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## **Non-Investment Finance in an NFT World**

**Joan MacLeod Heminway**

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# Non-Investment Finance in an NFT World

Joan MacLeod Heminway†

## Abstract

Recent years have witnessed the rise of NFTs as vehicles for non-investment finance, including in nonprofit and political fundraising. As with other financial sectors in which NFTs have a role, the use of NFTs in financing nonprofits and political campaigns and committees has revealed gaps and ambiguities in existing legal regulatory systems. Appetite exists to evolve legal frameworks to complete and clarify applicable bodies of law and regulation.

This chapter undertakes to illuminate and reflect on the use of NFTs in financing nonprofits, political campaigns, and political committees. It begins by reviewing general aspects of the non-investment Internet finance environment and then describes and illustrates the use of NFTs in nonprofit and political fundraising. The chapter also offers guidance and reflections on core issues under applicable law and regulation and reflections on legal and regulatory questions and approaches relevant to non-investment finance using NFTs.

## I. Introduction

Non-fungible tokens (NFTs)—the secure, digital assets minted, sold, and acquired on a blockchain that are the subject matter of this book—have grown in prominence and have received much attention in recent years. Ongoing efforts to modernize investment and other finance transactions have been a motivator of this trend. The deemed efficiencies in and other putative benefits of decentralized, automated funding transactions certainly have superficial appeal. However, the overall efficacy of blockchain finance remains questionable—in part because of unsettled policy and law.

Some of the other chapters in this handbook focus on the use of NFTs in investment finance—one piece of the NFT finance puzzle—an investment sector that invokes, perhaps most prominently, federal and state securities regulation as an actual or possible constraining force. Although some NFTs may be securities,<sup>1</sup> this chapter addresses the use of NFTs in financing transactions that do not involve the offer or sale of securities. Specifically, the ensuing pages address the use of NFTs in nonprofit<sup>2</sup> and political fundraising—financing environments governed

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<sup>1</sup> See, e.g., *Friel v. Dapper Labs, Inc.*, No. 21 CIV. 5837 (VM), 2023 WL 2162747, at \*22 (S.D.N.Y. Feb. 22, 2023).

(“Plaintiffs adequately allege that Dapper Labs’s offer of the NFT, Moments, was an offer of an ‘investment contract’ and therefore a ‘security,’ required to be registered with the SEC.”).

<sup>2</sup> The chapter uses the term “nonprofit” in a broad sense, for ease of reference, to denote to an enterprise organized as a nonprofit business association under state law, most of which also would be qualified as exempt from federal income tax under Section 501(a) of the Internal Revenue Code of 1986, as amended (the “IRC”). 26 U.S.C. § 501(a) (2018). However, the contents of this chapter are most likely to be relevant to organizations exempt from federal income taxes under Section 501(c)(3) of the IRC because they are operated exclusively for charitable or other qualified statutory purposes. 26 U.S.C. § 501(c)(3). References to “charitable” organizations may be read as references to all organizations operated for tax-exempt purposes enumerated in IRC § 501(c)(3).

by their own distinctive laws and regulations (as well as more generally applicable transactional laws).

There are several ways in which NFTs can be used to provide non-investment funding for nonprofits or political undertakings. NFTs can be sold to generate proceeds that can then be donated or contributed, or NFTs themselves can be donated if the nonprofit or campaign is willing to accept them. But other financing options—ones in which NFTs are more integral to the funding model for a nonprofit or campaign—are being employed with increasing frequency. Many of us have crowdfunded a project or cause in exchange for preferential access to a product or service, or for limited-edition merchandise or unique amenities. NFTs can serve as funding incentives in a similar manner.

With that in mind, this chapter focuses most closely on NFT offerings used to fund nonprofit organizations—especially charitable ventures—and political committees and campaigns. A fund-seeking entity or individual may create their own NFTs for this purpose. However, in current practice, it is more typical for a third-party NFT creator to generate an NFT or series of NFTs for the benefit of an enterprise seeking funding (selling or donating the NFTs to the enterprise for use in fundraising) or for an NFT creator to arrange with the enterprise to designate all or a portion of the proceeds of NFT sales (potentially proceeds from both the minting/initial sale and resale royalties) to the enterprise.

Ultimately, this chapter undertakes to offer a practical and applied legal context for, and related reflections on, this innovative use of NFTs as a matter of finance and law. To accomplish its purposes in the short order this format demands, the chapter begins with a brief précis of non-investment Internet finance—providing relevant background and regulatory context. The chapter then explains the use of NFTs in nonprofit and political fundraising. Finally, before concluding, the chapter offers observations on current legal and regulatory approaches to non-investment finance using NFTs.

## **II. Non-Investment Internet Finance**

The world of finance is deceptively broad. Individuals and entities require funding for many different types of endeavors, for personal or more broad-based benefit. Funders may be motivated to finance these endeavors in many ways. Taxonomies of the field take many different forms, based on the reference point of the observer. This chapter focuses on finance in the context of initiatives that do not exist to generate profit distributions—or even necessarily value appreciation—for funders. Rather, the finance settings addressed in this chapter relate to mission-focused financial support in the form of non-profit donations and political campaign contributions.

Not all financing of these undertakings takes place in the personal, negotiated contexts that exemplify traditional nonprofit and political fundraising. Non-investment finance using NFTs takes place in digital environments and therefore may be characterized as a type of Internet finance. A brief review of foundational Internet finance concepts provides useful background.

## A. Internet Fundraising for Projects and Causes

Not all promoters of endeavors have deep private networks of funders sufficient, when aggregated with other funding sources, to enable their enterprises to take shape, gain traction, and move forward operationally. Accordingly, promoters often seek funding from backers outside their existing networks. Those funders may not realistically or practically be financial institutions. They may be individuals.

Making connections with interested, engaged individual funders is not always easy, especially for start-up or early-stage ventures or for more narrowly focused projects or causes. As a result, intermediaries may be essential to making necessary connections. But finding the right intermediary also can be challenging, and the cost of securing the intermediary's services may be prohibitive.

With the World Wide Web's second generation—Web 2.0<sup>3</sup>—came the possibility and practicability of raising funds efficiently and effectively online. By combining social media and Internet commerce technologies (including online payment systems), entrepreneurs created online platforms that allow fund-seekers to connect with investors looking for funding opportunities by pointing and clicking. Internet finance—the solicitation of funding through these online platforms—was born and has rapidly increased in popularity since the early years of the 21<sup>st</sup> century.

## B. Crowdfunding as a Key Touchstone

Internet finance is exemplified by crowdfunding. Crowdfunding can be defined in many ways. For this chapter, crowdfunding is defined as the broad-based solicitation of pecuniary backing from an undifferentiated mass of individuals, typically in small per-investor increments, through an Internet-based platform. The fundraisers and funders may identify each other online or offline (although commonly the former), but the funding transaction takes place online.

Crowdfunding encompasses several different kinds of financing: investment (securities), presale, reward-based, and donative.<sup>4</sup> Nonprofit and political fundraising using NFTs has specific

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<sup>3</sup> See, e.g., Margaret Chon, *The Romantic Collective Author*, 14 VAND. J. ENT. & TECH. L. 829, 849 (2012) (“Web 2.0 refers primarily to a collection of digital network technologies that facilitate user-based interaction, in contrast to Web 1.0, which consists mostly of websites that do not allow or promote interactivity of content creation among decentralized Internet user-authors.” (citing Roggio, *infra*)); Armando Roggio, *Will Web3 Change Ecommerce?*, PRACTICALECOMMERCE, Dec. 24, 2021, <https://www.practicalecommerce.com/will-web3-change-ecommerce> (“Web 2.0 added interactivity and social media. It allowed just about anyone to create and share content. Web2 is what we use now for everything from Facebook to ecommerce. It is the ‘read-write’ web.”); Cecilia Ziniti, *The Optimal Liability System for Online Service Providers: How Zeran v. America Online Got It Right and Web 2.0 Proves It*, 23 BERKELEY TECH. L.J. 583, 591 (2008) (explaining that “[i]oosely defined, Web 2.0 embodies interactive service providers that leverage users’ collective intelligence and make the web, not the PC, ‘the platform that matters.’”).

<sup>4</sup> See, e.g., Steven Bradford, *The New Federal Crowdfunding Exemption: Promise Unfulfilled*, 40 SEC’S REG. L. J. 195, (2012) (describing these forms of crowdfunding); Joan MacLeod Heminway, *Securities Crowdfunding and Investor Protection*, 14 CESIFO DICE REPORT 11, 12 (2016), at <http://www.cesifo-group.de/ifoHome/publications/docbase/details.html?docid=19235734> ; Joan MacLeod Heminway, *The Legal Regulation of U.S. Crowdfunding: An Organically Evolving Patchwork*, in LEGAL ASPECTS OF CROWDFUNDING 271, 272-75

roots in donative and reward-based crowdfunding, respectively. Donative crowdfunding encompasses the solicitation of financing for a project or undertaking that the funder desires to support with a more altruistic intent. While the donor may be incentivized to give by a specific award (a t-shirt or a hat, for example), their primary desired return is merely the warm glow that they have provided financial backing to a worthy cause. Reward-based crowdfunding involves the solicitation of funding with the promise of a specific non-financial reward in return. For example, a backer may provide financial support to a nascent rock band to fund a set of marketable recordings of its music in return for front row seats to a local appearance. Both types of crowdfunding operate in similar ways and in ways analogous to NFT finance in the nonprofit and political contexts.

## 1. Key Practical Aspects and Processes of Crowdfunding

Crowdfunding is relatively simple in operation. Internet platforms are used to match prospective funders with those seeking funding.<sup>5</sup> Promotion typically occurs through a dedicated webpage on the platform (offering information about the entity or individual seeking funding and the nature of the project or cause), and the funding operates much like e-commerce: the platform accepts currency from funders, and (after taking a cut for itself) the platform passes along the remaining funds to the fundraiser. The conditions and terms of the exchange are explained on the platform, including in lengthy, standardized terms of use. Back-end payment systems (e.g., PayPal) handle the currency processing.

Non-investment crowdfunding platforms may specialize in particular types of financing. For example, GoFundMe (<https://www.gofundme.com>) is a well-established U.S. donative crowdfunding site. Similarly, Kickstarter (<https://www.kickstarter.com>) is a well-known U.S. crowdfunding platform that has been a long-standing player in pre-purchase and reward-based crowdfunding.

## 2. Bedrock Regulation of Crowdfunding

U.S. platforms engaged in interstate investment crowdfunding (multistate crowdfunding involving financial instruments defined as securities) are regulated at the federal level by the U.S. Securities and Exchange Commission (SEC) and the Financial Industry Regulatory Authority (FINRA). Their activities are constrained by federal securities law. Moreover, they are bound to federal disclosure rules and subject to legal actions and liabilities defined in and under federal securities law.

However, the online intermediation that facilitates non-investment crowdfunding is not regulated by any specific authority. Instead, depending on the type of financing, the platform itself and the activities conducted through it may be regulated under tax and other laws governing charitable solicitations and donations or contract and other laws relating to commercial

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(C. Kleiner, ed. 2018) [hereinafter *Legal Aspects*] (offering a slightly different taxonomy that covers the same types of financing, ordered in accordance with their regulatory context).

<sup>5</sup> See generally Joan MacLeod Heminway, *Intermediating Crowdfunding: A Foundational Assessment*, in STRATEGIC APPROACHES TO SUCCESSFUL CROWDFUNDING 34, 34-56 (Djamchid Assadi, ed., 2016) (explaining and categorizing crowdfunding intermediation, including by platforms).

transactions. Donative crowdfunding is more typically associated with eleemosynary fundraising that may implicate tax and charitable solicitation regulation, while reward-based crowdfunding is more centrally commercial and primarily engages contract and other commercial regulation (although donative crowdfunding also engages contract law, for example).<sup>6</sup>

### III. NFTs and Non-Investment Finance

NFTs are most widely used in non-investment crowdfunding as a funding incentive. In this way, they are much like the t-shirt or hat or event ticket that one may get for donating to a nonprofit or contributing to a political committee or campaign outside the blockchain context. They are a premium or reward for providing financing for the fund-seeking project or cause.

One might logically ask why an NFT has value as a reward for funding. The answer is the same in non-investment finance as it is in other contexts. NFTs have value because the person acquiring them believes they have value. Professor Brian Frye offers some relevant observations.

The value of an NFT seems to depend primarily on the popularity of the brand it represents. NFT collectors want to own NFTs associated with popular brands and want to associate themselves with those brands. That's why the most popular NFT collections are designed to be used as profile pictures or "PFPs." NFT collectors crave the clout of owning a popular NFT and PFP NFTs make it easy to show off.<sup>7</sup>

Professor Frye further suggests that the creator of the NFT matters in valuation because authorship is the basis for legitimacy, and legitimacy creates value.<sup>8</sup>

Similarly, observers note that NFTs, as an avowed Web 3.0 application,<sup>9</sup> create and exemplify a sense of community,<sup>10</sup> which may be especially important in non-investment finance.

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<sup>6</sup> See Heminway, *Legal Aspects*, *supra* note 4, at 275-80.

<sup>7</sup> Brian L. Frye, *NFTmarks*, ALTI FORUM (August 15, 2022), <https://alti.amsterdam/frye-nftmarks/> (last visited June 9, 2023).

<sup>8</sup> *Id.* ("NFTs collectors value NFTs based on the works of art they represent. However, NFT collectors only value NFTs they consider legitimate, and the perceived legitimacy of an NFT usually depends on who created it.").

<sup>9</sup> See JoHanna Cox, *Money's Future in Web 3.0*, ABA SciTECH LAW., Winter 2023, at 12, 13 ("The Web 3.0 era . . . incorporates more cryptocurrencies, NFTs, and related items. . . . [U]sers and a broader network of people will direct content and information available on the web."); Orly Lobel, *The Law of the Platform*, 101 MINN. L. REV. 87, 96 (2016) ("[T]he rise of the platform signifies the third generation of the Internet, Web 3.0, in which technology is transforming the service economy, allowing greater access to offline exchanges for lower prices. In turn, the physical infrastructure of offline markets is itself transformed by the technological infrastructure." (footnote omitted)).

<sup>10</sup> See Joshua A.T. Fairfield, *Making Virtual Things*, 64 WM. & MARY L. REV. 1057, 1077-78 (2023) ("People get involved with cryptocurrency or NFTs, they do not merely invest. And most NFTs find meaning within a community that generates interest in their value." (footnote omitted)); Stacey M. Lantagne, *Of Disaster Girl and Everyday: How NFTs Invite Challenging Copyright Assumptions Around Creator Support*, 13 HARV. J. SPORTS & ENT. L. 265, 291 (2022) ("The community aspect drives people to purchase your NFTs out of a desire to support you and belong to your digital community."); Kevin McCoy, *Art and NFTs: Past and Future*, 45 COLUM. J.L. & ARTS 353, 358 (2022) ("Community is another important aspect of the NFT phenomenon's future. NFTs are going to drive community participation as markers of common interests and common goals."); Mark Radcliffe & Katherine M. Imp, *Top Billing for NFTs*, L.A. LAW., May 2022, at 20, 22 ("NFT communities . . . enable community members to collaborate with the lead artist or

Those who are attracted by NFT offerings to funding nonprofits and campaigns may be seeking a community of like-minded financial contributors—people who, like them, support a specific kind of project or cause. Discord, a server-based social connection tool,<sup>11</sup> or another similar application may be used to facilitate NFT communities for a variety of purposes.<sup>12</sup> For example:

NFT projects that want to make a charitable donation will hold a vote among their fans and supporters to choose which nonprofit organization(s) to support. Conversations like these usually happen in digital spaces like Discord or Twitter, where project leaders can engage in a direct dialogue and users easily participate in the discussions.<sup>13</sup>

A blog post affiliated with Numero (<https://numero.ai/>), an Internet-based tool for campaign fundraising, notes more generally that “one of the less obvious — but more powerful — benefits of using NFTs for campaign fundraising is to help build stronger grassroots communities.”<sup>14</sup>

Based on the forgoing, it is clear that the use of NFTs (rather than tangible goods or experiences) as rewards in non-investment internet finance is designed to attract specific—and likely new—funding audiences.<sup>15</sup> Those audiences may include fans of the artist, NFT collectors more generally, or millennials, for example.<sup>16</sup> As a result, enterprises considering the use of NFTs as financing perks should want to understand relevant facts about their target demographics.

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other community members, share ideas, provide guidance about a project's ‘roadmap,’ introduce community members to other projects, and encourage purchases of new works, either of the leading artist or other projects.”)

<sup>11</sup> See *What is Discord?*, DISCORD, <https://discord.com/safety/360044149331-What-is-Discord> (last visited June 23, 2023); see also *Community Building 101: Curating and Cultivating a Space Using Discord*, TILTIIFY, Aug. 5, 2021, <https://blog.tiltify.com/community-building-101-curating-and-cultivating-a-space-using-discord-6f37b0bc6aaa> (“Discord is a free voice, video, and text chat app used by thousands of streamers and organizations worldwide to arrange meet-ups, build communities, exchange ideas, or afford people a space to gather and collaborate. It functions similar to Microsoft Teams, Cisco Jabber, Slack or, AOL Instant Messenger . . . where people type and share into a chat room real time.” (hypertext link removed)).

<sup>12</sup> Wee Min, *Put on the Spot: Damien Hirst's the Currency and the Future of NFTs*, 26 VA. J.L. & TECH. 1, 20 (2022) (“[T]he ownership of NFTs can create relationships between the NFT owner and the artist as well as among the community of NFT owners through Discord servers.”); Michael D. Murray, *NFTs and the Art World - What's Real, and What's Not*, 29 UCLA ENT. L. REV. 25, 57 n.187 (2022) (“Discord is a social media messaging app that has become popular with the crypto and NFT community in part because it is decentralized and therefore matches the ethos of the blockchain world.”).

<sup>13</sup> THE GIVING BLOCK, *THE RISE OF NFT FUNDRAISING 12*, available at <https://thegivingblock.com/nft-fundraising-report/> (last visited June 20, 2023) [hereinafter NFT FUNDRAISING].

<sup>14</sup> Brian Forde, *How NFTs Can Help Political Campaigns Build Stronger Communities*, NUMERO, Mar. 16, 2022, <https://numero.ai/blog/how-nfts-can-help-political-campaigns-build-stronger-communities/> (hypertext link removed); see also Laura Romero & Soo Rin Kim, *Not just for artwork, NFTs are being used by political candidates to raise money, attract young supporters*, ABC NEWS, Jan. 26, 2022, <https://abcnews.go.com/Politics/artwork-nfts-political-candidates-raise-money-attract-young/story?id=82445596> (quoting Vanderbilt University finance professor Joshua White: “NFTs can build a community where there's this positive feedback loop.”).

<sup>15</sup> NFT FUNDRAISING, *supra* note 13, at 6 (“[C]rypto and NFT donors are a distinct audience from their cash-donating peers, with their own set of values when it comes to personal finance and philanthropy.”).

<sup>16</sup> See Nest, *Political Fund Raising and the Use of NFTs*, MEDIUM, May 16, 2023, <https://nes-tech.medium.com/political-fund-raising-and-the-use-of-nfts-a5ee2579d313> (“NFTs can potentially attract young voters in the context of political fundraising.”).



## A. *The Role of NFTs in Non-Investment Finance*

NFTs can be used to generate donations for nonprofits and political campaigns in several different ways. Among the models observed in (or anticipated based on) research conducted for this chapter, several methods emerged as popular. The models identified are distinguishable primarily based on the relationship between the NFT creator and the nonprofit or campaign seeking funding.

For example, staff of the nonprofit or campaign may create their own NFTs for the enterprise as works-for-hire.<sup>17</sup> The nonprofit or campaign also may commission the creation of NFTs by third parties. The nonprofit or campaign would own of the NFTs in either such case and be able to offer them to donors or contributors as a premium or, if and as legally permissible, sell them outright to collectors.

More commonly, nonprofits and campaigns will partner with related or unrelated third parties that create, mint, and sell the NFTs as a funding incentive. A nonprofit or campaign may join with an NFT creator to promote the sale of dedicated NFTs or to conduct an auction on an NFT platform. Alternatively, a platform used by a nonprofit to raise funds through cryptocurrency donations may partner with an NFT artist to create, mint, and sell NFTs for the financial benefit of the nonprofit, acting as a relational intermediary.

NFT creators or projects also may independently mint and sell NFTs and establish smart contracts to make donations of sale or royalty proceeds to one or more recipients.<sup>18</sup> Similarly, a collector of NFTs may sell an NFT and designate all or a portion of the cryptocurrency proceeds received to a nonprofit or campaign.<sup>19</sup> Alternatively, a collector may donate an NFT directly to a nonprofit or campaign (assuming the donee will accept an NFT donation).<sup>20</sup> These donative asset transfers are comparable to asset transfers occurring outside the NFT context. However, blockchain technology facilitates the execution of the aggregate transactions necessary to convert the asset into a donation or contribution.

A review of the use of NFTs in nonprofit and campaign finance reveals that nonprofit funding initiatives are more prevalent, more innovative, and more diverse. Although NFTs were

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<sup>17</sup> One might imagine that few nonprofits or campaigns have NFT artists on staff. Accordingly, this self-generated-NFT model may more likely feature photographic or other graphic images related to the mission or operations of the fund-seeking nonprofit or associated with the campaign candidate.

<sup>18</sup> See *id.* (“Artists Matthew Weitzman and David Fugit, together with photographer Jon Luvelli, are partnering on canine NFT collectibles in order to donate proceeds to animal rescue groups such as New York Bully Crew, a charity that rescues pit bulls and other animals in need.”).

<sup>19</sup> See Gary P. Kohn, *NFTs and the Law*, L.A. LAW., November 2021, at 18, 21 (“New York Mets slugger Pete Alonso sold an NFT and donated the proceeds to More Than Baseball, a nonprofit supporting minor league baseball players in need of housing, equipment, and nutrition, and to his own charity, Homers for Heroes, whose mission is “to recognize the outstanding work of our heroes and inspire others to be a hero in others' lives.” (footnotes omitted)).

<sup>20</sup> Cryptocurrency donative crowdfunding platform The Giving Block notes in a recent report that “[n]onprofits should be cautious when accepting NFTs themselves as donations, because many organizations have restrictions on accepting property-like assets.” NFT FUNDRAISING, *supra* note 13, at 33; see also *id.* at 15 (“Accepting an NFT is very different from accepting a typical fiat or cryptocurrency donation.”).

used to help generate funding for Texas Democrats and New Jersey Republicans generally,<sup>21</sup> published reports indicate that as few as five political candidates may have used NFTs in their fundraising campaigns. To better illustrate how NFTs have been used to date in non-investment financings, examples of actual fundraising campaigns involving nonprofits and political campaigns may be beneficial.

## B. *Nonprofit NFT Fundraising*

Fundraising using NFTs has been a growing finance market for nonprofits.<sup>22</sup> “Minting new NFTs can serve as an additional stream for regular ol’ fundraising. Someone buys an NFT from your nonprofit—or an NFT artist you’ve partnered with—and your org receives a donation.”<sup>23</sup> Exemplar campaigns illustrate more specifically the ways in which this type of a nonprofit fundraising is conducted.

Corporations may sell NFTs and donate the proceeds of those sales to their associated charitable foundations. For example, through its website <http://www.worldofverabradley.com>, Vera Bradley marketed and sold two series of NFTs: The Heritage Pass (“a standardized token featuring dynamic imagery of the iconic Jilly Bag in four heritage prints”) and The 1982 Collection (“hand-drawn layers of art that share the same hallmarks as Vera Bradley’s prints: optimism, happiness, charm, energy and joy”).<sup>24</sup> The website indicates that, through its VB Cares initiative, Vera Bradley, Inc.—a for-profit corporation—was to donate all of the primary net proceeds from the two NFT series to The Vera Bradley Foundation for Breast Cancer, a charitable foundation associated with Vera Bradley Inc.<sup>25</sup> The creators of the NFTs are not disclosed, but the NFTs feature images and digital art based on Vera Bradley products and textiles.

Similarly, a year earlier, Taco Bell, a division of for-profit YUM! Brands, Inc. commissioned the creation of five NFTs with fast-food themes.<sup>26</sup> Minted and sold on the Rarible

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<sup>21</sup> Gopal Ratnam, *Nonfungible tokens the new fad for campaign fundraising*, ROLL CALL, Jan. 4, 2022, <https://rollcall.com/2022/01/04/non-fungible-tokens-the-new-fad-for-campaign-fundraising/> (“In October, a group of Democratic fundraisers banded together to launch politically themed NFTs through a marketplace called Front Row to raise money for Texas Democrats.”); Fred Snowflack, *The Reason for Laura Ali’s Confidence*, INSIDER NJ, Jan. 24, 2022, <https://www.insidernj.com/reason-laura-alis-confidence/> (describing the forthcoming Morris County Republican Committee NFT fundraising campaign in January 2022).

<sup>22</sup> See THE GIVING BLOCK, CRYPTO PHILANTHROPY DATA, TRENDS & PREDICTIONS 22, available at <https://go.thegivingblock.com/hubfs/Annual%20Report/2023%20Annual%20Report%20on%20Crypto%20Philanthropy.pdf>? (“In 2021, NFT fundraisers emerged as a trend, and we helped raise tens of millions of dollars for charities via creators auctioning off their web3 artwork . . . . In 2022, NFT philanthropy remained a multimillion dollar philanthropic channel for charities on our platform . . . .”).

<sup>23</sup> Emily Kostic, *What Could NFTs Mean for Nonprofits?*, AD COUNCIL, March 2, 2022, <https://www.adcouncil.org/all-articles/what-could-nfts-mean-for-nonprofits?>.

<sup>24</sup> Explore the World of Vera Bradley, <https://worldofverabradley.com/> (last visited June 22, 2023).

<sup>25</sup> *Id.*

<sup>26</sup> See, e.g., Mitchell Clark, *The brands are at it again — Taco Bell is hopping on the NFT train*, THE VERGE, Mar. 8, 2021, <https://www.theverge.com/2021/3/8/22319868/taco-bell-nfts-gif-tacos-sell>; Jamie Crawley, *Taco Bell Just Sold a Collection of 5 Fast-Food-Themed NFTs*, COINDESK, Mar. 9, 2021, <https://www.coindesk.com/business/2021/03/09/taco-bell-just-sold-a-collection-of-5-fast-food-themed-nfts/>; David Gianatasio, *Taco Bell Draws on the NFT Craze for Digital Art Sale*, MUSE BY CLIO, Mar. 11, 2021, <https://musebyclio.io/art/taco-bell-draws-nft-craze-digital-art-sale>.

platform (<https://rarible.com/tacobell>), the Taco Bell NFTs were offered at a price of \$1.00 each and sold out in 30 minutes,<sup>27</sup> with proceeds to be donated to the Taco Bell Foundation to support young adults' education initiatives and career-readiness.<sup>28</sup>

The Giving Block (<https://thegivingblock.com/>), a cryptocurrency fundraising platform for nonprofits, labels financing initiatives like those used by Vera Bradley and Taco Bell “corporate giving partnerships.”<sup>29</sup> The Vera Bradley and Taco Bell campaigns were both designed to fund nonprofits associated with those for-profit businesses. However, The Giving Block notes that corporate donors also may employ this strategy for unrelated nonprofits, offering The Coca-Cola Company's NFT-based fundraising campaign benefitting the Special Olympics as an example.<sup>30</sup> In all of these cases, the corporate partner sells NFTs and donates the proceeds to the nonprofit.

The Coca-Cola campaign was structured as an online auction. NFT auctions are a specific way that nonprofits use the Internet and blockchains to incentivize fundraising. Third parties may conduct auctions on NFT platforms to benefit nonprofits, or nonprofits may conduct their own auctions through NFT platforms if they are legally permitted to sell the NFTs being offered.

The Giving Block offers NFT auction services to nonprofits. An online article explains the concept.

The most common way of using NFTs for fundraising is no different than how we auction off pieces of art today. The only difference is that these pieces of art live on the blockchain as NFTs. For example, Nifty Gateway sold eight unique pieces donated by artists, and over \$6.6 million was raised for the Open Earth Foundation. The new owners of those pieces can prove their ownership via the blockchain.<sup>31</sup>

Thus, NFT auctions for the benefit of nonprofits work much the same way as charitable auctions of nondigital assets. In describing the general process of establishing an NFT auction of this kind, The Giving Block asserts that “[a]n NFT charity auction is one of the most exciting ways to fundraise with NFTs. It requires extensive planning, but the results can often be well worth the effort.”<sup>32</sup>

Blockchain-engaged crowdfunding platforms also have been a key partner for nonprofits in their NFT fundraising campaigns. For example, the Panxpan platform (<https://www.panxpan.com>) promotes its NFT fundraising services to nonprofits by directly linking them to both traditional nonprofit fundraising and non-NFT Internet financing activities

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<sup>27</sup> See Clark, *supra* note 26; Gianatasio, *supra* note 26.

<sup>28</sup> See Clark, *supra* note 26; Crawley, *supra* note 26; Mitchell, *supra* note 20; *Taco Bell*, RARIBLE, <https://rarible.com/tacobell/owned> (last visited June 20, 2023).

<sup>29</sup> *Nonprofits & NFTs Explained: A New Vision for Charitable Fundraising*, Oct. 12, 2021, <https://thegivingblock.com/resources/nonprofits-nfts-explained-a-new-vision-for-charitable-fundraising/>.

<sup>30</sup> *Id.* (“Recently, Coca-Cola partnered with the 3D artists at Tafi to auction off special-edition NFT ‘loot boxes,’ resulting in [\\$575,883.61 donated to the Special Olympics](#).” (emphasis removed)).

<sup>31</sup> *Opinion: 3 Reasons Why NFTs Will Shape the Future of Nonprofit Fundraising*, Oct. 6, 2022, <https://thegivingblock.com/resources/opinion-3-reasons-why-nfts-will-shape-the-future-of-nonprofit-fundraising/> (emphasis and hypertext link removed).

<sup>32</sup> NFT FUNDRAISING, *supra* note 13, at 16.

for nonprofits. On its website, Panxpan encourages nonprofits to sign-up for its services by noting the expense of traditional giveaways in relation to the generated funds.<sup>33</sup> Later on the homepage, under the heading “Digital Collectible,” Panxpan explains how campaigns are executed:

Give your fundraising participants a digital collectible (NFT) based on their donation tier. Its [sp] something real they can keep, transfer or sell. It also enables all the NFT token gated experiences that you can offer participants.<sup>34</sup>

Panxpan’s services to nonprofits include establishing a fundraising webpage and creating and managing the NFTs.<sup>35</sup> Panxpan’s services, taken together, effectively constitute reward-based crowdfunding using NFTs as the reward.

Nonprofit fundraising using NFTs is not all sunshine and rainbows,<sup>36</sup> however. The World Wildlife Fund in the United Kingdom discontinued an NFT offering (the “Tokens for Nature” collection) in response to public outcry about the negative environmental effects of the offering.<sup>37</sup> Although The World Wildlife Fund in Germany nevertheless continues to offer its Non-Fungible Animals NFTs,<sup>38</sup> the criticism of that offering is much the same.<sup>39</sup>

### C. NFT Political Campaign and Committee Finance

Typically, the use of NFTs in political campaign finance is quite straightforward. The campaign uses pre-existing art (or other content), generates NFT content on its own, or contracts for content and creates or purchases the related NFT. The NFT is then offered to campaign contributors at a fixed price or through bidding or another pricing process.

A summary of the five political campaigns identified in the research conducted for this chapter offers a quick snapshot of political campaign finance efforts.<sup>40</sup>

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<sup>33</sup> Fundraise using NFTs, <https://www.panxpan.com/> (last visited June 22, 2023) (“Many of us have tried chocolates, t-shirts and hats. There are a lot of giveaways [sp] you can try but they usually take most of the funds raised. Consider using NFTs to drive engagement and keep 100% of your funds raised.” (emphasis removed)).

<sup>34</sup> *Id.*

<sup>35</sup> *See id.*

<sup>36</sup> *See life isn't all sunshine and rainbows*, FREE DICTIONARY BY FARLEX, <https://idioms.thefreedictionary.com/life+isn%27t+all+sunshine+and+rainbows> (last visited June 22, 2023) (“Real life does not just consist of innocent, carefree happiness; there is more hardship or suffering in reality than one realizes.”).

<sup>37</sup> *See* Justine Calma, *How the World Wildlife Fund tried — and failed — to create an eco-friendly NFT*, VERGE, Feb. 8, 2022, <https://www.theverge.com/2022/2/8/22923530/world-wildlife-fund-nft-polygon-layer-2-blockchain-energy-emissions>; Rosie Frost, *WWF decision to sell NFTs labelled ‘astonishingly stupid’ by environmentalists*, EURONEWS.GREEN, Mar. 20, 2022, <https://www.euronews.com/green/2022/02/03/wwf-decision-to-sell-nfts-labelled-astonishingly-stupid-by-environmentalists>; Adam Hunt, *The World Wildlife Fund has canceled its NFT project after only a day*, TWEAKTOWN, Feb. 10, 2022 (updated Mar 8, 2022), <https://www.tweaktown.com/news/84503/the-world-wildlife-fund-has-canceled-its-nft-project-after-only-day/index.html>.

<sup>38</sup> *NFA Non-Fungible Animals - The NFT campaign by WWF*, <https://wwf-nft.com/> (last visited June 22, 2023).

<sup>39</sup> *See* Calma, *supra* note 37; Hunt, *supra* note 37.

<sup>40</sup> Information included in the chart was obtained from various news media sources. *See, e.g.*, Marvelous Akpere, *NFTs to fund US election*, CRYPTOTVPLUS, June 21, 2022, <https://cryptotvplus.com/2022/06/nfts-to-fund-us-election/>; Teresa Mettela, *Political Hopefuls Turn to NFTs to*

Candidate	State	Party	Office	NFT Offering	Price/ NFT	Launch Date
Scott Jensen	Minnesota	Republican	Governor	Digital images of Jensen at the state fair eating a corn dog or carrying a cow	\$5	August 2021
Shrina Kurani (two NFT offerings)	California	Democratic	U.S. House of Representatives	Digital representations of Kurani’s crypto policy agenda, including “vision and concept statements”; access to free digital assets from crypto and climate projects, communications with climate experts, and a metaverse Earth Day party	minimum bid of \$200, maximum of \$5,800; \$1,250 and \$5,800	December 2021; March 2022
Blake Masters	Arizona	Republican	U.S. Senate	Limited edition digital images of early cover art for Masters’s coauthored book (with Peter Thiel), <i>Zero to One</i>	\$5,800	December 2021
Steven Olikara	Wisconsin	Democratic	U.S. Senate	Tokenized portraits of Olikara	\$50	March 2022
Jared Polis	Colorado	Democrat	Governor	Digital images of a variety of objects relevant to Polis’s candidacy or the state (including sneakers, a chili pepper, mountains, and his dog, Gia, depicted with lasers coming from her eyes)	\$52.80	June 2022

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Raise Funds for Midterm Elections, WALL ST. J., May 14, 2022, <https://www.wsj.com/articles/political-hopefuls-turn-to-nfts-to-raise-funds-for-midterm-elections-11652520603> (subscription required); Reethu Ravi, *Shrina Kurani is Running for Congress to Teach Average Americans About Web3*, NTFEVENING, Dec. 26, 2021 (updated Feb. 1, 2023), <https://nftevening.com/shrina-kurani-is-running-for-congress-to-teach-average-americans-about-web3/>; Felix Salmon, *Exclusive: Colorado Governor Jared Polis fundraises with NFTs*, AXIOS DENVER, June 13, 2022, <https://www.axios.com/local/denver/2022/06/13/colorado-governor-jared-polis-fundraises-nfts>; Ben Strack, *Congressional Candidate Uses NFTs To Raise Awareness, Funds*, BLOCKWORKS, Mar. 14, 2022, <https://blockworks.co/news/congressional-candidate-uses-nfts-to-raise-awareness-funds>; Eli Tan, *Candidate for Minnesota Governor Releases Campaign NFTs*, COINDESK, Sept. 1, 2021 (updated May 11, 2023), <https://www.coindesk.com/business/2021/09/01/candidate-for-minnesota-governor-releases-campaign-nfts/>; David Thomas, *NFTs Gaining Popularity as Fundraising Method in Election Campaigns*, BEINCRYPTO, Jan. 10, 2022, <https://beincrypto.com/nfts-gaining-popularity-as-fundraising-method-in-election-campaigns/>.

The NFTs offered in these campaigns vary in content and price. Some “also come with real-life perks and exclusive access to events, which makes them attractive as campaign offerings.”<sup>41</sup>

Political committees also have been experimenting with NFT offerings. In the fall of 2021, NFT platform Front Row sold NFTs for the benefit of the Texas Democratic Party (the Lonestar Collection).<sup>42</sup> In New Jersey, the Morris County GOP has been offering and selling NFTs since the last week of January in 2022.<sup>43</sup> Despite initial optimism about sell-throughs,<sup>44</sup> few NFTs have been sold (although the sales reportedly made total \$17,500).<sup>45</sup> NFT political donation platforms like Electables (<https://www.electables.com/>)—which was created “specifically for Democratic campaign grassroots fundraising”<sup>46</sup>—are emerging that are designed to deliver comprehensive NFT fundraising services to campaigns. However, overall, campaign finance NFT platforms and sites have been slow to develop.

There are discernible advantages to using NFTs to encourage donations to political campaigns.<sup>47</sup> However, NFT campaign finance is not for everyone. Cautionary notes include regulatory ambiguities, skepticism about NFTs among campaign donors, uncertain connections between candidates and the NFT/crypto community, and distractions from more profitable,

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<sup>41</sup> Laura Romero & Soo Rin Kim, *Not just for artwork, NFTs are being used by political candidates to raise money, attract young supporters*, ABC NEWS, Jan. 26, 2022, <https://abcnews.go.com/Politics/artwork-nfts-political-candidates-raise-money-attract-young/story?id=82445596>; see, e.g., *id.* (“[F]or those who purchased Masters’ digital tokens, the perks included receiving a signed copy of his book and the opportunity to meet him and his co-author, tech billionaire Peter Thiel, who helped develop the NFT collection.” (hypertext link removed)); Salmon, *supra* note 40 (“Polis’ NFTs will act as tickets to get donors into events, Brian Forde, CEO of Democratic fundraiser Numero, tells Axios.” (emphasis removed)); Tan, *supra* note 40 (“Purchasing one of the [Jensen] NFTs unlocks access to a rewards program of prizes throughout the campaign, such as the opportunity to meet Jensen and watch a Minnesota Vikings football game with former Viking Matt Birk”).

<sup>42</sup> See Ben Davis, *Beeple Is Probably Right That NFTs Will Change Politics. So Far, That Change Is for the Worse*, ARTNET NEWS, Feb. 10, 2022, <https://news.artnet.com/opinion/political-nfts-blake-masters-zero-to-one-2070585>; Savannah Fortis, *Democratic Party Politicians Turning to NFTs to Raise Funds*, BEINCRYPTO, Oct. 11, 2021, <https://beincrypto.com/democratic-party-politicians-turning-nfts-raise-funds/>; Rachel Janfaza, *Goodbye campaign buttons, hello NFTs: Democrats turn to internet phenomenon to raise money*, CNN, Oct. 15, 2021, <https://www.cnn.com/2021/10/15/politics/democrats-fundraising-nfts-cryptocurrency/index.html#>.

<sup>43</sup> See Snowflack, *supra* note 21 (indicating that the NFT fundraising campaign began on Thursday, January 27, 2022); *The First Political Committee to Reward Donors with Limited Edition Digital NFT Collectibles*, MORRIS COUNTY GOP NFTs, <https://nft.morrisgop.org/> [hereinafter *First Political Committee*] (last visited June 24, 2023) (Morris County’s NFT fundraising site, showing the current status of Morris County’s NFT sales).

<sup>44</sup> See Snowflack, *supra* note 21 (“Ali is brimming with confidence. She said she expects all the tokens to be sold by the end of this week.”).

<sup>45</sup> See *First Political Committee*, *supra* note 43 (substantiating the sale of 11 of 39 MCRC Platinum Club tokens for \$1000 each, 16 of 199 MCRC Gold Club tokens for \$300 each, five of 100 Turn New Jersey Red tokens for \$100 each, and 24 of 500 Take Back New Jersey tokens for \$50 each, evidencing donations totaling \$17,500).

<sup>46</sup> Frequently Asked Questions: What is Electables, *Grassroots Fundraising with NFTs*, <https://www.electables.com/> (last visited June 25, 2023).

<sup>47</sup> See Frequently Asked Questions: Why should I buy an NFT instead of making a regular donation?, *Grassroots Fundraising with NFTs*, <https://www.electables.com/> (last visited June 25, 2023). (“NFTs . . . are verifiable proof that you were early and right in your support. They give you access and insight into campaigns . . . . They also are a platform for you to raise with your friends and the results of your collective action.”); Nest, *supra* note 16 (“NFTs have the potential to revolutionize political fundraising, offering benefits like better perks, easy access, lower costs, and the ability to attract younger voters.”).



efficient campaign fundraising tactics.<sup>48</sup> Although one commentator offers tips for using crypto and NFTs in political campaign finance, he also advises that “most campaigns should not try this.”<sup>49</sup>

#### IV. The Legal and Regulatory Environment for Non-Investment Finance Using NFTs

The law governing NFTs and transactions involving them is contextual and multifaceted. While the use of NFTs in non-investment finance does not (as simply employed) engage the application of federal or state securities law, other general and specialized areas of law may be applicable to NFT offerings based on the nature of the NFT being offered and the circumstances in which the NFT is offered. Nevertheless, there are some basic legal and regulatory systems that impact all non-investment finance conducted through NFT offerings.

The acquisition and disposition of NFTs is, at base, a commercial transaction, as are the accompanying arrangements (including through website terms of use) made by and among the NFT artists, platforms, payment system providers, and others involved in NFT offerings. Accordingly, contract law, commercial law, consumer protection law, federal and state anti-fraud laws of various kinds, and other laws governing asset transfers may apply in regulating conduct and resolving controversies. Because “[a]n NFT represents . . . typically ‘ownership’ of a digital image”<sup>50</sup> or another underlying asset, legal issues and disputes also may arise under property law, most commonly intellectual property law. Much of this general legal and regulatory ground has been trod to some extent by those involved with non-investment finance accomplished through donative and reward-based crowdfunding, although the application of these foundational areas of law and regulation in the NFT context may not be straightforward.<sup>51</sup>

U.S. federal and state income tax and election law and regulation also play foundational roles in nonprofit and political finance involving NFTs. The application of state income tax and election laws involves a fifty-state analysis that is beyond the scope of this chapter. Many (but by no means all) state income tax and election laws have similar policy reference points and, therefore, may follow principles established in or under federal law. In some cases, federal law preempts state law.

From a federal income tax perspective, NFTs (as digital representations of rights to various types of assets) are treated as property. Accordingly, the minting, sale, and resale of NFTs may result in taxable income, gain, or loss to the creator or reseller.<sup>52</sup> NFTs may be goods or capital assets, depending on the holder and the context.<sup>53</sup> The U.S. Internal Revenue Service (IRS) has

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<sup>48</sup> Joe Fuld, *Crypto for Political Campaigns and NFTs For Fundraising*, CAMPAIGN WORKSHOP, Apr. 11, 2022, <https://www.thecampaignworkshop.com/blog/political-campaign/crypto-political-campaigns>.

<sup>49</sup> *Id.*

<sup>50</sup> Frye, *supra* note 7.

<sup>51</sup> See Heminway, *Legal Aspects*, *supra* note 4, at 275-80; Lloyd Hitoshi Mayer, *Regulating Charitable Crowdfunding*, 97 IND. L.J. 1375, 1399-1419 (2022) (describing laws currently applicable to charitable crowdfunding).

<sup>52</sup> See I.R.S., *Digital Assets*, <https://www.irs.gov/businesses/small-businesses-self-employed/digital-assets> (last visited June 25, 2023).

<sup>53</sup> See McDermott Will & Emery, *Taxation of the Purchase and Sale of NFTs*, Jan. 11, 2022, <https://www.mwe.com/insights/taxation-of-the-purchase-and-sale-of-nfts/> (“In the hands of creators of and

also recently identified NFTs as potential collectibles.<sup>54</sup> Among other things, the sale or exchange of property designated as a collectible under federal tax law and IRS guidance “that is a capital asset held for more than one year is subject to a maximum 28% capital gains tax rate (while an asset that is not a collectible is generally subject to a lower maximum long-term capital gains tax rate).”<sup>55</sup>

Although NFT transactions can be executed for cash, they are more typically conducted using cryptocurrencies. Convertible cryptocurrencies typically are considered investment property (and therefore capital assets) under applied IRS guidance.

A taxpayer generally realizes capital gain or loss on the sale or exchange of virtual currency that is a capital asset in the hands of the taxpayer. For example, stocks, bonds, and other investment property are generally capital assets. A taxpayer generally realizes ordinary gain or loss on the sale or exchange of virtual currency that is not a capital asset in the hands of the taxpayer. Inventory and other property held mainly for sale to customers in a trade or business are examples of property that is not a capital asset.<sup>56</sup>

Thus, if a donor to a nonprofit or contributor to a political campaign or committee is required to convert cryptocurrency into dollars before donating or contributing, the donor will be engaging in a taxable transaction and will be required to pay taxes on any gain, decreasing the probability or value of the donation or contribution. Accordingly, it may behoove nonprofits and political campaigns or committees to position themselves to accept cryptocurrencies as well as dollars if they intend to raise funds through NFT sale or royalty proceeds.

Taxpayers must report the receipt, sale, exchange, gift, or other disposition of digital assets (including NFTs and cryptocurrencies) as well as any income, gain, or loss from those transactions to the IRS.<sup>57</sup> Separate IRS reporting may be required in connection with certain types of transactions. For example, the transfer of an NFT that constitutes a gift for federal income tax purposes must be reported if the fair market value of the NFT exceeds the then-current amount of the donor’s applicable annual gift exclusion.<sup>58</sup>

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dealers in NFTs, NFTs are ordinary assets. Such taxpayers have ordinary income and loss on their NFT transactions.”); *id.* (“NFTs held by traders, investors, collectors and personal users are treated as capital assets. Short-term capital assets are those that are held for one year or less, while long-term capital assets are held for more than one year.”).  
<sup>54</sup> See I.R.S. Notice 2023-27 I.R.B. 634, Treatment of certain nonfungible tokens as collectibles (March 21, 2023), available at <https://www.irs.gov/pub/irs-drop/n-23-27.pdf>; IR-2023-50, *IRS issues guidance, seeks comments on nonfungible tokens* (March 21, 2023), <https://www.irs.gov/newsroom/irs-issues-guidance-seeks-comments-on-nonfungible-tokens>.

<sup>55</sup> I.R.S. Notice 2023-27 2023-15 I.R.B. 634, Treatment of certain nonfungible tokens as collectibles (March 21, 2023), available at <https://www.irs.gov/pub/irs-drop/n-23-27.pdf>.

<sup>56</sup> I.R.S. Notice 2014-16 I.R.B. 938 (March 26, 2014), available at <https://www.irs.gov/pub/irs-drop/n-14-21.pdf> (modified in other respects by I.R.S. Notice 2023-34 I.R.B. 837, Modification of Notice 2014-21 (Apr. 24, 2023), available at <https://www.irs.gov/pub/irs-drop/n-23-34.pdf>).

<sup>57</sup> See IR-2023-12, *IRS: Updates to question on digital assets; taxpayers should continue to report all digital asset income* (January 24, 2023),

<sup>58</sup> See I.R.S., *Digital Assets*, <https://www.irs.gov/businesses/small-businesses-self-employed/digital-assets> (last visited June 25, 2023) (“[T]he transfer of property, including a digital asset, as a bona fide gift, requires the filing of Form 709, United States Gift (and Generation-Skipping Transfer) Tax Return if the fair market value of the property, at the time of the transfer, exceeds the donor’s annual gift exclusion amount available at the time of the transfer.”).



In addition to these generally applicable legal and regulatory principles, there are certain distinctive legal and regulatory regimes impacting NFT fundraising for nonprofits and political campaigns or committees, respectively, that deserve individualized treatment. Summaries of the most significant of these applicable laws and regulations are included below. Because NFT fundraising in these contexts is a relatively recent phenomenon, there is some legal and regulatory uncertainty in this environment.<sup>59</sup> As these and other markets for non-investment NFT finance mature, the legal and regulatory landscape will no doubt become clearer.

#### A. *The Legal Regulation of Nonprofit Fundraising Using NFTs*

The legal regulation of nonprofits is principally a matter of concern under federal and state income tax laws and regulations, state entity laws (which offer nonprofits reliable structure and governance rules through which they may conduct their operations), and for charitable nonprofits, state charitable solicitation laws and regulations. In each case, the nature and role of NFTs in the fundraising drives the application of law and the resulting legal conclusions or questions. Because NFT offerings are linked to nonprofit fundraising in multiple ways, several different types of issues arise, some affecting the donor and others affecting the donee nonprofit.

Federal income tax law, specifically IRC § 501(a),<sup>60</sup> offers the opportunity for nonprofits to qualify for an exemption from the payment of income taxes under specified conditions. Although the precise policy and theory underlying the federal tax exemption is difficult to discern,<sup>61</sup> the law establishes specific types of organizations—based on their essential purpose or function—that qualify for the exemption. Charitable organizations can qualify for the exemption under IRC § 501(c)(3).<sup>62</sup> This body of regulation is separate from, but works in coordination with, state business associations laws governing the organization of nonprofit business entities.

A nonprofit exempt from income taxation under IRC § 501(a) as an organization qualified under IRC § 501(c)(3) that desires to create NFTs and offer them to donors must ensure that this activity is consistent with its tax-qualified purpose or function, which is typically embodied in its organizational chartering document.<sup>63</sup> More broadly, regardless of its federal income tax status, a nonprofit organized as a corporation or other business entity under state statutory law must ensure that its activities relating to NFTs (e.g., creating, minting, offering, selling, transferring, or

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<sup>59</sup> See *Taxation of Cryptocurrency and Other Digital Assets*, BLOOMBERG TAX, April 3, 2023, <https://pro.bloombergtax.com/brief/cryptocurrency-taxation-regulations/> (“Not all digital asset transactions are taxed equally.”).

<sup>60</sup> 26 U.S.C. § 501(a) (2018).

<sup>61</sup> See, e.g., Michael Fricke, *The Case Against Income Tax Exemption for Nonprofits*, 89 ST. JOHN'S L. REV. 1129, 1138-53 (2015) (describing the development of the exemption and various theories justifying it).

<sup>62</sup> 26 U.S.C. § 501(c)(3).

<sup>63</sup> See 26 C.F.R. § 1.501(c)(3)-1(b) (“An organization is organized exclusively for one or more exempt purposes only if its articles of organization . . . : (a) Limit the purposes of such organization to one or more exempt purposes; and (b) Do not expressly empower the organization to engage, otherwise than as an insubstantial part of its activities, in activities which in themselves are not in furtherance of one or more exempt purposes.”); NFT FUNDRAISING, *supra* note 13, at 34.

delivering NFTs) are consistent with its chartered purpose under the state law of its organization.<sup>64</sup> Having said that, absent the constraints of, e.g., federal income tax law, nonprofit corporate charters—like those of for-profit corporations—can and sometimes do state a very broad corporate purpose, up to and including any lawful purpose.<sup>65</sup>

Supporters of a charitable organization have a tax incentive to donate NFTs that have appreciated in value to a charitable organization because that donation of appreciated assets, although reportable, would result in no gain realized by the donor under federal income tax law.<sup>66</sup> The donor should be able to take a deduction equal to the full value of the NFT, up to any maximum values applicable to the particular.<sup>67</sup> The valuation of NFTs for tax (and other) purposes can, however, be challenging because of volatility in the markets for digital assets.<sup>68</sup>

Given that volatility, a charitable organization that receives an NFT as a direct donation likely would want to sell it rather than hold it.<sup>69</sup> Importantly, all transactions in cryptocurrency are required to be reported to the IRS in U.S. dollars, necessitating a conversion requiring a fair market value assessment, in most cases (since NFTs typically are sold for cryptocurrency).<sup>70</sup> Because the process of receiving and reselling an NFT and converting the proceeds to dollars may be more trouble than it is worth, few nonprofits may decide to accept direct donations of NFTs. They may, however, determine to accept digital asset donations through a third-party provider or donor advised fund that processes transactions for them.<sup>71</sup>

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<sup>64</sup> See Johnny Rex Buckles, *Curbing (or Not) Foreign Influence on U.S. Politics and Policies Through the Federal Taxation of Charities*, 79 MD. L. REV. 590, 622–23 (2020) (“[D]irectors of a nonprofit charitable corporation must not cause the entity to act contrary to its corporate purposes (i.e., directors must obey corporate charters), but amendments to corporate charters, including purposes clauses, are often permitted through compliance with specified internal procedures.”).

<sup>65</sup> See Michael Haber, *The New Activist Non-Profits: Four Models Breaking from the Non-Profit Industrial Complex*, 73 U. MIAMI L. REV. 863, 943 (2019) (“[A]lthough corporations are still not permitted to operate outside of the corporate purposes listed in their charters, it has become increasingly common for state non-profit statutes to permit the incorporation of a non-profit for any lawful purpose, raising the issue of whether anything lawful could ever be ultra vires for an entity with such a broad corporate purpose.”).

<sup>66</sup> See generally McDermott Will & Emery, *NFTs and Charitable Fundraising: Navigating Tax Hurdles*, Jan. 11, 2022, <https://www.mwe.com/insights/nfts-and-charitable-fundraising-navigating-tax-hurdles/> (“Donors who can meet IRS reporting requirements can avoid paying tax on the amount of gain they would otherwise incur if they had sold the appreciated NFT in the market and donated cash to the charity.”).

<sup>67</sup> See *id.* (“Donors [who are not creators] can receive a deduction for an appreciated NFT’s full value up to the percentage cap of their adjusted gross income.”); Jennifer Galstad-Lee & Patrick Crosby, *Tax considerations on charitable giving of cryptoassets*, THE TAX ADVISOR, Dec. 1, 2022, <https://www.thetaxadviser.com/issues/2022/dec/tax-considerations-on-charitable-giving-of-cryptoassets.html> (“[T]he donor may claim a deduction if the donation is made to a qualifying charity . . . . The donor’s charitable contribution deduction is subject to certain limitation rules . . . , depending on the character of the contributed property and the donee charity’s use of the donated property, among other things.”).

<sup>68</sup> See Galstad-Lee & Crosby, *supra* note 67 (“[F]iguring out the FMV of cryptoassets can be difficult, depending on the circumstances.”); McDermott Will & Emery, *supra* note 66 (asking about, e.g., valuation methods and appraisals).

<sup>69</sup> See, e.g., McDermott Will & Emery, *supra* note 66 (“[M]ost charities would want to immediately convert an NFT to cash . . . .”).

<sup>70</sup> See Galstad-Lee & Crosby, *supra* note 67 (“[F]or tax purposes, transactions involving virtual currency must be reported in U.S. dollars. Therefore, taxpayers will be required to determine the FMV of virtual currency in U.S. dollars as of the date of payment or receipt.”).

<sup>71</sup> See *id.*

State charitable solicitation laws also may apply to the use of NFTs in charitable nonprofit fundraising. Although specific requirements vary from state to state, they typically fall into two regulatory types: registration and financial reporting.<sup>72</sup> The application of these laws in the context of charitable nonprofit NFT finance is uncertain. An analogy to donative crowdfunding for charitable organizations is instructive.

Based on state charitable solicitation laws in the United States generally applicable to donative crowdfunding for charitable nonprofits, NFT fundraising campaigns conducted by the charitable nonprofit for its own benefit would be most likely to trigger the application of charitable solicitation law.<sup>73</sup> Those conducted by a compensated third party (including an Internet fundraising platform and its related payment service provider) also may be regulated under these laws.<sup>74</sup> NFT offerings conducted for the benefit of charitable organizations by individuals who are uncompensated for their efforts are least likely to trigger the application of these legal requirements.<sup>75</sup> Overall, “while the definitions of the for-profit participants that are subject to charitable solicitation laws tend to be broad, it is still generally unclear whether either the . . . platforms or their third-party payment processors fall within them.”<sup>76</sup> This is a key area for further regulatory development.

#### B. *The Legal Regulation of Campaign Finance Using NFTs*

Among other things, federal campaign finance laws limit the source and dollar amount of contributions to political campaigns and committees. In a series of decisions over the years, the U.S. Supreme Court has expressed its understanding that these limitations exist, in significant part, to prevent corruption or the appearance of corruption through the exchange of contributions for political influence.<sup>77</sup> The application of campaign finance regulation to NFT fundraising for political campaigns and committees has not yet been fully clarified. The Federal Election Commission (“FEC”) has issued two relevant advisory opinions, but unaddressed concerns remain.

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<sup>72</sup> See, e.g., I.R.S., *Charitable Solicitation - Periodic State Reporting*, <https://www.irs.gov/charities-non-profits/charitable-organizations/charitable-solicitation-periodic-state-reporting> (last visited July 2, 2023); I.R.S., *Charitable Solicitation - State Requirements*, <https://www.irs.gov/charities-non-profits/charitable-organizations/charitable-solicitation-state-requirements> (last visited July 1, 2023).

<sup>73</sup> See Mayer, *supra* note 51, at 1408; see also *id.* at 1422 (“The easiest case for regulating is when a charity uses crowdfunding to benefit itself.”).

<sup>74</sup> See *id.* at 1409-10; see also *id.* at 1423 (“Platforms and third-party payment processors may also be reached by those rules if they apply to for-profit participants in charitable solicitation and the activities engaged in by these parties trigger those rules.”).

<sup>75</sup> See *id.* at 1409.

<sup>76</sup> *Id.* at 1410-11; see also Perlman & Perlman, *What Nonprofits Should Be Asking About Virtual Currency Regulation and Fundraising*, Oct. 11, 2021, <https://perlmanandperlman.com/nonprofits-asking-virtual-currency-regulation-fundraising/> (advising charitable organizations that are considering accepting cryptocurrency to ask fundraising platforms whether they are registered as professional fundraisers).

<sup>77</sup> See *Citizens United v. Fed. Election Comm'n*, 558 U.S. 310, 345 (2010) (“The *Buckley* Court recognized a ‘sufficiently important’ governmental interest in ‘the prevention of corruption and the appearance of corruption.’ This followed from the Court’s concern that large contributions could be given ‘to secure a political *quid pro quo*.’”).

Under a 2014 advisory opinion issued by the FEC, cryptocurrency contributions—the likely scenario in most NFT political fundraising situations—may be lawfully accepted as contributions.<sup>78</sup> Specifically, the FEC determined that bitcoins are “money or anything of value” within the meaning of the Federal Election Campaign Act of 1971, as amended.<sup>79</sup> The FEC concluded that bitcoin contributions may be accepted as proposed in the accompanying request and filings “subject to valuation and reporting procedures similar to those that the Commission has previously recognized in analogous circumstances.”<sup>80</sup> Because the concept of value is important to the application of campaign finance regulation, valuation issues (including market volatility) may arise in applying the law to campaign contributions made in cryptocurrencies or NFTs.<sup>81</sup>

The regulation of third-party service providers also has been a cause for concern addressed in an FEC advisory opinion. NFT-focused political committees and candidates that do not have the wherewithal to create and mint their own NFTs would need to arrange with third parties to provide those services. In December 2022, DataVault Holdings, Inc., a firm that designs and markets NFTs for use by third parties, received an advisory opinion from the FEC confirming the legality under federal election finance law of two business models for selling NFTs to political committees.<sup>82</sup> The question at issue was whether DataVault’s proposed conduct of business with political committees resulted in it making unlawful contributions to those political committees.<sup>83</sup> Under both models, DataVault would transfer the NFTs to a political committee to allow it to offer the NFTs to contributors, but it would not be compensated for the NFTs by the political committee until the NFTs are transferred to contributors.<sup>84</sup> “The Commission concludes that DataVault’s proposals to provide political committees with NFTs on the same terms that it regularly offers its non-political clients would be a permissible extension of credit by DataVault in the ordinary course of business.”<sup>85</sup>

Other legal and regulatory questions about NFT campaign finance stem from the nontransparent nature of blockchain transactions. Concerns include potential foreign influence on politics and illicit contributions made by proxies.<sup>86</sup> Contributions by minors also may be harder to discern or track. Federal law prohibits foreign nationals from contributing to federal, state, or local elections, prohibits one person contributing in the name of another to influence any election for federal office, and prohibits individuals 17 and under from contributing to candidates and donating to political party committees.<sup>87</sup> Effective, standardized compliance processes in these areas are still evolving. Additionally, the mechanics of public enforcement of campaign finance rules in the blockchain context present unique challenges.<sup>88</sup>

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<sup>78</sup> F.E.C. Advisory Opinion 2014-02, May 8, 2014, <https://www.fec.gov/files/legal/aos/2014-02/2014-02.pdf>.

<sup>79</sup> *See id.*; 52 U.S.C. § 30101(8)(A)(i) (2018); 11 C.F.R. § 100.52(a) (2023).

<sup>80</sup> F.E.C. Advisory Opinion 2014-02, *supra* note 78.

<sup>81</sup> *See, e.g.,* Noah Briggs, *Does the FEC Have a Plan to Deal With Crypto?*, WHOWHATWHY, Apr. 27, 2023, <https://whowhatwhy.org/politics/elections/does-the-fec-have-a-plan-to-deal-with-crypto/>.

<sup>82</sup> F.E.C. Advisory Opinion 2022-22, Dec. 15, 2022, <https://www.fec.gov/files/legal/aos/2022-22/2022-22.pdf>.

<sup>83</sup> *See id.*

<sup>84</sup> *See id.*

<sup>85</sup> *Id.*

<sup>86</sup> *See id.*

<sup>87</sup> 52 U.S.C. §§ 30121, 30122 & 30126 (2018).

<sup>88</sup> *See* Briggs, *supra* note 81 (“Cryptocurrency and NFTs have so far outpaced the FEC’s rulings on their use by campaigns and political donors making enforcement . . . difficult.”).

## V. Conclusion

NFTs are here—perhaps to stay. Nonprofits, political candidates, and political committees have begun using NFTs in financings. NFT-fueled funding in the nonprofit sector is developing and growing faster than NFT usage in campaign finance, with specialized funding platforms emerging. Though the IRS and FEC have begun addressing NFT-related issues, many remain unresolved. For example, NFT valuation difficulties in volatile digital asset markets present challenges to the accurate and complete financial reporting required by both nonprofit and campaign finance regulation. Moreover, the faceless nature of blockchain transactions, including NFT-based financings, complicates adherence to laws requiring transparency in value transfers.<sup>89</sup>

Although efforts currently are underway to look at digital asset regulation more holistically, it is not evident where those efforts might lead. President Biden signed an *Executive Order on Ensuring Responsible Development of Digital Assets* in March 2022 that sets forth related policy (supportive of innovation and risk management) and objectives and directs coordinated executive branch action in response.<sup>90</sup> The executive order notes concerns about transparency, among other things, but not valuation.<sup>91</sup> Six months after release of the executive order, the White House published a fact sheet summarizing progress made to date—the output reflected in nine reports outlining frameworks and policy recommendations.<sup>92</sup> The fact sheet, like the executive order, is general in application overall, but it indicates that “the President will evaluate whether to call upon Congress to amend the Bank Secrecy Act (BSA), anti-tip-off statutes, and laws against unlicensed money transmitting to apply explicitly to digital asset service providers—including digital asset exchanges and nonfungible token (NFT) platforms.”<sup>93</sup> Additionally, both the executive order and the fact sheet mention the importance of private and public enforcement numerous times. Thus, the gross parameters of a legal regulatory path forward are being developed, but the precise shape and direction of the path remain to be seen.

Despite areas of legal and regulatory uncertainty, nonprofits, political candidates, and political committees may be adopters of NFT fundraising campaigns in greater numbers as time moves forward. Unless and until additional legal frameworks are developed to address the uncertainties, however, compliance and enforcement challenges will persist. These challenges may slow the rate of growth of NFT usage in non-investment finance in the short term as fund seekers, funders, and other market participants test the limits of existing regulation.

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<sup>89</sup> Daniel Castro, *NFTs: US Policies and Priorities in 2023*, Info. Tech. & Innovation Fdn, Apr. 24, 2023, <https://itif.org/publications/2023/04/24/nfts-us-policies-and-priorities-in-2023/>.

<sup>90</sup> Exec. Order No. 14067, 87 F.R. 14143 (March 9, 2022), available at <https://www.whitehouse.gov/briefing-room/presidential-actions/2022/03/09/executive-order-on-ensuring-responsible-development-of-digital-assets/>.

<sup>91</sup> *Id.* (“The United States must ensure appropriate controls and accountability for current and future digital assets systems to promote high standards for transparency, privacy, and security — including through regulatory, governance, and technological measures — that counter illicit activities and preserve or enhance the efficacy of our national security tools.”).

<sup>92</sup> FACT SHEET: White House Releases First-Ever Comprehensive Framework for Responsible Development of Digital Assets (Sept. 16, 2022), <https://www.whitehouse.gov/briefing-room/statements-releases/2022/09/16/fact-sheet-white-house-releases-first-ever-comprehensive-framework-for-responsible-development-of-digital-assets/>.

<sup>93</sup> *Id.*