



Supreme Court Upholds Internet Sweepstakes Ban

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The writing may be on the wall for internet sweepstakes businesses. On Friday, the state supreme court unanimously upheld the constitutionality of G.S. 14-306.4, the statute enacted to target such operations. The principal decision is [Hest Technologies, Inc. v. State](#), __ N.C. __ (2012), written by Justice Hudson.

Background. The legislature has been concerned for several years with video gaming, or with businesses that offer an experience similar to video gaming. The current business model involves selling telephone or internet time to customers. Each customer receives an entry into a sweepstakes. The business owners generally analogize this to receiving a scratch-off game ticket with the purchase of a Big Mac, and, as with McDonald's promotions, there is generally a way to obtain some free entries. The customer normally goes to a video terminal, where he or she learns whether his or her sweepstakes entry is a winner. Typically, the video terminal simulates some form of gaming or gambling in the process of revealing the result, but the outcome is predetermined. That is, the entry either is a winner or it isn't, and the display merely reveals, rather than decides, that result. If the sweepstakes entry is a winner, the customer can claim a cash prize on site. Some customers spend hours purchasing many increments of internet or telephone time in order to receive numerous sweepstakes entries. The General Assembly viewed this as involving the same social ills as gambling, and in 2010, it enacted G.S. 14-306.4, "[e]lectronic machines and devices for sweepstakes prohibited."

The statute makes it a crime to "operate . . . an electronic machine" to "[c]onduct a sweepstakes through the use of an entertaining display, including . . . the reveal of a prize." Industry representatives sued to block implementation of the law, asserting, among other things, that it violated the free speech guarantee of the First Amendment. This argument was partially accepted by a superior court judge, then entirely adopted by a divided court of appeals, which viewed the statute as overbroad. Jessie's analysis of that opinion is available [here](#).

Ruling. The state appealed and the supreme court reversed. Initially, the court observed that "[e]lsewhere in the country, other courts facing challenges to the enforcement of similar laws have upheld them precisely because the Internet sweepstakes systems have been viewed as gambling in disguise," citing *United States v. Davis*, 690 F.3d 330 (5th Cir. 2012), and *Telesweeps of Butler Valley, Inc. v. Kelly*, 2012 WL 4839010 (M.D. Pa. Oct. 10, 2012). Yet our court did not conclude that electronic sweepstakes are gambling as traditionally defined. Sweepstakes operators generally contend that, like McDonald's, they are merely using sweepstakes entries to promote sales of a legitimate product, namely, telephone and internet time. On this theory, because the customers receive the telephone and internet time in exchange for their money, the money is not "bet" on the sweepstakes, which are merely a free bonus incidental to a commercial transaction. The court noted that in other states, over 99% of the telephone and internet time went unused, but because it had no similar data for North Carolina, it could not conclude that the customers' money was in practice a bet rather than a legitimate purchase.

Instead, the court reasoned that, even if sweepstakes are not gambling, the General Assembly had "identified a threat to the public and acted to address it." Further, because the "legislation regulates conduct and not protected speech," it is valid under the legislature's general police power. The court stated that "[o]perating or placing into operation an electronic machine is clearly conduct, not speech" and that "the act of running a sweepstakes is conduct rather than speech, despite the fact that sweepstakes participants must be informed whether they have won or lost."

The court acknowledged that regulating conduct may sometimes incidentally burden speech, but concluded that any incidental impact on speech in this case was justified by the state's "important or substantial interest" in "combatting the encouragement of vice and dissipation presented by these operations." And the court rejected the claim that the statute is overbroad: "We see no speech or conduct, other than that which is plainly the target of the legislation, that would be chilled or otherwise burdened by this statute. . . . [P]laintiffs have provided no actual examples . . . of conduct or speech that was not intended to be covered . . . yet still arguably falls within the statute's ambit."

Upshot. Although this decision is a big loss for the industry, I don't think that law enforcement officers should necessarily rush to charge sweepstakes operators with a crime.

- First, the opinion doesn't become the court's official mandate for 20 days. N.C. R. App. P. 32(b). Until then, I believe that the original ruling by the trial court – which generally upheld the ban on the specific types of entertaining display listed in the statute but struck it down as to entertaining displays generally – may remain in effect. I am not certain about this, however, and I encourage smart appellate lawyers to correct me if I am mistaken.
- Second, because this case involves a federal constitutional claim, the industry could ask the United States Supreme Court to review it. Statistically, the odds are against the Court accepting the case, but this issue is cropping up across the country so perhaps the Court will be interested.
- Third, industry representatives claim that they are ready to roll out a software update that will allow operators to avoid the law by using "non-entertaining reveals" rather than entertaining displays. I have long wondered exactly how far the definition of "entertaining display" extends, and in particular, what the requirement of "actual game play, or simulated game play" encompasses. See some of the hypotheticals I considered [here](#).

As a practical matter, for the time being, it appears that most businesses remain open, and that many law enforcement agencies are waiting for guidance from the Attorney General's office. Stay tuned.