In essence, the peer-to-peer network of participants takes the place of the third-party intermediary.
- While there is some use of bitcoins for legitimate transactions, there are concerns Bitcoin is being used in criminal activity as users are able to maintain a high degree of anonymity.
- The use of Bitcoin for illicit transactions or money laundering is an issue of law enforcement. In general, criminal law enforcement and money laundering issues are overseen by the Attorney-General's Department.
 - Australia's anti-money laundering regime, set out in the *Anti-Money Laundering and Counter-Terrorism Financing Act 2006* (AML/CTF Act), is currently subject to a statutory review which will consider whether the regime should be expanded to cover new payment methods (such as Bitcoin) to enhance law enforcement capabilities.

• s47F

• s47C

s22
Senior Adviser
Financial System Division

Contact Officer: s22 Ext: s22

ADDITIONAL INFORMATION

Overview

- Beginning operations in 2009, Bitcoin is one of the first implementations of a decentralised virtual-currency, created by a group or individual known as ‘Satoshi Nakamoto’.
- Since 2009, Bitcoin has drastically expanded such that it has attracted the attention of regulators. Bitcoin is free open-source software, such that any developer or programmer can contribute to its development.
- In a traditional payments system, operations and transactions occur through a third-party intermediary or centralised administrator (such as PayPal or MasterCard). A key purpose that the intermediary serves is that it maintains a ledger of account holders’ balances and transactions to ensure that money is not spent twice and has a correct record of who is holding the money. The Bitcoin system is a *public ledger* removing the need for an intermediary by utilising the users who are connected to the network to provide computer processing power to verify and update the public ledger of transactions through the use of public-key cryptography. These users are then rewarded in bitcoins.
- There are currently approximately 12 million bitcoins currently on the global market with a market capitalisation growing from US \$1.5 billion in May 2013 to approximately US \$10 billion as at 14 January 2014. (Note: **The price of bitcoins are extremely volatile** with indications of the price ranging from AUD \$300 to AUD \$1900 per bitcoin over the last 30 days). Its total supply is capped at 21 million bitcoins (to be reached in 2140).
- Although its decentralisation and lack of a monetary authority with the power to reduce its value has been of appeal to some sections of society, anecdotal reports indicate it is used for illicit activities due to the anonymity afforded to users.
- The volatile price of bitcoins will likely preclude its widespread adoption for legitimate purposes. Some businesses have begun accepting bitcoins, with some having done so as a gimmick. Some examples include:
 - the online retail store Bitcoinstore (www.bitcoinstore.com) sells electronics which accepts bitcoins as payment;
 - reportedly small businesses in the United States which have begun accepting bitcoins as payment and in some cases, offering discounts to those who do so;
 - in November 2013, Richard Branson, founder and Chairman of Virgin Group announced that Virgin Galactic, which provides commercial space flight services, would be accepting bitcoins as a form of payment;
 - many gambling websites such as poker and online betting sites are also accepting Bitcoin in their operations; and
 - locally, the Daily Telegraph reported on 29 September 2013 that Woolloomooloo pub The Old Fitzroy was accepting bitcoins from customers.

Regulation of Bitcoin

- The use of Bitcoin for illicit transactions or money laundering is an issue of law enforcement, rather than payments system regulation. This is covered by the *Anti-Money Laundering and Counter-Terrorism Financing Act 2006* (AML/CTF Act), AML/CTF Regulations and AML/CTF Rules. These are collectively referred to as the ‘AML/CTF regime’.
 - The AML/CTF regime establishes reporting requirements for regulated entities in order to deter, detect and combat serious and organised crime, money laundering and terrorism financing.
 - The AML/CTF regime is administered by the Attorney-General.
- As a virtual currency, Bitcoin currently falls outside the scope of both the Australian AML/CTF regime and international AML/CTF standards, which are set by the Financial Action Task Force (FATF), of which Australia is a member.
 - Australia, represented by the Attorney-General’s Department (AGD), will take over as President of FATF on a rotating basis on 1 July 2014. s47C
- Australia’s AML/CTF regime is currently subject to a statutory review, required by the AML/CTF Act. The review was commenced by the AGD in December 2013.
 - This review will seek to identify how the regime could be enhanced to achieve the goal of maintaining a regulatory framework which complies with international standards and combats money laundering and terrorism financing effectively and efficiently.
 - The review will also consider whether the current scope of Australia’s AML/CTF regime is appropriate, including whether it should be expanded to cover new payment methods (such as Bitcoin) to enhance law enforcement capabilities.

:

s47C

- s47C

Views

- s47C

- s47C

- s47C

-

-

Internationally

- In 2013, it was reported that the US financial regulators were discussing whether Bitcoin might fall under their regulatory remit. Officials from the Commodity Futures Trading Commission (CFTC) said that Bitcoin was an issue they would need to explore.
- In December 2013, the People's Bank of China (PBOC) banned financial institutions from trading in Bitcoin. The ban reflects the concern about the risk that the virtual currency may have on financial stability.
- The Reserve Bank of India (RBI) have warned the public against the use of virtual currencies such as Bitcoin, pointing out the potential financial, legal, and security related risks.
 - The RBI have indicated that it had been examining the issues associated with Bitcoin's use under their country's legal and regulatory framework.

Consumer protection issues

- As the use of Bitcoin and other virtual currencies is not illegal in Australia, there are no immediate concerns from a consumer protection perspective. However there are growing concerns about the use of these currencies to purchase illegal and illicit goods such as drugs and firearms online.

-

- In 2013, former Assistant Treasurer Bradbury imposed a national interim ban on a range of dangerous synthetic drugs under the product safety framework contained under the Australian Consumer Law.
 - This interim ban provided the States and Territories with sufficient time to update their own drug legislation (specifically NSW and the Northern Territory) to prohibit the supply of all substances that are currently proscribed by Schedule 9 of the Poisons Standard and consumer goods containing synthetic drug substances that were being offered for sale over the counter and online. All jurisdictions have now updated their drug legislation to adopt Schedule 9 of the Poisons Standard.
- Consumer agencies have agreed that the issue of synthetic drugs should fall back to law enforcement and health agencies that have responsibility for these issues.