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## GENERAL COUNSEL NOTE

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April 2008

Vanderbilt has a rich tradition of charitable giving. Whether through university sponsored opportunities like the Faculty Staff Campaign, the Vanderbilt Community Giving Campaign, or support for national campaigns like the Heart Walk (American Heart Association), Daffodil Days (American Cancer Society), or simply individual commitments to donate time or resources to local community organizations, Vanderbilt employees participate. Because the Vanderbilt spirit embodies creativity and entrepreneurial talent, employees often develop unique methods of maximizing giving efforts. For example, this office has received calls asking whether employees can raffle donated gifts. Since state law prohibits certain types of activities, the purpose of this article is to provide some information to contemplate when those creative juices start flowing.

### **Can we run a casino night?**

Certain types of games or competitions are forms of gambling. Gambling is regulated by the Tennessee legislature and is prohibited.<sup>1</sup> State statute defines gambling as “risking anything of value for a profit whose return is to any degree contingent on chance, or any games of chance associated with casino, including but not limited to, slot machines, roulette wheels and the like.”<sup>2</sup> Gambling includes chain or pyramid clubs, numbers, pinball, poker, games played on gambling devices that incorporate computer or software programs, like video slot or black jack machines.<sup>3</sup> Gambling is considered “contrary to the public policy” of the state and courts can impose criminal penalties ranging from a Class C misdemeanor which carries a minimum sentence of up to 30 days in jail and/or a fine of \$250 to a maximum of a Class E felony with sentences ranging from 4–6 years in jail. Note that a person who induces or aids another to gamble can be guilty of gambling promotion, which is a Class B misdemeanor.<sup>4</sup>

### **What about a raffle or bingo night?**

The control of gambling activity is intertwined with charitable gaming. The convoluted, erratic history of charitable gaming begins with the Tennessee Constitution adopted by the constitutional convention of 1834. Article XI, Section 5 prohibited lotteries:

The Legislature shall have no power to authorize lotteries for any purpose and shall pass laws to prevent the sale of lottery tickets in this State.

While this statement seems simple enough, the definition of what constitutes a lottery in Tennessee has taken several decades to clarify.

The definition became hotly debated in 1970’s and 80’s. Under state criminal statutes, lotteries are prohibited gambling and are defined as the “selling of anything of value for chances on a prize or

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<sup>1</sup> TCA 39-17-501 *et seq.*

<sup>2</sup> TCA 39-17-501(1).

<sup>3</sup> TCA 39-17-501(3).

<sup>4</sup> TCA 39-17-503.

stake.”<sup>5</sup> In the 1970’s, various organizations lobbied the Tennessee General Assembly to enact statutes exempting bingo and raffles from the state’s general gambling laws. The intent of the legislation was to allow various non-profit organizations, including religious and fraternal entities to conduct bingo games and raffles for fundraising purposes. The legislature rationalized that bingo and raffles constituted a form of gambling (not a lottery prohibited by the constitution) and could, therefore, be regulated by the legislature. The state’s Attorney General periodically advised the General Assembly that these “charitable bingo statutes” were unconstitutional and that the activities regulated constituted lotteries under Article IX, Section 5.6

In the late 1980’s, the Tennessee Secretary of State finally filed a lawsuit in Davidson County, challenging bingo activities of various churches and religious organizations across the state. Chancellor Irvin H. Kilcrease, Jr. issued an opinion finding the “charitable bingo statutes” unconstitutional. The organizations appealed. The Tennessee Supreme Court issued the opinion in Secretary of State v. St. Augustine Church, 766 S.W. 2d 499 (1989) which among other things, explored the definition of lottery. The Court cited Black’s Law Dictionary 853 (5<sup>th</sup> ed. 1979) as one measure:

A chance for a prize for a price. Essential elements of a lottery are consideration, prize and chance and any scheme or device by which a person for a consideration is permitted to receive a prize or nothing as may be determined predominantly by chance.

Picking up on this definition, the court indicated that the measuring stick for determining whether a game is considered a lottery is based on the presence of the three elements, consideration, prize and chance.”<sup>7</sup> The Court then reviewed specific games. The Court accepted previous court decisions founding that “opportunity night” or “bank night” programs where movie theaters awarded a cash prize to the holder of a lucky movie ticket were not lotteries because there was no consideration, or charge, to the theater patrons or members of the public who obtained a ticket for the drawing.<sup>8</sup> The court stated that lotteries are based on randomly selected numbers rather than a player’s skill; chance is involved. The Court also rejected the argument that bingo should be compared to “innocent” parlor games like dominoes or Parcheesi, (although these games required some skill on the part of the player, while bingo is simply a random drawing of numbers). The charitable organizations argued that bingo did not exist in 1835 and therefore could not have been contemplated as a prohibited lottery by the Constitution. The court rejected this argument and the rationale that “when cards for bingo play were sold by charitable, religious and similar organizations, the payment made by the customer constituted a charity contribution” rather than a wager or consideration.<sup>9</sup> In applying the elements of consideration, prize and chance the Court found that “bingo” met the measuring stick to constitute a lottery. The Court indicated that the appropriate manner to legalize bingo is repeal or amendment of Article XI, section 5 of the Constitution.

Charitable organizations were concerned about the Supreme Court’s decision. As noted in the St.

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<sup>5</sup> TCA 39-17- 501(5).

<sup>6</sup> Op. Atty. Gen. No 84-141, April 26, 1984.

<sup>7</sup> *Secretary of State v. St. Augustine Church*, 766 S.W. 2d 499, 501 (1989).

<sup>8</sup> *State ex rel. District Attorney General v. Crescent Amusement Co.*, 95 S.W. 2d 310, 312 (1936).

<sup>9</sup> *St. Augustine Church*, at 500.

Augustine Church decision, “receipts from ‘bingo’ operations in TN totaled thirty-one million dollars in 1987.”<sup>10</sup> Law enforcement officials were also concerned, but for a different reason, as they were engaged in the “Rocky Top” investigation. During the 1980’s, it was alleged that professional gamblers utilized charities and churches as fronts for casino-like games. Federal investigators found that most of the proceeds of games being run under the auspices of the “charity bingo and raffles statutes” did not actually go the charities.<sup>11</sup> “Rocky Top” resulted in several public officials, businessmen and others being indicted and convicted. The charitable bingo statutes were repealed in 1989.

### **What about an invented game?**

While the Supreme Court had provided the basis for evaluating whether a transaction was a lottery, charitable organizations continued to develop games in the hope that the particular game would not be considered a “lottery.” For example, “annual rubber duck races” continued to be held through 1997 (about 8 years after the St. Augustine Church decision). Knoxville, Nashville, Chattanooga and Kingsport provided local events where individuals were asked to consider a gift of \$5.00 to adopt a rubber duck, with the proceeds of the event donated to a local charity like the Boys and Girls Clubs. As many as 60,000 yellow rubber ducks were released into a river or lake at one time to float along a predetermined course. The participating individuals whose assigned ducks were first to cross the finish line were awarded prizes, such as cars, tractors, gift certificates, and cash. In 1997, the Attorney General’s Office determined that the suggested donation to adopt the rubber duck was really a ploy to acquire a chance to win one of the advertised prizes.<sup>12</sup> While the Attorney General’s opinion stated that a prize giveaway generally lacks the element of consideration and is not a lottery where the participants can play without paying a money donation. Upon application to the rubber duck races, merely labeling payments as a suggested or voluntary donation does not alter the fact that consideration is present, and therefore, found the races constituted a lottery.<sup>13</sup> Raffles where participants purchase a ticket to be eligible for a prize or cash are still illegal lotteries.<sup>14</sup>

### **What about the state lottery?**

In order to allow Tennesseans to purchase lottery tickets without driving to Kentucky or an adjacent state, Tennessee had to amend its constitution. The General Assembly passed a resolution calling for a referendum on the ballot that was voted on by the citizenry of the state on November 5, 2002. As a result, Article XI, Section 5 of the Tennessee Constitution currently allows the legislature to authorize a state lottery as long as the net proceeds are allocated to “provide financial assistance to citizens of this state to enable such citizens to attend post-secondary educational institutions.” Tennessee developed a “Hope” scholarship program under which Tennessee students who meet certain academic requirements receive grants that are applied to education costs at Tennessee colleges and universities. The amendment also allows any excess to be used for K-12 educational facilities, early learning and afterschool programs. Various programs using excess lottery earnings

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<sup>10</sup> Ibid., at 501.

<sup>11</sup> “*The Tennessean*,” 12-3-89.

<sup>12</sup> Op. Atty. Gen No. 97-025, March 19, 1997.

<sup>13</sup> Ibid.

<sup>14</sup> Op. Atty Gen. No 03-49, April 22, 2003.

and unclaimed prizes have been implemented for at-risk children through afterschool programs and pre-kindergarten quality initiatives. All other forms of lotteries continue to be prohibited unless authorized by a 2/3 vote of all members of the General Assembly for an annual event to benefit a 501(c) (3) organization.<sup>15</sup>

### **What about a silent auction?**

Auctions are regulated by statute and are defined as “a sales transaction conducted by means of oral or written exchange between an auctioneer and member of the audience, which exchange consists of a series of invitations for offers for purchase of goods or real estate made by the auctioneer and offers to purchase made by members of the audience culminating in the acceptance by the auctioneer of the highest or most favorable offer made by a member of the participating audience.”<sup>16</sup> An auction is not considered a lottery, as it lacks the elements of prize, chance and consideration. Whether a silent auction is a lottery depends on the factual situation. Some of the issues to be considered are whether anyone can participate or must participants purchase a ticket. Are the tickets auctioned? Is a portion of the selling price of the tickets set aside and paid the organization sponsoring the event? Depending on the structure, the silent auction may actually be considered payment of money for a chance to win a prize.

### **What about the Steeplechase?**

Since the constitutional amendment allows flexibility, as long as the Tennessee legislature approved the type of lottery/game, the general assembly passed a statute allowing charitable organizations to create fundraising events.<sup>17</sup> Events meeting the specific requirements of this charitable gaming statute are exempt from punishment under the state gambling statute.<sup>18</sup> The Iroquois Steeple Chase, named after Iroquois, the first American-bred horse to win the English Derby and set out to stud at the Belle Meade Mansion, has been an annual Nashville event for about 66 years. Currently conducted by the Volunteer State Horsemen’s Foundation in association with the Friends of Vanderbilt Children’s Hospital, it is sanctioned under the Tennessee Charitable Gaming statute.

Under the charitable gaming statute, passed in 2004, TN organizations with tax exempt status under section 501(c)(3) of the federal income tax code can sponsor one annual fundraising event to benefit a particular organization. The annual event may include a single type of lottery game, must be conducted on one event date and must be authorized by 2/3 vote of all members of each house of the TN General Assembly. Acceptable lottery games include raffles, reverse raffles, cakewalks, or cakewheels. Raffles and reverse raffles are defined as games where the participant is required to purchase a ticket or chance to win a prize through a random drawing. Cakewalks or cakewheels are games where a wager is made and the winner is randomly selected by walking to music, colored space, a spinning wheel, or drawing. Other games are unacceptable and can be prosecuted under the gambling statutes. For example, organizations cannot operate instant and on-line lottery games such

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<sup>15</sup> TN Const. Art. 11, § 5, Amendment adopted in Convention Feb. 15, 2001, approved at election 11/5/02.

<sup>16</sup> TCA 62-19-101(2).

<sup>17</sup> TCA 3-17-101 *et seq.*

<sup>18</sup> TCA 39-17-501(1)(B).

as those operated by the Tennessee Education Lottery Corporation, keno, or games of chance associated with casinos including, slot machines and roulette wheels. Additionally, bingo, instant bingo, video lottery, pulltabs, and punchboards cannot be utilized to raise money for the organization.

An application outlining the details of the event, including the type of lottery game, number of tickets, and location of event must be filed with the Secretary of State. The organization has to pay an application fee up to a maximum of \$700, which the Secretary uses to defray the cost of administering the program. The applications are reviewed very carefully. The event must support a charitable, religious, educational, scientific or other humanitarian purpose or program. The organization must have been in existence for at least 5 years preceding the event date and submit an application each year (even if the event is the same) to the Division of Charitable Solicitations (in the Secretary of State's Office). Tickets or chances can be sold in any political division of the state. Organizations may hold joint events, as long as each participating organization meets all the statutory qualifications (like tax exemption). The event must be managed, conducted, and operated by directors, officers, or employees of the organization(s). Unpaid volunteer personnel must run the event. Directors, officers, and employees cannot receive any benefits from the event, (e.g. rent for facility). All gross proceeds, less expenses, must be returned to the sponsoring organization for the programs described in the application. The charitable organization must justify to the Secretary of State any return less than 25% of gross proceeds.

A list of qualified organizations and events is sent to the legislature by March 1 for a vote. All approved events are posted on the Secretary's website. Any organization whose event is rejected may obtain review at the Tennessee Claims Commission upon the standard that the Secretary acted in an arbitrary and capricious or clearly erroneous manner. Monetary damages are not available.

Organizations are required to keep records and must provide a final accounting to the Division of Charitable Solicitations within 90 days after the event date in the application. An audit is required if the event grossed more than \$50,000. The Tennessee Bureau of Investigation (TBI) investigates any violations of this law.

## **Conclusion**

If you are contemplating an event to assist Vanderbilt in fundraising, and plan to utilize some form of game, please contact this office to make sure your event will meet legal requirements.

This Note is for informational and educational purposes only.  
It states general propositions and is not intended to  
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