StartBitcoin

New York Department of Financial Services
One State Street
New York, NY 10004

October 21, 2014

Dear Mr. Syracuse,

We write on behalf of StartBitcoin (http://startbitcoin.org). We are a recently-formed group of entrepreneurs promoting the future of digital currencies and decentralized technology. Our projects include the successful BitLicense extension letter, where nearly 500 industry leaders signed on to a request to extend the comment period, and the website New York Needs Bitcoin (http://nyneedsbitcoin.com), a resource for the digital currency community to read about reactions to BitLicense and submit comments.

Our founders are Austin Walne, a Bitcoin entrepreneur with experience in political and public affairs advocacy, and Elizabeth Stark, a former lecturer at Stanford and Yale on technology policy with years of advocacy experience and virtual currency entrepreneur who holds a J.D. from Harvard Law School. Since the introduction of BitLicense, we've been collaborating with a network of entrepreneurs across the country and around the world.

There have been many comments that highlight many of the specific problems with the BitLicense proposal, including those of Circle, Mercatus Center, BitGo, EFF, Bitcoin Foundation, and Coinbase. While we agree with the issues these commenters have raised, we are choosing not to focus on the specifics of the proposal. Instead, we'd like to highlight several broader points that are relevant to our community.

(1) BitLicense Hurts Entrepreneurs

As entrepreneurs, we know how hard it is to start a business. You're putting your livelihood, reputation, and capital on the line, going through a tumultuous process to start a company. As Silicon Valley thought leader and VC Marc Andreessen has stated: "a startup puts you on an *emotional rollercoaster* unlike anything you have ever experienced."

BitLicense, as it stands, turns this already-difficult process into an impossible one. As we stated in our TechCrunch piece when the BitLicense draft was first announced, no startup could possibly comply with the requirements imposed or afford the cost associated; and therefore people would choose not to start a business at all.

There has been one common ground amongst the entrepreneurs we've spoken to: BitLicense will hurt them.

(2) BitLicense Hurts the NY Tech Ecosystem

New York has developed a thriving startup and entrepreneurial ecosystem over the last decade. As part of StartBitcoin, we have been in touch with many of these startups, who care deeply about Bitcoin's future but do not necessarily know how to, or have the time to, engage in the policy space.

We've already heard of stories of startups leaving New York, or leaving the United States altogether. We've heard of technologists preparing to block New York residents. We've participated in meetups with the New York Bitcoin Developers community, all of whom are deeply concerned about what this regulation will do to their livelihood.

(3) BitLicense Hurts the Next Generation of Bitcoin

Many of the comments that people have submitted focus on the first generation of Bitcoin, that of its role as a currency. One of the perspectives that has been less vocal, though, is that of the entrepreneurs developing new technologies dubbed "Bitcoin 2.0." This is in part because these innovations are so new and many of these entrepreneurs and developers are just getting started. We'd like to highlight two examples:

a. Tokens Bitcoin's technology enables the creation of tokens that use the backbone of cryptography and virtual currency technology to create exchangeable denominations that are not primarily financial in nature. Think of these like frequent flyer miles, or reputation points, that anyone can trade over the Internet. One example of these is LTBCoin, a token issued on top of the Counterparty network for members of the community website Let's Talk Bitcoin. Users send them to each other in recognition of good posts. There are many more examples of these that are in development.

While these tokens may be exchangeable for money, their primary purpose is not one that is financial. Think of them as property that may have some value, but whose main goal is to convey some other non-financial form of value. We strongly suggest that DFS implement a standard to discern when "digital currency" is financial in nature, and make it explicit that they will not regulate the crypto-equivalent of social capital. The standard should exclude all non-primarily-financial tokens.

b. Blockchain-Based Applications Superintendent Benjamin Lawsky recently stated in his talk at Cardozo Law School that he doesn't intend to regulate software developers. Unfortunately, though, many of the Bitcoin 2.0 technologies both involve some financial nature and the creation of software. One of the most compelling examples of this is the emerging field of blockchain-based applications.

Blockchain-based applications use the distributed public ledger of Bitcoin to certify transactions and ensure that there is no central authority that could be compromised. Examples of these include a decentralized Dropbox-style file storage (Storj, Maidsafe), a digital art property registry (Monegraph), a way to verify one's identity (Onename.io), and distributed voting mechanisms that can't be forged (Agora). Every day more and more of these solutions emerge.

Because these technologies often use digital currency as a means to regulate the system or compensate participants, BitLicense would very much regulate software developers and architects in the Bitcoin 2.0 ecosystem.

(4) Licensing Isn't the Way to Go

While we understand that there is a tradition of licensing money transmitters in the regulatory realm, we'd like to underscore that licensing is not a good option for our community. Digital currencies are not akin to traditional money, and as we've explained above, there are a multitude of both non-financial and semi-financial uses that are not necessarily analogous to pre-Internet uses. The technology evolves so quickly that by the time a licensing regime came into place, the technology will have already outpaced the rules.

If you must license companies in the Bitcoin space, we urge you to limit it to full custodial services (i.e. users do not hold their private key and without multisig) where the currency held is fully financial in nature (i.e. Bitcoin), or exchanges that provide an endpoint to "fiat" currencies such as the US Dollar. Instead of creating a new licensing regime, a far better means would be to rely on the existing money transmission regime, or something less onerous. While imperfect, especially for entrepreneurs given the different licensing practices amongst various states, this is an approach that would not disadvantage Bitcoin entrepreneurs as compared to startups building technology in the traditional monetary space.

(5) Safe Harbors Are a Better Way

It has been a common conception amongst technology leaders that Bitcoin is the next Internet. This is not only in terms of financial uses, but all of the technological innovations that the blockchain can enable. It's vital that regulators, when looking at the regulation of Bitcoin, learn their lessons from the early days of the Internet. Imagine a world in which we had a licensing regime for any website that an individual put up on the Internet. We would have lost trillions of dollars of value that this technology ultimately produced.

Instead, what worked for the early Internet and what can work for the Bitcoin community is the creation of safe harbors. Key safe harbor regimes like the Communications Decency Act § 230 or the Digital Millennium Copyright § 512 were essential to the growth of the early Internet. One important point with these safe harbors is that they did not just apply to small startups. They were available to small and large companies alike. For example, companies like Facebook, Google, and Twitter are still reliant on these safe harbors today.

Instead of creating a BitLicense, the DFS should create a BitSafeHarbor. This safe harbor should include a set of industry standards and best practices that companies in the space would have to abide by to ensure consumer protection and public safety. It would allow for flexibility in terms of emerging solutions in the space, and there could be an annual review of the rules to account for the evolving technology. Companies that do not comply should be subject to fines, liability, or even a private right of action. An entire industry would spring up around complying with the safe harbor, and it would leave for flexibility in this fast-growing field.

We urge DFS to reconsider its approach when it comes to licensing companies in the virtual currency space. A safe harbor-based approach would compel companies with requirements without having to ask for permission. The early regulation of the Internet got it right, and we would be in a very different place today if regulators had taken the tack of the BitLicense.

(6) Blockchain-Based Solutions Provide Compelling Answers

Some of the most exciting developments in the cryptocurrency space right now are around solutions that leverage the power of the blockchain to achieve public policy goals without stifling innovation. When asked about these at Cardozo Law school, Superintendent Lawsky replied that they mostly seemed like "theories" right now. His answer highlights the nature of our space: many of the solutions are still developing, which is why we must allow them to flourish instead of regulating too quickly. These emerging technologies that seem like "theories" can become reality very soon. Mandating inefficient solutions that do not take advantage of the great power this technology possesses would be a huge mistake.

There are existing and proven cryptographic solutions such as "multisig," "proof-of-solvency" audits, and blockchain-based approaches for AML monitoring. We are members of Crypto-Economy Working Group, which is documenting research and developing best practices in this space. We urge the DFS to take a closer look at how these solutions will solve their regulatory objectives. Instead of having to comply with any specific technological approach or standard, as new ones often evolve, we urge DFS to again come up with standards in conjunction with a safe harbor. There are precedents for using a "best practice"-based approach, and any policy solution should rely on them.

If DFS ignores the novel solutions that blockchain-based technology brings, we risk discouraging solutions that are cheaper, more efficient, and provide a substantially higher degree of consumer protection and privacy.

Concluding Thoughts

We ask that the DFS engage more with the entrepreneurial community. As such, we would be happy to meet with the Department, organize an event with startups, and work together on the creation of a BitSafeHarbor that would enable companies of any size to grow while meeting public policy objectives. We would be pleased to work with the DFS on the further detailed development of such a regime in conjunction with policy groups, investors, and entrepreneurs.

Other states and jurisdictions are looking to New York as a first mover in this space, but many believe that DFS has gone too far. By the creation of a permissionless regime that fosters entrepreneurship in the way that Internet safe harbors did, DFS can play a role in creating trillions of dollars of new value for New York and the United States. We urge DFS to do just that, and cement its role in history as the steward of the next Internet.

Sincerely,

Elizabeth Stark and Austin Walne

Founders, StartBitcoin