

Nonprofit Knowledge: Sweepstakes and Other Prize Promotions

Compliance and Ethics





Many US nonprofit organizations use prize promotions, such as sweepstakes and contests, as a way to engage with their donors and other supporters. However, organizations may not realize that prize promotions are highly regulated by state and federal law and could potentially be considered illegal gambling. And, even though nonprofit tax-exempt organizations are exempt from certain tax laws, they are not exempt from prize promotion laws. Below is an overview of issues to consider when

running an online prize promotion.

1. Don’t host an illegal lottery

Running a lottery is illegal, except when run by a government agency. Lotteries are generally defined as involving three elements: consideration, chance, and a prize. If only one of these three elements is present when deciding to run a prize promotion, you will not run afoul of the illegal lottery rules.

One way to ensure that an organization is not running an illegal lottery is to not require consideration for an entrant to take part in the promotion. Consideration is usually thought of as cash consideration, but it could also be the level of effort taken to enter a promotion.

If consideration is involved, for example where a prize is offered in connection with a conference registration or the purchase of a membership, organizations can offer a free Alternative Method of Entry (AMOE) to ensure that entrants have another way to enter.

However, the AMOE should not be unduly burdensome. An AMOE can involve entering by mail or electronically, and it often requires the collection of an entrant’s name, address, or other contact information.

Although AMOEs are usually seen in the context of a sweepstakes, they are also sometimes used where there is a no element of chance, such as with a contest. While some contests appear to be skill-based, sometimes there continues to be an element of chance, such as where a tie is broken by flipping a coin. In these instances, using an AMOE ensures that the prize promotion does not become an illegal lottery. Some states, such as Colorado and Maryland, prohibit a purchase in connection with a skills-based contest.

If an AMOE is offered, there must be “equal dignity” where every entrant has the same chance of winning the same prizes, such that someone who makes a purchase or provides other consideration to enter does not have a different (or greater) chance of winning.

2. Sweepstakes and contests

A sweepstakes is a prize promotion where a prize is offered and the winner is selected at random. A contest involves selecting a prize winner based on skill. Because the element of chance is involved with sweepstakes, they usually do not require consideration to enter, or also include an AMOE, otherwise they are considered illegal lotteries.

Contests involve skill and not chance, and consequently, they can generally include the other elements of consideration and a prize without being considered an illegal lottery. However, entries must be judged and scored by objective measurable criteria, and states have determined that skill must be the dominant factor in selecting a winner.

Depending on whether any element of chance is involved, such as to break a tie, organizations may need to include an AMOE for a contest to ensure that it is not an illegal lottery.

3. Regulatory structures

Prize promotions are regulated by state and federal law, generally under the consumer protection laws, and the Federal Trade Commission (FTC) rules on false and deceptive advertising, but other laws apply such as the Federal Deceptive Mail Prevention and Enforcement Act (DMA).

Organizations should be sure to have clear rules outlining the specifics about the prize promotion to ensure compliance with various state and federal requirements. These rules generally include information such as “no purchase necessary disclosures, eligibility requirements, the method of entry, deadline dates, the odds of winning, the prize description, and number of prizes and their value, and any special conditions.”

If a promotion is on social media, additional disclosures may be required by the relevant platform, and the FTC requires additional disclosures through the use of hashtags such as #sweepstakes or #contest so that it is clear that individuals are taking action in connection with participating in a prize promotion.

In addition to providing clear rules, some states require registration of a sweepstakes depending on the value of the prize. New York and Florida require registration and bonding if the prize value exceeds US$5,000, and Rhode Island requires registration and bonding if the prize value of a brick and mortar promotion exceeds US$500. In Arizona, if a skill-based contest is an “intellectual contest” and requires the purchase of a product to enter, an organization may be required to pre-register with the Attorney General.

Lastly, even though many nonprofit organizations are tax-exempt, winners of prizes are required to pay taxes on their winnings; if the prize is valued at US$600 or more, an organization will need to issue a 1099 to the winner.

Before running a prize promotion, nonprofits should be mindful of the complexities of these types of activities and make sure that they are structured appropriately.

Further Reading

Rules that apply to mail-in promotion are also used, by extension, to online prize promotions. However, this article will focus online prize promotions.

The DMA and other federal laws apply primarily to promotions run by US Mail. However, these requirements are reflected in online sweepstakes rules.

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