

Bonanza!

MEDIA LAW: While online contests could be a windfall for users, they also promise a lot of legal work for lawyers.

By David Halberstadter and Leon Liu

Free Stuff! Over 500 Prizes Awarded! Enter Now!" trumpets one site on the Internet. "Hot Prize Giveaway!" and "Hello? My Name is RICH!" proclaim still other Web sites. At any given moment, there are literally thousands of online promotions running on the Internet.

FreeLotto.com, the Internet's most popular sweepstakes Web site, with more than 12 million users per month, offers daily grand prizes of up to \$10 million and a guaranteed \$1 million winner every month. The well-advertised iWon.com search engine conducts a sweepstakes that offers daily prizes of \$10,000, monthly prizes of \$1 million and a yearly prize of \$10 million. Topping both of these, the new Web site grab.com recently launched a contest giving eligible entrants the chance to win a cool billion.

More modest online sweepstakes also abound, offering electronics, cars, vacations, tickets, videos, T-shirts, computer software and gift certificates. Some sites are even devoted to listing all of the sweepstakes available online and allow users to register for multiple sweepstakes simultaneously.

Internet sweepstakes have become one of the most popular methods of driving traffic to a company's Web site. They are also a particularly effective way to collect valuable marketing and consumer information. This no doubt explains why any number of companies will tailor special promotions for individual e-businesses, administer their sweepstakes and even guarantee the payment of prizes.

These contests are not new. Sweepstakes originally were popularized in the 1960's through magazine-publishing companies to promote magazine subscriptions. Stores, fast-food restaurants, timeshare resorts, entertainment businesses and even charitable organizations have long since jumped on the bandwagon.

Sweepstakes and contests are hardly trouble-free advertising, however. Because of the potential for consumer deception, the U.S. Postal Service examines promotions that involve the use of the mail. The Federal Trade Commission has jurisdiction generally over unfair or deceptive acts and promotions. And, virtually every state has some legislation affecting the conduct of sweepstakes; a number of states have passed laws that specifically regulate such promotions.

Even the pioneers of such promotions can run afoul of these laws, often in a big way. **Publishers Clearing House** of Port Washington, N.Y., one of the sweepstakes industry's largest players, agreed last August to refund \$16 million to customers in 24 states and to make fundamental reforms to its business practices. Earlier in the year, it agreed to settle a class-action lawsuit for \$30 million.

Time Warner of New York recently agreed to refund nearly \$5 million to customers who might have been deceived into believing that their chances of winning a company-sponsored sweepstakes would be improved by purchasing magazine subscriptions.

Last April, Northridge-based **United States Corp.**

agreed to settle for \$30 million claims brought by the attorneys general of 48 states and the District of Columbia. And, in December 1999, **American Family Enterprises**, the Jersey City, N.J.-based sweepstakes regularly plugged by Dick Clark and Ed McMahon, agreed to a \$33 million settlement of a class-action lawsuit challenging its marketing practices.

Given the global reach of the Internet, businesses not only must be careful to comply with the strict federal and state laws regulating sweepstakes promotions in general; they must also anticipate, and protect themselves from liability from the

myriad issues that could arise, particularly from online sweepstakes. The last thing that any e-business needs before its long anticipated initial public offering is a state attorney general investigation or a potential costly class-action lawsuit.

A sweepstakes is basically a game of chance that awards a prize to a winner or winners selected from a random drawing. However, the addition of the element of consideration - for example, a required purchase, the payment of a fee or an expenditure of substantial effort by an entrant to enter - would make a sweepstakes a lottery. See *Peek v. United States*, 61 F.2d 973 (5th Cir. 1932); 47 C.F.R. Section 73.1211(b); Advisory Opinion No. 57, 69 F.T.C. 1232 (1966).

Except for those that are state-run, lotteries are prohibited by federal law and the laws of all 50 states. Thus, all sweepstakes, including online sweepstakes, must avoid requiring any kind of payment, entry fee or other consideration to enter the sweepstakes.



For this reason, Internet sweepstakes typically are conducted at “free” Web sites, without any entry or subscription fees. If not, the sponsor will provide a free alternative method of entry, which removes the element of consideration.

But, most Internet users pay a fee to their online service provider in order to obtain Internet access. Could that payment constitute “consideration” sufficient to convert a sweepstakes into an illegal lottery, even though no payment is made to or for the benefit of the sponsor of the sweepstakes itself? See, e.g., *People v. Cardas*, 137 Cal.App.Supp. 788 (1933) (element of consideration depends on whether participant paid something for his chance to win, not whether sponsor received something of value).

Past enforcement patterns suggest that the answer is no. Given the potential risks, however, new e-businesses may be wise to follow the conservative approach adopted by certain major sweepstakes sponsors, which provide for an alternative method of entry (such as an old-fashioned mail-in entry form).

The official rules for a sweepstakes are the most important element of the promotion. They serve as the terms of the contract between the sponsor and the entrants. For this reason, an Internet sweepstakes should be governed by official rules that are as complete and comprehensive as possible. The rules should anticipate to the greatest extent possible the types of future disputes that could arise from the promotion in general and should especially take into consideration that the sweepstakes is being conducted over the Internet.

Generally speaking, the official rules should include such details as a statement that no purchase is necessary; the odds of winning; how many prizes are available, what they are and how much they are worth; any restrictions on who may enter, including residents of particular states or countries; how one may enter, when the promotion will start and end; the deadline for receipt of entries; how the winner will be chosen; how to obtain a list of the winners; a reminder that the winner will be responsible for all applicable taxes; what happens in the event of fraud or unforeseen glitches affecting the sweepstakes; what law will govern the sweepstakes in the event of a dispute; and a statement that the sweepstakes offer is void where prohibited by law.

All of these provisions are essential for any sweepstakes, whether conducted on the Internet or otherwise. But some of these rules are especially important for online promotions.

State laws vary with respect to what information must be disclosed in the rules for a promotion. States with special disclosure requirements include California, Connecticut, Florida, Iowa, Maryland, Massachusetts, Minnesota, New Mexico, New York, Rhode Island, Tennessee and Texas. See, e.g., California Business and Professions Code Section 17539.1; Florida Statutes Annotated Section 849.094(3),(4)(a); Iowa Code Annotated Section 714B.1; New York General Business Law Section 369-e(1),-e(4).

A company preparing to conduct an online sweepstakes, therefore, must comply with the most stringent states’ laws or exclude states whose requirements are either too cumbersome or conflict with the intended operation of the sweepstakes.

Sponsors of online sweepstakes are also potential subject to worldwide exposure and liability. Many countries expressly prohibit sweepstakes contests. A sweepstakes designed to comply with U.S. laws may not be fully compliant with the laws of other countries where such promotions are not entirely forbidden. Internet sweepstakes, therefore, should be expressly limited to residents of the United States, unless efforts are made to comply with the laws of other countries.

The official rules should also specify where disputes arising from the promotion must be brought and what jurisdiction’s laws will apply, so that claims can be handled with some measure of predictability and efficiency.

The anonymity of the Internet makes it easy for minors to enter sweepstakes, whether using their own Internet account or that of a parent. Minors ordinarily do not have the legal capacity to agree to the specific rules and conditions governing a sweepstakes. A sponsor, therefore, could experience problems seeking to enforce the official rules against a minor entrant. Issues also could potentially arise if a minor were to win a prize, such as an automobile or vacation, that was intended for an adult.

Online sweepstakes now are subject to the new privacy guidelines set forth in the recently enacted Children’s Online Privacy Protection Act, which regulates the online collection of personal information from children under 13 years old. 15 U.S.C.A. Section 6501 et seq. Thus, in addition to disqualifying employees and their families, sponsors may want to limit the age of eligible entrants to 18 years or older, or at least to those who are at least 13-years old.

Anyone who has ever used the “cut and paste” function of a word-processing application knows just how easy it can be to duplicate information on a computer. With only a few keystrokes, each potential entrant can submit hundreds of electronic entry forms. This may encourage users to enter the contest, but it also could overwhelm an unprepared Web site and undermine the company’s effort to generate goodwill by conducting the contest.

It is, therefore, advisable to limit the number of entries that may be submitted in connection with an online sweepstakes, for example, by permitting only one entry per person, household or e-mail address per contest. A sponsor can also prohibit entries submitted by automated subscription services and should make clear that any entries after the first one will be disqualified.

In the online world, Web sites and servers crash; files can be corrupted or even lost. Then there are hackers and the creators of viruses, who take pleasure from interfering in e-business. A sweepstakes sponsor must protect itself from the possibility that its promotion may be disrupted by expressly limiting its liability and/or reserving the right to terminate the promotion in such an event.

To be sure, an online sweepstakes can generate terrific “buzz” and increase site traffic. But such promotions also have their legal pitfalls. Nevertheless, with careful planning and consideration given to what could go wrong, an e-business can launch a successful and compliant promotion with a minimum of risk.

David Halberstadter is a partner in the litigation group at Katten Muchin Zavis Rosenman.