

Client Advisory

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Are You an E-Winner?

“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. There are literally thousands of online promotions running on the Internet at any given time. Some sites offer regular cash prizes of \$1 million and an occasional \$10 million grand prize. A recently launched site now gives eligible entrants the chance to win a cool billion.

More modest online sweepstakes abound, as well, offering electronics, cars, vacations, tickets, videos, T-shirts, computer software and gift certificates. In fact, Internet sweepstakes have become one of the most popular methods of driving traffic to a company’s Web site and collecting valuable consumer information. Some firms will administer sweepstakes for other e-businesses and even guaranty the payment of prizes.

Sweepstakes and contests are hardly trouble-free advertising, however. Because of the potential for consumer deception, the

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United States Postal Service and the Federal Trade Commission are on the lookout for unfair or deceptive promotions. And every state’s attorney general has the authority to investigate sweepstakes that may violate state consumer protection statutes.

Even the pioneers of such promotions can run afoul of these laws, often in a big way. Publishers Clearing House, one of the sweepstakes industry’s largest players, agreed in August to refund \$16 million to customers in 24 states and to make fundamental reforms to its business practices. Earlier in the year, it settled a class-action lawsuit for \$30 million. Last April, United Sales Corp. settled 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 sweepstakes regularly plugged by Dick Clark and Ed McMahon—agreed to a \$33 million settlement of a 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 also must anticipate the myriad issues that could arise from the fact that the sweepstakes are conducted online. The last thing that any e-business needs before its long-anticipated IPO is a state attorney general investigation or a potentially costly class-action lawsuit.

It's a Sweepstakes, Not a Lottery

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 in order to enter—would make a sweepstakes a lottery. See *Peek v. United States*, 61 F.2d 973, 974 (5th Cir. 1932); 47 C.F.R. § 73.1211(b); Adv. Op. 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 fifty 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; or, they provide a free alternative method of entry. 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) (the element of consideration depends on whether the participant paid something for his chance to win, not whether the 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, who provide another way of entering the promotion (such as a mail-in entry form).

It's All in the Official Rules

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 the fact that it is being conducted on the Internet in particular.

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Generally speaking, the Official Rules should include details such 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, and 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.

“Void Where Prohibited”

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., Cal. Bus. & Prof. Code § 17539.1; Fla. Stat. Ann. §849.094(3),(4)(a); Iowa Code Ann. §§ 714B.1; N.Y. Gen. Bus. Law §369-e(1),-e(4). A company preparing to conduct an online sweepstakes therefore must either comply with the most stringent states’ laws or exclude states with requirements that are too cumbersome or that conflict with the intended operation of one’s sweepstakes.

Sponsors of online sweepstakes are also potentially subject to worldwide exposure and liability. Many countries expressly prohibit or place significant limitations on the conduct of sweepstakes. Internet sweepstakes therefore should be expressly limited to residents of the United States unless efforts will be 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.

This May Be Child’s Play

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.

Online sweepstakes are also subject to the privacy guidelines set forth in the recently enacted Children’s Online Privacy Protection Act, which restricts the online collection of personal information from children under 13 years old. 15 U.S.C.A. §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 13 years and over.

Too Much of a Good Thing

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. A sponsor can also prohibit entries submitted by automated subscription services and should make clear that any entries after the first will be disqualified.

“We Are Experiencing Technical Difficulties . . .”

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.

Goodwill Hunting

To be sure, an online sweepstakes can generate terrific “buzz” and increase site traffic. But such promotions have their legal pitfalls, as well. 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.

For More Information

If you have any questions regarding these issues or if you wish to be on our distribution list for future Client Advisories on entertainment, intellectual property and media issues, please contact one of us.

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