

Sweepstakes and Contests: Legal Issues

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Sweepstakes and Contests: Legal Issues

Companies use sweepstakes and contests as a way to create buzz or excitement about a specific product, service or promotion. The emergence of social media and the Internet have made these types of promotions even more attractive to advertisers. A simple, inexpensive giveaway has the potential to introduce a new product or brand to an entirely new market or geographic region.

These promotions generally seem fair and straightforward; however, there are a number of federal and state legal requirements that must be met if a company seeks to use a sweepstakes or contest to promote its business venture. If the necessary legal requirements are not met, a promotion may be considered an illegal lottery prohibited by state and federal law. Even though a promotion may not be considered an illegal lottery, it will still be regulated by federal and state laws regarding sweepstakes and contests.

Sweepstakes and contests are subject to the jurisdiction of numerous federal agencies, including the United States Postal Service, the Federal Trade Commission, the Federal Communications Commission, and the United States Department of Justice. In addition, the promotion will also need to comply with the registration and bonding requirements of each state in which the sweepstakes or contest will be promoted. If a promoter decides that, due to the time and expense of complying with certain states' registration and bonding requirements, it will not offer its promotion to residents of certain states, the promoter must disclose in its eligibility rules that residents of particular states are ineligible to participate in the promotion.

The Definition of an Illegal Lottery

A promotion will be considered an illegal lottery if there is an element of chance, a prize is awarded and the participant offers some form of consideration for their participation in the promotion. If a promotion is deemed an illegal lottery, the promoter can face civil and criminal penalties. Sweepstakes and contests are two types of promotions that companies use to market their products and services. If structured and managed appropriately, these types of promotions will not be deemed an illegal lottery. To avoid classification as an illegal lottery, promotion sponsors and legal counsel should review the Deceptive Mail Prevention and Enforcement Act, as well as regulations promulgated by the Federal Trade Commission.

The Difference Between Sweepstakes and Contests

As a general rule, a sweepstakes promotion is a random drawing for prizes, which meets two of the criteria of a lottery (chance and a prize). In order to avoid being classified as an illegal lottery, a sweepstakes promotion must make certain that it does not meet the third criteria of an illegal lottery: consideration. Accordingly, in order to qualify as a sweepstakes, the participant must not be required to offer any consideration in exchange for the chance to win the prize.

A contest, on the other hand, avoids classification as an illegal lottery because it removes the element of chance. Generally, most contests require the entrant to demonstrate some skill or exert some level of effort. By selecting the winner based on an objective determination of the level of skill and effort displayed, the promotion eliminates the element of chance, which is a hallmark of an illegal lottery.

Special Rules Related to Sweepstakes

As stated above, to avoid being considered an illegal lottery, a promotion should not require an entrant to purchase a product or expend significant time or effort to enter the sweepstakes. There are, however, exceptions to this rule. If a contest is going to require a purchase or the investment of significant time and effort, it can still be considered a sweepstakes if one of the following requirements is met:

- At least one method of entry is free, with no mandatory consent to receive marketing materials.
- No physical prize is given. The sweepstakes may award items that have no value (e.g., displaying video on corporate web page).
- The winner is determined by skill, not chance.

The promoter of a sweepstakes should ensure that each entrant in the promotion is treated the same, including allotting the same chance to win regardless of the method of entry. In sweepstakes that include a purchase as part of the entry process, the promoter must ensure that entrants who do not comply with the purchase requirement are given the same number of entries as individuals that do purchase the required product or service.

Special Rules Related to Contests

The distinguishing factor between sweepstakes and contests is the way the winner is determined. In a sweepstakes, the winner is selected at random, compared to a contest where the winner is selected based on unbiased judging of an actual skill. The laws and regulations of each state have their own definition of what constitutes a "skill" and promoters should familiarize themselves with their state's particular requirements prior to determining the selection criteria. Generally, a promotion will be considered a contest if the winner is predominantly chosen based on skill. This does not mean that there cannot be some component of luck involved in determining the winner. Contests may require payment of some form of consideration and still avoid being tagged as an illegal lottery. If a promoter decides to require that some form of consideration be paid prior to entry in the contest, it will be particularly important to review the state laws in each jurisdiction. Some states permit promoters to require a purchase or to charge an entrance fee. Other states permit a purchase requirement but do not permit the charging of an entrance fee. Other states' disclosure, registration and bonding requirements will vary depending on the nature of consideration required.

Other requirements for a contest include:

- The promoter must disclose the specific judging criteria that will be used and how heavily each criteria will be weighted. If there is no weighting assigned to each category, the promoter should weight each category equally.
- The contest must be judged by qualified judges who must fill out specific scoring cards when judging the contest.
- There must be a specific plan as to how to break any ties between participants' entries. The mechanism for determining tie-breakers must be disclosed in the official rules. Sponsors should note that ties cannot be broken by chance or random drawing.

Promoters of contests that require a purchase or payment to be made prior to entry, need to check applicable state laws to determine whether this requirement is permitted and, if so, whether there are any additional reporting or registration requirements. Some states do not allow promoters to require a payment or purchase in connection with a contest. Even in states that allow a payment or purchase to be a prerequisite to entry in a contest, there may be specific disclosure and registration requirements.

Federal Legal Requirements for Sweepstakes and Contests

To ensure that a promotion will not be considered an illegal lottery, there are a number of legal requirements that the promotion must meet. As a general rule, these requirements are designed to ensure that each entrant of the sweepstakes or contest is treated the same and that the rules for the sweepstakes or contest are consistently written and enforced. Specifically, to ensure legality of a sweepstakes or contest, a promoter should make sure that the promotion adheres to the following rules:

- When entrants can participate in the promotion via different methods (e.g., mail, online) the start and end date for each method should be the same. In practice, this means that participants who elect to mail in their entry must be allowed to mail it up to and including the last date of the promotion.
- There can be no requirement that participants purchase anything or make any payment to enter the contest or receive a prize.

The marketing and implementation of the sweepstakes or contest must be performed in a consistent and fair manner. The promoter must make sure that its official rules and any advertisements of the promotion make a full and accurate disclosure of each prize detail, as well as who is eligible to participate in the promotion. This disclosure should include any requirements that entrants be of a certain age or reside in a certain location. Finally, each promoter must ensure that the implementation of the sweepstakes or contest fully adheres to its published rules and regulations. For instance, if the promotion's official rules state that winners will be selected at random on a given date at a certain location, the promoter must randomly select the winner at the specified time and location.

Documentation Required for a Sweepstakes or Contest

Prior to beginning a promotion that utilizes a sweepstakes or contest, the promoter should have all of the requisite legal documentation in place. This documentation includes:

- A listing of the official rules for the sweepstakes or contest that specifies the requirements of the promotion.
- Releases from each winner of the sweepstakes or contest regarding eligibility for the promotion and releases that permit the promoter to use their name and/or likeness in any publicity materials. The releases should also include releases by any guests of the winner who are entitled to take part in the winning prize (e.g., a trip for two).
- Advertisements of the promotion must include a shortened rules disclosure as required by applicable state laws. The specifics of the advertisement regarding size and disclosure will vary depending on the type of advertisement.

If the promoter is using any third party vendors to assist in the marketing, administration, or implementation of the sweepstakes or contest, the promoter should have a signed written contract with each of these parties. These contracts should specify the obligations and responsibilities of the third party provider. It is also advisable for these contracts to contain indemnification provisions that require the third party provider to indemnify the promoter for any liabilities arising out of a contract breach.

Record-keeping Requirements for Sweepstakes and Contests

As previously stated, it is imperative that promoters of sweepstakes and contests make sure that their promotional and advertising materials for the promotion are drafted in full compliance with legal requirements and that the disclosures and information are consistent across all mediums of advertisement and promotion. Copies of the official rules, advertisements and entry materials, including winner lists, should be retained by the promoter for at least four years. The promoter should also be prepared to provide, upon request, a list of winners for at least six months after the end of the promotion or the date of prize redemption.

Situations Presenting Additional Compliance Issues

There are a number of particular types of promotions that may have more stringent disclosure and registration requirements, including:

- Promotions in foreign countries.
- Promotions conducted by direct mail.
- Promotions that require a survey, questionnaire or visits to a particular website.
- Promotions that require entrants to create any user-generated content, including videos and music.
- Promotions that require entrants to post to another website, including Facebook and Twitter.
- Promotions where the winner is determined by public voting, including ranking.
- Promotions involving any highly regulated industry, including alcohol or tobacco.
- Promotions aimed at minors.
- Promotions that benefit a charitable purpose.
- Promotions that require entrants to promote the contest by text message or forwarding to friends.

Private Right of Action

The Deceptive Mail Prevention and Enforcement Act (the Act) permits consumers to seek damages in a civil action in connection with sweepstakes promotions made available or promoted through direct mail. In addition to requiring certain disclosure information on mailed sweepstakes entry materials, the Act also prohibits sponsors from:

- Giving the recipient the impression that they have already won a prize.
- Mailing void checks that do not clearly indicate that they are non-negotiable and have no cash value.
- Using seals, insignia, names or terms that imply the promotion is endorsed by or related to a governmental entity.
- Conditioning participation on the purchase of something or the consent to receive future solicitations or mailings.

Specific State Requirements for Sweepstakes and Contests

Some states, including Rhode Island, New York and Florida require that promotions be registered in and/or bonded in that particular state. If a promoter does not wish to register in a particular state or go through the hassle and expense of the bonding process, residents of those states must be explicitly listed as ineligible to participate in the promotion. While promoters and legal counsel should familiarize themselves with the legal requirements of each state in which they plan to market their promotion, there are a few states with particularly stringent sweepstakes and contest laws that should be mentioned.

New York State

Under New York law, sweepstakes offered in connection with the sale of consumer products or services with prizes valued in excess of \$5,000, must register with the state and secure a surety bond. The promoter may create a trust fund instead of obtaining a surety bond. The New York registration must be completed at least 30 days prior to the commencement of the promotion and must include a copy of the official rules and a \$100 filing fee. After completion of the sweepstakes, the promoter must file with the State of New York, a certified list of individuals that won prizes valued in excess of \$25. If the sweepstakes is advertised or promoted in a retail outlet, the promoter must conspicuously post the official rules, prizes offered, and the geographic area eligible to participate in the promotion.

Florida

Florida law requires that sweepstakes utilizing prizes with an aggregate retail value in excess of \$5,000 must be registered and bonded at least one week prior to commencement of the sweepstakes or contest. In lieu of a surety bond, the promoter can establish a trust account equal to the value of the prizes offered in the promotion. In connection with its application, the promoter must file a copy of its official rules and pay a \$100 filing fee at least 30 days prior to commencement of the sweepstakes. Once the rules are filed, they cannot be altered or amended. Promoters with a five-year history of conducting sweepstakes in Florida may apply for a waiver of the bonding requirement. Upon completion of the sweepstakes, the promoter must file a certified list of winners with the State of Florida. This certified list must be filed within 60 days of the end of the sweepstakes and must include all winners of prizes with a retail value in excess of \$25.

Rhode Island

Under Rhode Island law, any promotion where a retail establishment offers a sweepstakes promotion with an opportunity to receive a gift, prize or gratuity valued in excess of \$500, requires registration with Rhode Island's Secretary of State. The registration must be filed before the promotion begins. Registration requires the payment of a \$150 filing fee and the filing of a statement setting forth:

- The minimum number of participating objects to be made available.
- The minimum number of available prizes to winners of the promotion.
- The minimum value of the prizes.
- All applicable rules of the promotion, including eligible participants and any geographic or time limits.
- The chances of having a winning entry.

Unlike New York and Florida, Rhode Island does not require the posting of a bond or establishment of a trust account. There is also no requirement that sponsors file a list of winners with the State, although they are required to retain a list of winners for at least six months after the end of the promotion.

Issues Presented by Online Promotions

The use of online technology in promotions is an advertising boon to businesses because it allows them to inexpensively broaden their target market and also utilize existing customers to help spread information about the company, its brand and its promotions. The use of online promotions does create a number of issues. First, because not everyone has access to a computer or the Internet, a promotion should not be strictly an online promotion because it may then be considered an illegal lottery. Also, the vast, world-wide reach of the Internet can create a compliance headache because individuals around the world may be able to gain access to an online promotion. This may trigger filing, registration or other requirements in virtually any jurisdiction in the world. To limit this risk, it is advisable for promotions to contain "void where prohibited by law" language or to specify the eligible jurisdictions for participation in the promotion.

Online promotions also raise issues of privacy to the extent that the sponsor of the promotion obtains personal information regarding the participants. While obtaining this information is often one of the goals of an online promotion, the sponsor must ensure that it properly maintains the privacy of this information by establishing, disclosing and enforcing a privacy policy and adopting reasonable technological systems to safeguard personal information.

Other Unique Situations Which May Arise

In addition to the state requirements set forth above, other states may impose additional requirements on promoters of sweepstakes and contests. The insignificant nature of some of these requirements highlights the importance of reviewing all relevant federal and state laws relative to sweepstakes and contests prior to commencing a promotion. Examples of some of these prohibitions and restrictions pertain to the amount of materials that needs to be provided to retail outlets as well as who pays the return postage on correspondence between a participant and promotion sponsor.

Sweepstakes and contests can be an inexpensive and effective means of promoting a business, product or service. The advent of new avenues for contacting participants, including social media outlets like Facebook and Twitter, broadens the reach of these promotions and the methods used to advertise them. This increase can lead to more successful promotion campaigns but it can also create new or different legal obligations. The legal requirements of these types of promotions is complicated by the joint federal and state regulation of the industry and is compounded by each state's different requirements regarding registration and financial surety. The increased time and expense associated with state and federal regulatory compliance necessitates a thorough review of all applicable federal and state laws, regulations and advisory opinions.

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