

# Legal regulation of cryptocurrency and NFTs

Hong Kong





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## Introduction

There is an increasing number of charities across the world that have started accepting cryptocurrency as donations, including **UNICEF** and the **Salvation Army**. New platforms like **The Giving Block** and **DoinGud** are helping nonprofits to raise funds with cryptocurrency and non-fungible tokens (“NFTs”).

To help charities better understand the opportunities and risks involved in working in this new context, PILnet with its partners launched a project about legal regulation of cryptocurrency and NFTs in different jurisdictions around the world.

The report below aims to consider:

- (a) The legality of cryptocurrency
- (b) Accepting cryptocurrency
- (c) Accepting NFTs and its proceeds
- (d) Issuing NFTs to raise funds

## Disclaimer

PILnet, and partners participating in this research, are not liable toward third parties for the accuracy of the information contained in the research about cryptocurrency and NFTs. The information contained herein cannot be considered as legal advice. The research was carried out in 2022-2023 and responds to the regulatory framework in effect during this time period.

## Contents

Introduction.....	I
Contents .....	II
1. Is engaging in blockchain technology legal in Hong Kong?.....	1
2. Is accepting cryptocurrency permitted for charities? If so, what legislation/regulation governs it? .....	1
3. Is issuing NFTs to raise funds permitted for charities? If so, what legislation/regulation (if any) governs it?.....	3
4. Are there tax implications for donations of cryptocurrency or NFTs? Are there obligations to pay tax for charities who sell NFTs for fundraising purposes?.....	5
5. What is the best practice or guidance?.....	6

## 1. Is engaging in blockchain technology legal in Hong Kong?



There are currently no laws or regulations that provide that engaging in blockchain technology is illegal in Hong Kong. However, certain activities related to blockchain technology, including activities relating to cryptocurrency and virtual assets, may be subject to restrictions under Hong Kong laws and regulations. Please refer to the sections below.

## 2. Is accepting cryptocurrency permitted for charities? If so, what legislation/regulation governs it?

There are no specific limits and restrictions on charities accepting crypto assets (including NFTs) as donations, or otherwise dealing with crypto assets (including opening and managing wallets or accounts with crypto exchanges or using crypto assets directly). However, charities should consider the following when accepting crypto assets as donations.



### Money Laundering, Terrorist Financing, and Sanctions

Accepting crypto assets (including NFTs) as donations, or otherwise dealing with crypto assets in Hong Kong, would be subject to Hong Kong money laundering, terrorist financing, and sanctions laws and regulations. These include the Organised and Serious Crimes Ordinance (“**OSCO**”), Drug Trafficking (Recovery of Proceeds) Ordinance (“**DTROPO**”), United Nations (Anti-Terrorism Measures) Ordinance (“**UNATMO**”), United Nations Sanctions Ordinance (“**UNSO**”), and Weapons of Mass Destruction (Control of Provision of Services) Ordinance (“**WMDO**”).

### Anti-Money Laundering and Counter-Terrorist Financing (“**AML/CTF**”) -- **OSCO**, **DTROPO**, and **UNATMO**

Under **OSCO** and **DTROPO**, it is an offence for a person (including a charity) to deal with property, knowing or having reasonable grounds to believe that it (directly or indirectly) represents the proceeds of an indictable offence, or the proceeds of drug trafficking, unless the person can prove that they intended to disclose such knowledge or suspicion (and any matter on which that knowledge or suspicion was based) to an authorized officer as soon as it was reasonable for them to do so, and that they had a reasonable excuse for failing to do so earlier.

**UNATMO** prohibits, among other things, (i) the provision or collection of property with the intention that the property will be used (or knowing that the property will be used) to commit terrorist acts (whether or not the property is actually so used), and (ii) dealing (directly or indirectly) with any property knowing that (or being reckless as to whether) the property is terrorist property, is property owned or controlled directly or indirectly by a terrorist or terrorist associate, or is property held by a person on behalf of (or at the direction of) a terrorist or terrorist associate, unless the person made a disclosure to an authorized officer and does the act (deals in the relevant property) with the consent of the officer, or the person made the disclosure after they carried out the act, on their own initiative, and as soon as it was reasonable for them to make it.

A charity (including individuals representing the charity) should, before accepting crypto assets as donations, ensure that such acceptance would not contravene the above anti-money laundering laws, that is, these crypto assets are not proceeds from an indictable offence, drug trafficking, or terrorist properties. If a charity (including individuals representing the charity) knows or suspects that such crypto assets contravene the said laws, a suspicious transaction report (“STR”) should be made to the Joint Financial Intelligence Unit (“JFIU”), which is jointly run by the Police and the Customs and Excise Department. In the case an STR is made, the charity should also not disclose to others any matter likely to prejudice an investigation which might be conducted following such a report (i.e., tipping off).

### Sanctions – UNSO and WMDO

UNSO and its subsidiary regulations implement sanctions imposed by the UN Security Council, including complete or partial economic and trade embargoes, arms embargoes, and other mandatory measures. For example, it is an offence under the UNSO to deal with funds or other financial assets or economic resources owned by or otherwise belonging to, or held by, certain persons or entities, a list of which is published in the Government Gazette.

WMDO prohibits a person from providing any services where they believe or suspect, on reasonable grounds, that those services will or may assist the development, production, acquisition, or stockpiling of weapons of mass destruction.

A charity (including individuals representing the charity) should, before accepting cryptocurrencies, ensure that such acceptance would not contravene the above sanctions laws, that is, these cryptocurrencies are not related to sanctioned countries / entities / persons or would assist in the development, production, acquisition, or stockpiling of weapons of mass destruction.

### **Dealing with Banks**

Financial institutions in Hong Kong, including banks, are subject to the abovementioned anti-money laundering, counter-terrorist financing, and sanctions laws, as well as the Anti-Money Laundering and Counter-Terrorist Financing Ordinance (“AMLO”) and regulatory guidance issued by their respective regulators on anti-money laundering and counter-terrorist financing requirements and obligations (“**AML Guidelines**”).

In particular, the Hong Kong Monetary Authority (“HKMA”), the regulator of banks, issued regulatory guidance setting out guiding principles on what HKMA-regulated authorized institutions (i.e., banks) should pay attention to when dealing with crypto assets and crypto-asset service providers (“**HKMA Guidance**”). The HKMA Guidance provides guidance on how banks should interface with and provide intermediary services relating to crypto assets to customers. The HKMA adopts a risk-based approach in supervising banks’ VA-related activities. In accordance with the HKMA Guidance, banks will:

- undertake risk assessments to identify and understand the associated risks before engaging in any crypto-asset-related activities;
- conduct proper due diligence of the crypto assets to which they will incur exposures;

- pay attention to customers engaging in crypto-asset-related activities through their bank accounts (e.g., frequent fund transfers to and from crypto-asset platforms), and will file STRs to the relevant authority where there are grounds for suspicion;
- conduct appropriate money laundering and terrorist financing risk assessments in line with the risk-based approach to differentiate the risks of individual crypto asset service providers. Banks may need to undertake additional customer due diligence measures similar to those for offering correspondent banking; and
- confirm with the crypto-asset service providers concerned that its operations do not breach any applicable laws and regulations in Hong Kong or other relevant jurisdictions.

### Dealing with Crypto Exchanges

While there are no specific laws and regulations restricting or prohibiting persons from Hong Kong (including charities) to deal with crypto exchanges, many of these exchanges are not appropriately regulated or licensed in Hong Kong or other relevant jurisdictions. Accordingly, there may be heightened risks relating to anti-money laundering, counter-terrorist financing, and sanctions, which charities must consider when dealing with these crypto exchanges, as they may not have put in place appropriate measures to manage money laundering, terrorist financing, and sanctions-related risks. These crypto exchanges may also not have, among other things, appropriate internal governance procedures and policies and investor protection measures, and therefore charities may lose all their crypto assets in the event that such crypto exchanges are compromised (or otherwise subject to liquidation), if charities decide to deposit their crypto assets with such exchanges.



### 3. Is issuing NFTs to raise funds permitted for charities? If so, what legislation/regulation (if any) governs it?

Generally, charities are permitted under Hong Kong laws and regulations to issue NFTs to raise funds. However, crypto assets, including NFTs, have different terms and features, and such terms and features may evolve over time. The laws and regulations applicable to crypto assets depend on the terms and features of such assets.

The most relevant piece of legislation would be the securities laws in Hong Kong, the Securities and Futures Ordinance (“SFO”), as certain crypto assets (including NFTs) may fall within the broad definition of “securities” under the SFO, or “collective investment scheme,” of which an interest would also fall within the definition of “securities.” Generally speaking, if a crypto asset possesses features and terms such as providing or promising profits, incomes, or other returns (whether by way of crypto asset or otherwise), including by way of staking, burning of tokens, or providing royalties to crypto-asset holders, such crypto asset would likely be viewed as “securities.” If a crypto asset confers any ownership of share capital or equity interests of a company or project, it would also likely be viewed as “securities.” On the other hand, if a crypto asset, such as an NFT, is a genuine digital representation of a collectible, the activities related to it would unlikely fall

within the remit of the SFO.<sup>1</sup> Likewise, if the NFT possesses features which provide real-world benefits (other than providing returns to holders), such as allowing attendance to certain charity events, this would also unlikely fall within the remit of the SFO.

The SFO regulates activities regarding securities and futures contracts, including in particular the regulated activity of “dealing in securities,” which is widely defined to include making (or offering to make) an agreement with another person, or inducing or attempting to induce another person to enter into an agreement (i) for or with a view to acquiring or disposing of “securities,” or (ii) the purpose of which is to secure a profit to any of the parties from the yield of securities or by reference to fluctuations in the value of securities. This would include any marketing and sales activities of securities. Accordingly, marketing or selling of crypto assets that fall within the definition of “securities” would be caught under the SFO, and if such activities are carried on as a business in Hong Kong, the person carrying out such activities would be required to be licensed by the Securities and Futures Commission (“SFC”), unless otherwise exempt. While one-off selling and marketing of securities crypto assets may potentially not be considered “carrying on a business” in a regulated activity, this will ultimately depend on the relevant factual circumstances. In particular, in 2017 the SFC issued a statement on initial coin offerings (“ICOs”) and requested an ICO issuer to halt its ICO over concerns that such issuer has engaged in potential unauthorized promotional activities and unlicensed regulated activities.<sup>2</sup>

### **Other Considerations**

While there are no laws and regulations with regard to accepting proceeds or royalties in relation to the sale of crypto assets, charities should bear in mind their obligations under laws relating to money laundering, terrorist financing, and sanctions as set out in section [2] above.

When collaborating with third-party partners in relation to creating and selling crypto assets, including NFTs, charities should also bear in mind any intellectual property rights implications to ensure there are arrangements in place to protect the charity’s rights in relation to the NFT’s underlying asset (e.g., art, music, videos, etc.), as well as ensuring that there are no infringements of intellectual property rights (e.g., selling of NFTs of art, music, and videos that are created or owned by other parties).

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<sup>1</sup> See circular issued by the Securities and Futures Commission (“SFC”): <https://apps.sfc.hk/edistributionWeb/gateway/EN/news-and-announcements/news/doc?refNo=22PR34>.

<sup>2</sup> See announcements made by the SFC: <https://www.sfc.hk/en/News-and-announcements/Policy-statements-and-announcements/Statement-on-initial-coin-offerings> and <https://apps.sfc.hk/edistributionWeb/gateway/EN/news-and-announcements/news/doc?refNo=18PR29>.

#### 4. Are there tax implications for donations of cryptocurrency or NFTs? Are there obligations to pay tax for charities who sell NFTs for fundraising purposes?



In principle, pursuant to DIPN No. 39 (revised) issued by the Inland Revenue Department of Hong Kong (“IRD”),<sup>3</sup> the IRD is of the view that the profits tax treatment of crypto assets would depend on the nature and use in each different scenario.

DIPN No. 39 has broadly classified crypto assets into the following three categories: (i) payment tokens which are used as a means of payment for goods or services, (ii) security tokens which provide the holder with particular interests and rights in a business and represent ownership interest in the business, and (iii) utility tokens which provide the holder with access to particular goods or services and the token issuer would normally commit to accepting the tokens as payment for the particular goods or services.

Generally speaking, any gain of a capital nature is not chargeable to Hong Kong profits tax. Pursuant to DIPN No. 39, for crypto assets, if these assets are purchased for long-term investment purposes, any profits derived from the disposal of such assets would not be chargeable to Hong Kong profits tax. The nature of such crypto assets would be determined based on the facts and circumstances surrounding the assets, having regard to degree, frequency of activity, and level of system and organization, and whether the purpose of the activity is in fact to make a profit. For example, the DIPN No. 39 provided that if digital tokens offered in an ICO represent equity or ownership interests in the issuer (i.e., security tokens), which is also known as a security token offering, the proceeds of the ICO would be capital in nature since the token holders would be given shareholders’ rights.

On the other hand, if digital tokens offered in an ICO give the token holders a right to future benefits (i.e., utility tokens) without any equity or ownership interests, such tokens would require the issuer to supply a good to or perform a service for the token holder. The proceeds of the ICO would be viewed as a prepayment for future goods or services, which may therefore be subject to profits tax. The timing of revenue recognition would depend on the details of the issuer’s performance obligations and should be determined in line with generally accepted accounting principles. Subject to any specific exemptions provided, profits arising in or derived from Hong Kong from the ICO can be charged to profits tax.

If a business is considered to be carried on, say by trading, exchanging, or mining assets, it will be only Hong Kong-sourced profits that are subject to profits tax.

There are no special tax rules relating to donations of crypto assets.

Certain charities registered with the IRD may qualify for profits tax exemption. Charities in Hong Kong may also refer to the “Tax Guide for Charitable Institutions and Trusts of a Public Character” issued by the IRD.<sup>4</sup>

<sup>3</sup> See <https://www.ird.gov.hk/eng/pdf/dipn39.pdf>.

<sup>4</sup> See [https://www.ird.gov.hk/eng/pdf/tax\\_guide\\_for\\_charities.pdf](https://www.ird.gov.hk/eng/pdf/tax_guide_for_charities.pdf).



## 5. What is the best practice or guidance?



Is there non-binding guidance issued by any regulatory or government authority or industry association in Hong Kong in relation to best practices relating to acceptance and issuance of cryptocurrencies and NFTs?

There are various charity-specific best practices guidelines, which charities should generally bear in mind when accepting cryptocurrencies as donations, including “An Advisory Guideline on Preventing the Misuse of Charities for Terrorist Financing” issued by the Narcotics Division of the Hong Kong Securities Bureau;<sup>5</sup> the “Best Practice Checklist – Management of Charities and Fund-Raising Activities” issued by the Independent Commission Against Corruption;<sup>6</sup> and “Good Practice Guide on Charitable Fund-raising” issued by the Social Welfare Department, the Home Affairs Department, and the Food and Environmental Hygiene Department of Hong Kong.<sup>7</sup>

For general guidance, charities may also reference the AMLO, which sets out anti-money laundering and counter-terrorist financing rules and obligations applicable to financial institutions and other high-risk institutions in Hong Kong. Various regulators and bodies who administer the AMLO, such as the SFC and the HKMA, have issued AML Guidelines to financial institutions. While AMLO and these AML Guidelines are generally not applicable to charities, the requirements and obligations to financial institutions and other high-risk institutions set out therein provide helpful guidance to charities when ensuring their compliance with the applicable anti-money laundering, counter-terrorist financing, and sanctions laws, including due diligence of donors on a risk-based approach, enhanced due diligence with regard to larger donations, and donations in connection with potential sanctions or politically exposed persons or other high-risk factors that are otherwise atypical, unusual, or suspicious in the experience of the charity, as well as record keeping. This is particularly important as cryptocurrency donations may be anonymous and may be subject to higher risks from an anti-money laundering, counter-terrorist financing, and sanctions perspective.

If charities have any questions as to whether crypto assets at hand are “securities,” they may consider reaching out to the SFC via the Fintech Contact Point,<sup>8</sup> which was established to enhance communication with businesses involved in the development and application of financial technology which intend to conduct regulated activities in Hong Kong.

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<sup>5</sup> See <https://www.sb.gov.hk/eng/special/moneylaundering/index.html>.

<sup>6</sup> See [https://cpas.icac.hk/UploadImages/InfoFile/cate\\_43/2016/a65540f5-91c5-46a8-8adf-7384e8c694b0.pdf](https://cpas.icac.hk/UploadImages/InfoFile/cate_43/2016/a65540f5-91c5-46a8-8adf-7384e8c694b0.pdf).

<sup>7</sup> See [https://www.gov.hk/en/theme/fundraising/docs/good\\_practice\\_guide.pdf](https://www.gov.hk/en/theme/fundraising/docs/good_practice_guide.pdf).

<sup>8</sup> See <https://www.sfc.hk/en/Welcome-to-the-Fintech-Contact-Point>.

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