

Client Update: Government Brings Important Case Against Illegal Marketplace “Silk Road;” Government Acknowledges Lawful Uses of Bitcoin



Decentralized Virtual Currencies, Electronic Financial Services, Investigations & White Collar Defense

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The virtual currency industry is in the news once again following the October 1, 2013, Federal Bureau of Investigation’s shutdown of the “Silk Road” website. As part of the shutdown of the well-known underworld bazaar, the government seized \$3.6 million worth of Silk Road’s bitcoin assets, constituting the largest bitcoin seizure seen to date, and **arrested the website’s alleged operator**, Ross William Ulbricht at a San Francisco public library. According to the unsealed criminal complaint filed in the Southern District of New York on September 27, 2013, Ulbricht, who used the moniker “Dread Pirate Roberts,” used the website to participate in a **narcotics trafficking conspiracy**, a computer hacking conspiracy and a money laundering conspiracy.

Prosecutors alleged that Silk Road was a virtual marketplace allowing consumers to procure narcotics and other illegal and fraudulent goods and services without detection. Indeed, Ulbricht is alleged to have designed the Silk Road to process transactions in a manner that, like cash transactions at actual bazaars, cannot be traced back to either the buyers or the sellers of merchandise.

Ulbricht, the government **alleges**, took a number of precautions to ensure the anonymity of his clientele, including operating the website on “The Onion Router” or “Tor” network, which requires special software and is “designed to make it practically impossible to physically locate the computers hosting or accessing . . . the network.” Ulbricht also took steps to limit the form of payment accepted to bitcoin digital currency, which was then “tumbled” with “dummy transactions” to frustrate the public recording procedures built into the **bitcoin platform**.

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The criminal complaint might seem to provide fodder for recent suggestions that virtual currencies are “a virtual **Wild West** for narcotraffickers and other criminals” that “support[s] dangerous criminal activity.” Yet, Ulbricht’s use of both the Tor network and a Bitcoin tumbler underscore that the mere use of bitcoins does not provide the anonymity required to shield criminals from law enforcement scrutiny. Significantly, the criminal **complaint** itself notes that “Bitcoins are not illegal in and of themselves and have known legitimate uses.” Moreover, **representatives** of the virtual currency industry welcomed the news of the Silk Road enforcement as a positive step aligned with their efforts to root out bad actors that detract from the otherwise legitimate uses of virtual currencies.

Although Ulbricht’s arrest only adds to the growing number of enforcement actions involving virtual currency-based businesses, including those actions against **Mt. Gox**, **Liberty Reserve** and **Trendon Shavers**, it is clear that the government’s actions do not target virtual currency itself. Rather these are prosecutions of criminals that happen to have used virtual currencies to accomplish their unlawful ends.

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