

Mintz: As many of you know, there has been an explosion in these types of contests and sweepstakes and awards, and it's really quite remarkable. I was listening to a tech talk, which actually, for some of you who want a little more history, there's a fellow named Jason Morgan who is a consultant at the common pool and he has a short tech talk on the history of prizes and sweepstakes, so there was some interesting tidbits there for those of you who want a little bit of history. I think many of us recognize the prizes and bounties go way back to the pirate times.

I had forgotten that Charles Lindbergh's flight across the Atlantic was a consequence of a prize as well, which I thought was interesting. And we kind of trundled along for a long time in that and there has been this explosion in the last probably five to seven years. I think McKenzie did a report -- I believe it was 2009 -- detailing the growth of this and it has only gotten larger since then.

At MacArthur Foundation, where I'm general counsel, we are well known, or best known, I should say, for our Fellows' Prize Program, the Genius Grants colloquially known, and that's the kind of special sauce that we use and we get a lot of calls from people asking us what's the secret to it, how does it work. We did have a ruling from the IRS on this, although it wasn't actually necessary, I think we originally went just as an income tax ruling at the time -- this was back in 1981. But we've also had a lot of experience with other competitions and prizes that some of worked better than others, and so our goal today is really to go through both some of the practical questions as well as, of course, the legal ones. I'm really glad that we have experts up here, both from the tax and the state law side that can help us wade through some of the intricacies.

When we thought about how best to approach this -- I have a series of questions that I'm going to ask -- we were talking a little bit earlier about how it might have been a fun thing to do to say I could pretend to be a client and ask a bunch of questions, and it struck me -- although I haven't told my friends this yet -- that actually MacArthur is considering another type of prize or contest which we're still in the process of thinking through, but we have announced a little tidbit of it, which would be that every three years we would give away \$100,000,000 to be spent over three to five years on a solution of a particular problem. And we're not at the moment, although we're still in the process of thinking it through, constraining the problem, other than it has to be a problem that has a potential solution -- a social, environmental problem that would help the world in some ways, but it raises a lot of interesting questions about charitability and the types and scopes. And we were thinking about it and I said, Gee, I could have an hour of free advice. So I might ask some questions from time to time and I don't think that would be private benefit -- would it?

Reid: No, absolutely not.

Mintz: The other thing, because we have a lot of very smart, experienced people in the room, if somebody has a comment or a questions about an issue that we're touching upon, please feel free to walk to the mics so everybody can hear you, but we'd love to have more of a conversation. So, let me start out by just asking my colleagues, why are these things so popular? What's the attraction to these types of contests or prizes or awards? Why are so many groups -- charitable and otherwise -- moving towards them?

Alpert: I guess I'm probably the one to start off with that, and it's not just charitable organizations that are moving toward it, I think businesses are moving towards it as well. And I think part of it is the way the world has changed with regard to the internet and social media's use, and so it's both a vehicle that can be used to promote a lot of different things and it seems like it's easy and not until you really dig

down do you understand that there are a lot of issues and pitfalls associated with what appears to be happening on a daily basis. I probably get at least every day some solicitation from somebody about some sweepstakes or contest or raffle that you could be engaged in. So it's almost like it's become commonplace as a way to promote and therefore it seems easy. And the goal, I think of today, is it needs to make it clear that it's not so easy.

But I think tax-exempt organizations in particular have really begun to embrace the notion for a variety of different reasons. Some organizations are interested in just building engagement with the organization. People feel that people give money, but if they could engage them on a regular basis then it would be more sustainable and hopefully increase the loyalty to the organization. Other people see it as a way to increase volunteers and another sort of objective that I've seen happening is just the notion that it's a way to address, as Josh was saying, possibly difficult issues where your current base of people are not sort of seeing, or don't have the capability of perhaps addressing some sort of technological solution to a big problem, or to just get fresh ideas. So I think there's a multiple basis and I think that the way the world has changed has increased the visibility.

Reid: I'd just add that just one of the ways that the world has changed is the development of behavioral economics as a discipline and just economics in general. And that whole science is about incentives and tying an incentive to a behavior. So if a prize is essentially something that attracts behavior and you can attract charitable behavior as well by offering a prize. "If you build it, they will come," sort of a Field of Dreams idea. It's also, maybe, an acknowledgement of some limitations of the grant-making process where the grantor might not have all of the expertise to know whether the end goal is being accomplished or the best way to get that end goal accomplished. How would you write a grant agreement if you don't know how to achieve your goal? Prizes are a way of funding only after the solution has been achieved, so you can sort of try before you buy.

Mintz: There's a lot of issues implicated in that broad question. One of the things that we thought about it terms of this new competition was also expanding the field of ideas. As many of you who represent or are a part of foundations know, as shocking as it sounds, we are not the font of all wisdom. So there is an opportunity when you do a particular type of competition to really open the aperture in a way to get ideas from people that aren't just within the circle of foundation grant making or particular programs. So that's what, particularly, I think enticing to us, is we think about this bigger competition.

As Alex said, there's a lot that has to do with finding innovation, opening the ability to have people evaluating the ideas beyond just, for example, a program officer or a board of directors. So there's lots of different reasons -- I think many of you probably have seen or heard about a whole range of them.

What I would like to turn to now, Shelly, is let's talk a little bit about the forms that these might take, and then we'll get into some of the implications of the forms. So it might be helpful for those of us in the audience and otherwise, to sort of think about in terms of what forms these may take.

Alpert: So in terms of the variations of a theme that can exist, you can have a contest that is sheerly random chance. So you might have a drawing, for instance, for an iPad as an example where you are just trying to increase people who are interested in your organization. So you would have them submit an entry and you could or could not -- and those entries wouldn't be judged in any way but just would be chosen by chance.

If there is any consideration as part of that entry, however, then that becomes an illegal lottery under

state laws and gambling, and that's not allowed. In that situation you would have to eliminate consideration, whether consideration would be monetary or non-monetary. Like, for example, if you require somebody to do a video for that prize drawing, that might well be considered non-monetary consideration and would still put you in the gambling bucket.

So you want to create a situation if you are doing a drawing kind of thing, which is totally random, where you've eliminated one of those three elements -- and you can't eliminate the prize because that's the motivation here. So, it's really just two elements. Is there chance and is there monetary or non-monetary consideration?

One way you'll see -- if you look at drawings that are held oftentimes is they give an alternative means of entry. So you can either submit your idea, your video, your photograph, or you can just mail in an entry and that's called an alternative means of entry and thereby you are eliminating that consideration juncture.

The other kind of contest that we see a lot and that we're talking about more and what Josh is thinking about is more a skill contest where you have set criteria, you have independent judges and you have people spend time and energy creating a concept, an idea, an actual product that they will then submit to be evaluated by these judges. And the way that that contest works is that you're eliminating chance because you have this criteria.

On the other hand, if you then have the public -- which we see a lot of these days -- vote on who the winner is, so far the view is that it puts it back into the chance category, so you would need to work on eliminating the consideration again. So it's a very problematic kind of analysis that each kind of promotion we'll call it that you're considering has to be evaluated to figure out which bucket it fits into and which state laws and federal laws then become applicable.

And then there's the traditional raffles, which again people think you can do on the internet, but most state laws don't even let tax-exempt organizations do that on the internet. Those raffles are often defined as paper tickets that are torn half of it off - like California's very draconian still -- you can't use the internet in any way to run a raffle that's legal in California. You can announce it on the internet, but you can't have people buy tickets on the internet without violating state laws. So there's various structures that you can use and it's just a matter of then figuring out what laws apply to that particular structure.

Mintz: Let me just ask about the public participation, because we have seen a lot of that where it's this crowdsourcing idea, both in terms of whether it's the idea or some participation in the selection. If the public is just part of a process in providing an evaluation of a particular criteria or giving feedback on ideas, that would not make it into a chance? Or what's the criteria where that crosses a line?

Alpert: So, if they're the final determinator, if the public vote, if the final determinator, then you have an issue. Because you can just be voting for your best friend, you don't need to be applying the criteria that are set out in the contest. On the other hand, a lot of contests are structured where the public is a component of the criteria. For example, the judges will take 10% of their decision-making will be what the public vote is. And ultimately, that still puts it back with these judges who have the criteria, and you've set those out in the rules, and they're applying those criteria -- hopefully -- to the different entries. And if you don't adhere to the rules that you set out, and your judges don't do their job right, that can create issues.

So one of the references in the materials is to a Salesforce contest where they were trying to incentivize developers to create apps for the Salesforce software platform and they had these criteria about you couldn't be a Salesforce employee and you had to do certain things and it had to be done in a very set period of time and it was going to be judged by independent judges.

And then, low and behold, they announced the winner and the winner was supposedly somehow related to or composed of partly a Salesforce employee. This was for a million dollar prize. So after they got this complaint and a lot bad publicity on social media, which is another thing to think about when you are encouraging participation on the internet, it can also be a way of people commenting on what you are doing.

Salesforce announced a second prize to a different group and the complaints were out there about that group and how they were still violating the rules that Salesforce had set out. So, I think you have to sort of monitor what is going on -- and an important part of this is not only having rules and creating a contract that the people that are participating in the promotion, but also to adhere to those rules and not just unilaterally decide you're not going to adhere to those.

So, the public can participate and be engaged, but how they're engaged and how much a factor they are can very well impact which bucket your particular promotion falls into. Is it just a random drawing in effect or is it a skill contest where you can have more control about what is happening.

Mintz: So let's turn to the darker side of our topic, which is the potential liability or consequences. And Alex, let me ask you first because we're at a tax conference, talk a little bit about the tax consequences to these different types of contests and awards and how they may break down in and the sort of pitfalls that we might need to be concerned about.

Reid: I'd say that the main set of tax questions are around "Is this a charitable activity or not?" And so, depending upon the size and extent of the prize -- I don't know if we're talking about a hundred million dollar prize -- you know, maybe that can have an impact on your exempt status. What's kind of interesting and challenging about analyzing these contests from a tax perspective is that it's like a law school 101 exam: income tax accounting. Is there income? Or is it a payment that is excluded from income?

Who really benefits from the prize? Is it the charity that offered the prize? Is it the public? Is it some identified charitable class? Are the contestants themselves part of a charitable class? And of course once you figure out the income tax accounting questions: is there income, yes or no? Does it fall into an exemption?

Then you layer on the form withholding tax questions on top of that. So if you have non-resident aliens participating in the contest and maybe there are services involved, is there U.S. source income? So there's kind of a broad range of tax questions. I mean the biggest one for charities is preserving their exempt status, but I think it's not -- getting crosswise on foreign withholding and whether your contestants have taxable income or not is also pretty serious.

Mintz: So, Shelly, what are some of the other potential legal consequences or liability, or Alex, this question is directed to you as well in terms of we know there's some tax consequences, you have to make sure you're following the right rules, withholding and so forth, but talk about some of the other

potential pitfalls from the legal liability standpoint and some of the complexity. You've touched upon this a little bit, but some of the complexity of the state rules -- who are likely plaintiffs. And then Alex I'd like to come back to you just as a placeholder to talk a little bit about this charitable purpose element, which I think would be of interest to everybody.

Alpert: Really, there's a broad range of potential people. As I referenced in the Salesforce example, it could be disgruntled participants who spent time and energy creating something and they feel that they've been treated unfairly. It can even be the prize winner in the sense that they think that the prize they were awarded wasn't what was described in the rules that they understood that they were participating in. And, it can also be the government.

A recent case that was brought by the federal government, which was kind of interesting, and it was brought against the Ironman. For any of you that aren't athletically inclined, the Ironman has been running, I think, for probably ten years and has sort of various stages. You can do a triathlon locally and if you get qualification -- if you were fast enough in biking, running and swimming -- you can qualify for the big one in Hawaii.

Apparently for a number of years now, they were also offering the opportunity to qualify for the World Championship by paying either -- for awhile I think it was \$50 and then it went up to \$80 -- to enter a drawing where you would pay your money of \$85 which wasn't the participation fee which was several hundred dollars that everyone pays for this race. But just to win the chance, even though you hadn't qualified to participate in the event in Florida and the U.S. government filed a lawsuit and said that's an illegal lottery because you're asking people to pay money for a random drawing and you're awarding a prize -- the prize being participation in what they would otherwise have had to qualify for at an event. And they actually had to turn over, as a result of this they settled, and paid to the federal government all of the profits that they had gained over I think it was a three-year period from these sweepstakes events.

The back story that someone wrote, which I think is kind of interesting, is why did the federal government spend their time and money bringing this case? Why wasn't it a state proceeding? And the one article that I read, which shows you where the potential plaintiffs are, the motivation -- whether it be government or private -- was that one of the U.S. Attorneys in Florida involved with this case was a big triathlon participant and he was irritated that people could buy their way in to the World Championship and he thought that that was wrong and decided that this was a case to bring.

So there's a lot of different motivations that prompt people to raise issues and while they're not the most common kind of litigation, a lot of these things wind up getting resolved behind the scenes because people don't want the bad publicity from it, number one. And there's just a lot of potential, people that are looking at it -- whether it's state governments, the federal government or just the people who are participating or the people who are offended by what you are doing.

Mintz: I think your comment earlier about social media is a really important one too as we've seen in any number of different instances and different areas and industries that taking a misstep you can get a real piling on effect in terms of the use of social media. Alex, when you referred earlier to about the charitable purpose, are you aware of any of these prizes or awards or contests that are funded by foundations or public charities in which there was a question whether the award itself or the purpose of the award ran afoul of charitable purposes and there was really a question that arose?

Reid: Well, if you go back to the '86 Act, before that time there were scholarships and prizes that weren't limited in the way that they are now and gifts also were not. So, you have section 102 now that applies to gifts -- gifts are excluded from gross income. Section 74, certain prizes are excluded from gross income, and in section 117 certain scholarships are excluded from gross income.

So, before the '86 Act, these terms weren't very well-defined, or maybe they were used in more of their colloquial common understanding of them. A scholarship would be the way most people think of scholarships -- payment to help someone get education. Now, when we say scholarship as tax lawyers, we mean qualified tuition and related expenses, full stop.

That's a result of the '86 Act changes and limitations that happened because there were some abuses. Particularly companies trying to provide compensation to employees through a scholarship, through a prize, that weren't subject to payroll taxes, weren't subject to income taxes, weren't subject to foreign withholding taxes because they were excluded from income.

So the '86 Act considerably narrowed each of those concepts and, as a result of that, there tends to be this real disconnect between tax lawyer speak when we say scholarships we mean qualified scholarships and what everyone else means when they say scholarships. So, to answer your question, have there been problems with that, I think the reason that we have complicated rules now is kind of a result of the Wild West that was the early 1980s.

Mintz: So in competitions where the recipients may not be individuals, but organizations, what kind of considerations should a charitable organization give in terms of the criteria to winners? In other words, can it be a for-profit entity? Can it be a collection of people who are loosely affiliated for purposes of entering the competition? Can they do anything -- if the competition is more wide open, as the potential one we're thinking about -- are there limitations in terms of what people can do with the money that might have either tax or liability consequences?

Reid: I guess the big take away for all of this is to put the competition into the right tax boxes before you run the competition and don't do the competition first and then try to unscramble the omelet and talk to the tax lawyer then. Because if you figure it all out in advance, you can draft all of your agreements in such a way that we know that this is not a payment for services, we know that this is a payment in order to encourage charitable activity, we can put some definitions about what we mean when we say a charitable activity.

So that's kind of my overall thing. Talk to your clients, make sure -- there's a whole new cottage industry of consultants that help exempt orgs develop their competitions and they're great, they've got lots of creative ideas, lots of people working for them on your social media campaign, etc., but they'll do it however you want and they won't necessarily think about the tax things for you.

So, this chart is a schematic of what happens to an organization offers a prize. The person with their arms up is the winner. That represents the contestants and then there's the faceless hoard -- that's the charitable class. So you want to, when you are designing these, think about each of these elements. This prize is being offered for what exactly, to whom, and for whose benefit? It's sort of a schematic answer to your question. We can fill in the details.

Mintz: What I'm hearing in part though, many of what we would say, normal rules with respect to charity, charitable class, would apply, and the important lesson, I think, is to consult your lawyers

when you are forming these. I do think that when you look out in a lot of these things, and I was struck, Shelly, by your comment, charitable organizations can't run raffles on the internet, and you think about all the galas and so forth in which raffles are a critical part, and I would bet many of us could go online right now and find a lot of organizations offering raffle tickets online.

The other aspect of this that I think that's interesting -- we were touching upon this question -- and again, it's probably the same analysis, but private benefit and how one thinks about that and, in particular, this question of intellectual property and who gets the benefit of it. I think we're all aware of the increasing blurring lines between not-for-profit / for-profit activity, who you can fund -- the discussion this morning with Ruth Madrigal about the new guidance I think is part of that trend in terms of a lot of social entrepreneurs wanting to do good and how that fits into the charity. So, Shelly, maybe start with you in terms of a little bit about the IP issue and then Alex talk a little bit about the contours of private benefit that can be less clear.

Alpert: I'm just going to back up a little bit and make a comment that there definitely are people online thinking that they can sell raffle tickets. I had a client that was doing that and I went "Whoa! We gotta stop right now and you've got to return all the money and we'll start over and do it the right way." I mean, someone had come to them -- some singer, I can't remember who it was, that shows it was awhile ago -- and offered to give them to raffle off a Mustang and her original recording and something else and, of course, they jumped at it and put it up online and she sang her song and then they came to me.

Which was unfortunate, but that raises the other issue in my next statement is that consultants oftentimes have a model that they want to use and they don't think about the nuances of what you want to do versus this model. And what might work as a model for a \$1,000 prize is not necessarily going to work as a model for a \$100,000,000 prize or something in between. And it all depends on what your goals are and how you want to implement them as to how you should structure and define the contest and the rules.

That's a very important thing to do beforehand versus when you're right at the threshold of publically announcing what you're going to do. I can't tell you how many times I get a call at the 11th hour, somebody is going public with these rules like in a week and they want to turn this around and that's a disaster.

And so I really think if you're going to do anything particularly with a large prize threshold, you really need to spend a lot of time sort of looking into your magic eight ball and figuring out what the problems are likely to be. We all can brainstorm and it's a really important part of what you're doing because you need to think of every step of the way what could happen and how you can address that in your rules. And that's your contract. And that's your enforceability, both to limit your liability and also make sure that people know what they're getting involved in. If you can be as clear in your contract as you would in any other contract you can eliminate a lot of the risk and really create the kind of buzz that you want to create. So it's a really important thing to do.

That directly relates to the question, which is intellectual property. Because there are a lot of issues, particularly when you are asking -- I think this morning's example about creating something to eliminate the kerosene stoves in the Third World and -- there are, effectively, contests that tax-exempt organizations are trying to encourage new ideas, new awareness, new approaches and those then raise a huge number of intellectual property issues as well as tax issues.

So, it's like a movie company that gets scripts submitted to them all the time and then gets sued because they've used somebody else's ideas. You have to address those intellectual property issues upfront. You need to make it clear who owns the idea or what your organization can do with it because what if somebody submits an idea, it's not chosen, but five years from now, independently, not even remembering that it was an idea submitted to your organization, you implement something. Is that disgruntled person -- or even if they're not disgruntled before, they will be now that you're suddenly promoting their idea that lost the contest. So you want to be sure that you address that issue just like any business, hopefully, would address that issue as well.

You also have some concerns on the other end in terms of being more defensive, you want to make sure that this is an original idea of this person, or entity, that they didn't take somebody else's idea and submit it to your contest. And there's limitations to what you can do, but you can certainly put these things into the rules. Likewise, if it's an individual that you are having enter the contest you want to make sure that it's not some idea that their employer really owns because a lot of people have agreements, especially in the technology industry, that what they do is owned by the corporate entity, not by them individually. So you need to think through these kinds of issues in terms of intellectual property as well and spell it all out in the rules so everybody knows what's involved and you minimize the risks to your organization as well.

And then there's another concept that you need to think about if you're going to be publically vetting these or crowdsourcing these and these ideas are going to be made public. You need to make sure that that's clear in the rules because if somebody loses and they want to use this idea in some other way they may not be interested in that. You want to be able to, if you're going to use people's names, you want to have rights to publicity so that you're not blindsided when you say this is somebody's idea and they say: "Well, you didn't have the right to use my name and you're using it to promote your organization."

So there's a lot of things, like I say, you need to really brainstorm and think about and be as inclusive as you can. And even then there will be times when you haven't thought of everything and you have to, sort of, as the contest -- especially if it's a long contest like some of these big prizes are -- they can last for multiple years and have different stages before a winner is actually chosen.

Mintz: I think you've really touched well upon some of these viability questions out of IP and the contests that we have supported, or competitions, it's always been one of the thorniest issues in terms of trying to get clarity in your rules in the so-called contract and especially when teams of people are submitting ideas to be sure there's a consensus about who owns it.

But, Alex, let's talk a little bit about a hypothetical situation in which you have a contest -- it may be about the production of, it could be software, it could be some sort of invention, it's a for-profit entity that is proposing it, and what kind of things does a charitable organization have to worry about from the private benefit standpoint?

What are the sorts of things that you have to impose upon the winner in terms of sharing and where is that delicate balance? And we've seen this in lots of other instances and I know some of our friends in the audience have dealt with it in the pharmaceutical contests. So, talk a little bit about where that fine line is, if there is one, and if others have had experiences and want to provide some perspective, that would be great.

Reid: Sure, one of the ways of looking at this question of private benefit is to say “Where is the public benefit?” You have to first find the charitable piece and then see where else is the money that you’re putting out or whatever the prize is -- where else is that flowing? So, in the schematic there can be the charitable element, the something coming back to the organization. Of course, the organization being a 501(c)(3), when it engages in activities to further its mission, that is a source of public benefit, a charitable element.

Even if the recipient, the winner of the prize, is not itself a member of a charitable class, maybe it’s a taxable corporation, we know that that is a permitted kind of payment to make. We know that in particular from 4945(g)(3) so we have the taxable expenditure rules applicable to private foundations and there’s a specific carve out there. You know, Congress says private foundations shouldn’t make payments to non-charitable parties as a general matter, but if you make a payment in order to accomplish a specific objective, that is an acceptable use of private foundation funds. So, non-private foundations could also take some comfort from that statute.

Sometimes the entrants to the competition are themselves members of a charitable class. Maybe they’re school kids and the prize is something that encourages them to learn. So, these are individuals but the competition itself generates a charitable or educational benefit. Or maybe, in the example we were just talking about, the payment to this taxable party encourages the taxable party to develop some intellectual property that will then be used to benefit a charitable class. So, you know, some sort of solution. That’s Silicon Valley speak. I’m learning the lingo -- a solution. Because we don’t want to limit ourselves to an app or a service. So, a payment to create a solution to benefit a charitable class.

To get back to your question, how do we know that we really are going to benefit that charitable class? We have to write it into our grant agreement that you have to use this solution to, in fact, benefit the charitable class. And if you, the taxable party that is winning the award, are not going to do it, you have to at least allow us, the charity putting up the money, to do it. So you could get a tech company to build you some software that they own but grant you a license that allows you to use it to benefit this charitable class.

Mintz: What’s the balance on that? So you’re saying that if the for-profit can own the IP, but say it’s a school curriculum or an educational game, they have to give it to X number of schools for free? And you’re not concerned if they then use it to launch an IPO and the individuals walk off and become the next Mark Zuckerberg. Is that a problem?

Reid: Another Silicon Valley word: the unicorn. That’s a company with a billion-dollar valuation. Everyone is trying to have one of those. Well, it’s always hard to know in advance whether you’re going to have a unicorn, if you’re actually going to make money through this charitable activity. The PRI examples are -- that’s a situation foundations confront all the time. You know, making this PRI -- what if I have the misfortune of making money on my investment. Is it still charitable? I think you have to look at the facts at the time that you do it. Hindsight is 20/20 and in the future maybe you accidentally created Facebook. Maybe you can fix some of that with using the funds that are generated in that idea to give back.

Mintz: But -- in the kind of MacArthur context -- do we have to say you agree that you will donate part of your earnings to the next good cause? Or is it sufficient that I know in that context of pharmaceutical research, Gates and others have sort of said, look, if you make this vaccine available widely in the

developing world, then the ownership can be held by company A or company B and MacArthur has done similar sorts of things. So, that balance is just a case by case analysis?

Reid: With intellectual property in particular, you can look to the scientific research regulations and the publication requirement is a helpful source of guidance for concluding that some sort of public use, some sort of publication of the research or use of the intellectual property gets you into the charitable bucket.

Mintz: So, Shelly one of the questions we've talked about, some of the pitfalls, we talked about the necessity of defining the charitable class, are their classes of people or locations that are particularly problematic that we'd want to highlight today in terms of one of the benefits is opening up this participation to as many people as possible. But are there certain types of people in terms of age or geography for perhaps that you would counsel caution?

Alpert: Well, certainly you want to have somebody who is capable of entering, in effect, into a contract. So normally, you would require that the person who is participating is at the age of majority so that you are not risking any issues, especially if you're talking about developing technology and all of those kinds of things. But even if you're not, then you certainly want to not run afoul of COPPA either, so you definitely don't want to have a contest that's aimed at under the age of 13 unless you're prepared to do all kinds of hoops and other things.

The other thing is that the laws and requirements vary from country to country and what might be okay in the United States, which is really what we're talking about today, may not be legal outside of the United States, and that's important. Some countries -- like Canada -- actually has a skill requirement, although pretty perfunctory, for running any kind of contest. Like there has to be a skill question involved. So if you run a sweepstakes kind of contest in Canada before the winner can qualify, they have to answer a question. It can be $5 \times 2 = 10$, but it has to be some sort of skill question. And there are also issues about if you're offering it in Quebec that you have to do it in French.

So, it is very problematic to go beyond the United States and beyond the requirements legally, there's just cultural issues that you have to think about as well. Because in some cultures, a sweepstakes is not something that is acceptable or traditional, even though we may think they're commonplace and everyday. So you need to think about not only the legal issues that are involved, but also the cultural issues that you may be raising as well by what you're doing.

And then I think the other group of people that you have to think about is excluding from participation people that would have the appearance of conflict. Whether it's your employees, any organizations affiliated with your board members, with you, and really making this as fair and arm's length as possible so that you can avoid some of the risks that we've talked about.

Reid: I think that's a great point and we have that of course in the tax rules with disqualified persons. Often organizations want the competition to be as broadly open as possible. We want everyone to apply without really thinking about, well, do we actually want our employees, do we want our board members' children to apply and to win?

Another point is sometimes we don't even know who the recipient of the award is. If it's just a matter of filling out an online form, and some individual has filled that out, when you go to make the payment you may discover that that person was actually speaking on behalf of a group of people. Some of them,

maybe, are non-resident aliens. They could be speaking on behalf of an entity, a taxable entity, a flow-through entity.

There could be complex subcontractor agreements -- if you're talking about a prize to create a software solution, you might have programmers in Poland who are actually doing the work to build the software. And a real big income tax question is the person who filled out the form, does that poor soul have the misfortune of receiving 100% of the taxable payment you are about to make and what are they going to do with that?

Alpert: That raises another sort of tax issue that you and I have dealt with and that's the question of, one, whether or not you should have -- especially if it's a big prize -- individuals participating as groups and how do you address the tax issues that arise from that, or whether you should require the participants to be entities so you can award the taxable prize to an entity.

These raise really complicated issues and, as you can imagine, there is a lot of competing tensions because you want to make it as available as you can to people to encourage these ideas and new vantage points and everything like that, but it really makes it a lot more complicated for you and has real issues about vetting conflicts and all kinds of things as well. So that's an issue and any prize over \$600 is reportable income, so that's another part of what you have to do and make sure you're complying with your obligations as an entity as well.

Mintz: Cognizant of time, I'm going to give a little bit of perspective and then ask both of my colleagues up here to summarize, perhaps if I don't cover it, I think the issue of what we thought about in terms of individuals too is a private foundation -- can you make a grant to an individual or do you have to get a pre-ruling?

So we know today there's a lot of continued excitement about competitions and prizes and we talked a little bit about some of the advantages of these. We didn't mean to scare everybody off by some of the challenges, but I think that the advantages still remain. I think that part of what we want to convey here today is that there all challenges to these things as well.

They can be a lot harder than they look -- there's actually some push back because everybody's doing a competition or a prize and how do you distinguish yourself in terms of why is a charitable organization you're doing it, what do you hope to accomplish? So there's some non-legal issues that you have to be concerned about, how open you want it to be in terms of transparency, who's making the selection of the criteria, are the judges' decisions open?

There are some prizes like the National Geographic Prize in which the judges' determinations are made open on the internet and anybody who was judged knows who judged -- there's issues with that, but there are proponents of openness versus closed. You know how audacious you want to make the prize versus a more controlled environment and ensuring that there might be a successful outcome.

So, there are people who feel it's way overdone, that you can't really distinguish yourself. I think some of the mitigating factors in terms of the risk -- I think the number one thing I'm hearing is make sure you have your rules clearly spelled out and have thought about it. Don't feel rushed into it to beat the next X prize or Pulitzer Prize, but really think long and hard about it, that there are some advantages to doing it, but that it isn't just simply a question of joining the herd and that both from a state and federal law standpoint, of Shelly's expertise or Alex's expertise on the tax and charitable side, there are lots of

issues to consider. So, real opportunity, but really you have to think about it in the context of what you're trying to accomplish and the practical constraints.

Alpert: I echo what you just said. I would not say you shouldn't do it. I think there have been examples of where this has been successful and you can do it without alienating anyone or causing any undue risks to the organization. It just takes time and planning and isn't necessarily simple and there is no one size fit all no matter what the consultants say.

Reid: I think those are great points. I would conclude with a non-tax point which is as tax lawyers, we're used to having the most complex rules and the most regulation, but this is an example of where the non-tax ones are actually considerably worse. And so your clients can get themselves into a lot of trouble even if they're thinking they're doing, you know -- we're just going to run a small contest, just a trial balloon, dip the toe into the water, and maybe we'll see how it goes and then maybe we'll do a bigger one later. There probably is not going to be any issue, because it's small, right? And the answer is no and in fact the risk is sort of unquantifiable, particularly if you have a completely open competition that is global.

I think part of the reason that the rules are so complex in the regulatory gambling side is that as a country we have the government occupying a monopoly on who is allowed to gamble. And the government runs lotteries. In other countries, gambling is just taboo and the government does not run - - so they're kind of more like criminal activities, whereas here you're going up against the big monopoly who is supposed to have all of the right to do gambling, mainly, your state. So, that's a large set of issues. I guess I'd just advise you to ask the GCs you work with: "Are you running any prizes that you haven't told us about?"

Mintz: There's a growing body of literature on this. I have some materials I collected when Shelly and I did this at Georgetown a few years ago, and I'm sure it's probably doubled since then, but if anybody is interested, I'd be happy to send those around. So, any questions?

Borenstein: Eve Borenstein, Minneapolis. In your summary, I appreciated, and in the slide I appreciated, the highlighting that there's rules that you really need to check here. This area is so mistreated on a state law basis by practitioners who have looked at the state gambling statutes which typically will allow charitable organization or a nonprofit organization in existence for a certain number of years to do raffles of this or that, and it's unbelievable to me how the baseline rules get ignored. A raffle, legal in one state, does not allow you to sell five tickets for \$25, but each ticket stand-alone is \$7. I mean, so we need to impress upon our clients that copying what somebody else has done is the perfect way to ensure yourself that you're in trouble.

Lion: Ofer Lion, Los Angeles. Where, by the way, the next ABA meeting will be. And there is a 1 in 50,000 chance that I'll invite you all to my new beach house in Santa Barbara. But my question is sort of towards that cottage industry that you mentioned, and I know you the likes of Charity Buzz will auction off whatever you want and they take 20% and I just wondered if you had any thoughts or guidance on how these sort of service providers can structure their payments? Can it be sort of a percentage of the amount raised in the sweepstakes or raffle or whatever?

Reid: You're asking whether the promoter or a consultant can take a percentage of whatever is raised. As a kind of a section 170 matter, the rules really do allow fundraisers to take an awfully large percentage of whatever is raised and that doesn't seem to affect the deductibility of the contribution.

You know the Posner decision in the *United Cancer Council* case didn't make clear, but the issues lurking around there is whether there is private benefit, if there's a relationship between the promotor and the charity, and the promotor is taking an exceptionally large chunk. Does that jeopardize the exempt status or is there maybe an excess benefit transaction?

Alpert: Well, it depends on where you are doing it and how you're promoting it and it sort of raises the issues. I mean it's just a matter of how you promote it. So a lot of the -- you know, there's eBay that does a lot of charitable auctions, and that doesn't violate any particular state law. But when you get into raffles in particular, there's a huge host of laws and everybody has their own draconian approach to this. And every state has to be looked at and the idea of doing a national raffle is just not viable. People don't understand that. There's a lot of aspects of these laws that are not logical, is what I would say. You wouldn't think it would be this way, so if you decide you're going to go with common sense, that's not a good idea, necessarily.

Franklin: Jennifer Franklin, New York. I just wanted to make sure I understood a point that Shelly made before. Which is I see a lot of these online contests where the public votes for, you know, a list of charities, one of a list of charities or any charity in their community, and then the charity gets a grant from a company or a foundation or another charity. And, as long as the public is not paying to enter that contest, I understand that doesn't violate state laws, correct?

Alpert: Right.

Franklin: Okay, just wanted to make sure.

Alpert: And, like I say, you can do a sort of a crowdsourcing contest, as long as there is no consideration that is dominant, and that you have an alternative means of entry. It's when the crowd is determining a winner and someone is paying to enter that it becomes an issue.

Mintz: Okay. Thanks everybody.