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## Coates' Canons Blog: “Bah, Humbug” Gamers Say: Video Sweepstakes Statute Upheld

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If you are looking for a last-minute holiday gift for someone at this time of year, you may want to forego purchasing your friend or relative a gift card at the local video sweepstakes operation (VSO). That gift card may not be worth so much in the new year, if law enforcement personnel in North Carolina have their way. Plans are now afoot to close down these operations in light of the North Carolina Supreme Court's decision last week. In *Hest Technologies, Inc. v. State ex rel Perdue*, the court upheld the constitutionality of the statute that makes it a criminal offense to conduct video sweepstakes games “through the use of an entertaining display.” (G.S. 14-306.4(b)). Game sponsors may now seek to block enforcement of the law, pending an appeal to the United States Supreme Court. The purpose this blog is not so much to trace the history of North Carolina's attempt to regulate gambling and sweepstakes operations or to analyze the key legal doctrines in the *Hest Technologies* case. (See my earlier blog and the blogs of my colleagues Dave Owens, Chris McLaughlin, and Jeff Welty.) Instead the purpose is to consider what implications the decision has for those communities that are currently regulating such establishments through zoning.



A very brief history is in order. In 2006 the North Carolina General Assembly banned video poker and other forms of electronic gambling. Since then promoters of gaming software have developed systems intended to skirt gambling restrictions by combining otherwise legal sweepstakes activities with video games that simulate a gambling environment. The purpose has been to rid this activity of the betting element associated with gambling. Originally, the software used simulations of poker or classic slot machine play to reveal the game results, but that practice was banned in 2008. In reaction to this legislation, promoters modified their systems to simulate a broad range of new games so that the action did not simulate poker or slot machine play. G.S. 14-306.4 became effective on December 1, 2010, and made it illegal to operate an electronic device to be used by a sweepstakes entrant involving any kind of an “entertaining display.”

As a result of a suit brought by software developers and promoters, the North Carolina Court of Appeals ruled earlier in 2012 that both the announcement of the sweepstakes result and the video games themselves were protected speech under the First Amendment. In a 2 to 1 decision it held that because the definition of an “entertaining display” was virtually unlimited, the sweep of the law was unconstitutionally overbroad.

On December 14, 2012, the North Carolina Supreme Court reversed, ruling that G.S. 14-306.4 primarily regulates non-communicative conduct rather than protected speech. The court noted that operating an electronic machine involves conduct, not speech. Promoters are free to provide video games to their patrons and their patrons are free to play them, thus enjoying whatever message is communicated by the video game, but only so long as the games are not linked to a

payoff associated with gambling.

Interestingly enough, the court chose not to rest its decision on claims that the sweepstakes operations were a mere pretext for gambling in disguise. It noted that there was no evidence in this case that Internet time and telephone calling cards sold by sweepstakes establishments to trigger play were not actually used by customers. Such evidence might have supported the idea that their sale was a mere pretext for initiating the gambling scheme to follow.



The effect of the decision is to vindicate G.S. 14-306.4, which first became effective in 2010. What, then, are the ramifications of the decision for local governments that have been subjecting sweepstakes sponsors to zoning requirements in the recent past?

(1) First, zoning cannot make legal that which the state makes illegal. Now that the statute has been upheld and injunctions against its enforcement dissolved, zoning no longer applies to video sweepstakes operations that are subject to G.S. 14-306.4, which are now unlawful. This result stems from the preemption rule provided for in G.S. 160A-174(b)(3) that an ordinance is inconsistent with North Carolina law (and thus preempted) if it makes lawful an act, omission, or condition which is expressly made unlawful by State or federal law. If enforced, a zoning ordinance that allows sweepstakes operations under express circumstances set forth in the ordinance could be viewed as intending to make such operations lawful despite the fact that G.S. 14-306(b)(4) makes them unlawful. Such a zoning ordinance regulation would thus be inconsistent with G.S. 14-306.4 and be invalid. As noted below, however, it seems likely that the industry will try once again to alter its methods of operation so that establishments are not subject to the criminal sanctions of G.S. 14-306.4. If they succeed in coming up with a new lawful form of entertainment, then zoning may once again apply.

(2) In order to avoid the preemption problem described in (1) above, local zoning officials should leave enforcement matters to state and local law-enforcement officials to determine when and how to proceed to enforce the criminal law. This is particularly true in light of the possibility of a further appeal by the plaintiffs and another injunction prohibiting the statute's enforcement. There is no need for zoning officials to revoke outstanding certificates of occupancy held by existing video sweepstakes operators. However, if a sponsor is in the midst of the approval process for a new video sweepstakes operation subject to G.S. 14-306.4, no further development permissions, approvals, or reviews should be granted.

(3) Should a local government amend its zoning ordinance in light of the *Hest Technologies* decision? A number of larger local governments have adopted standards and zoning requirements tailored to video sweepstakes and "Internet cafes." Some localities use definitions and standards that directly refer to G.S. 14-306.4 or use much the same language as the statute. If so, a city may simply delete the relevant portions of the ordinance that are tied directly to G.S. 14-306.4 by repealing them. Or, as a less attractive option, it may also simply leave the regulations in place, but avoid enforcing them. In other instances, however, ordinance definitions and standards may not be tied much to the criminal statute. If an ordinance treats a video sweepstakes operation as an "arcade," or an "amusement center," or some other more general class of land use, then a local government may continue to rely largely on the ordinance's existing terminology. In this latter instance a locality might add language restricting arcades or amusement center or other similar uses to those uses that are "otherwise lawful." Because it is expected that the industry will try to alter its operations to develop a harbor safe from the criminal law, the use of broad zoning categories to classify these entertainment uses has its advantages.

(4) Some may suppose that the *Hest Technologies* decision finally clarifies once and for all that the operation of video sweepstakes is unlawful and that simulated gambling will fade away. But history has proven how creative and persistent the promoters have become in devising new ways to circumvent the law. For example, the industry may now try to develop a routine that avoids "an entertaining display." (Of course, as my colleague Chris McLaughlin has pointed out, it is unclear why anyone would pay good money for displays and routines that are not entertaining.) In any event the attraction of gambling and lotteries in the future may grow. Local government leaders, planners, attorneys, and zoning officials will be called on to respond again. For now we may have come to the end of a chapter in this saga, but it is unlikely that we have seen the end of the story.

So, you may want to forego buying a relative or friend a gift card at your local video sweepstakes parlor this holiday season. But who knows what future seasons may bring.

## Links

- [appellate.nccourts.org/opinions/?c=1&pdf=MjAxMi8xNjIjBMTetMi5wZGY=](http://appellate.nccourts.org/opinions/?c=1&pdf=MjAxMi8xNjIjBMTetMi5wZGY=)
- [www.ncleg.net/EnactedLegislation/Statutes/HTML/BySection/Chapter\\_14/GS\\_14-306.4.html](http://www.ncleg.net/EnactedLegislation/Statutes/HTML/BySection/Chapter_14/GS_14-306.4.html)
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- [www.ncleg.net/EnactedLegislation/Statutes/HTML/BySection/Chapter\\_14/GS\\_14-306.1A.html](http://www.ncleg.net/EnactedLegislation/Statutes/HTML/BySection/Chapter_14/GS_14-306.1A.html)
- [www.ncleg.net/EnactedLegislation/Statutes/HTML/BySection/Chapter\\_14/GS\\_14-306.3.html](http://www.ncleg.net/EnactedLegislation/Statutes/HTML/BySection/Chapter_14/GS_14-306.3.html)
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