

Findings

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Losing the Lottery

Why the State Should Not Enter the Gambling Business

By Stephen Daniels



For over 20 years, legislation has been introduced in the North Carolina General Assembly to authorize a lottery. As bills are introduced each session, so another round of debate is kicked off about whether a lottery is a smart policy for state government.

Advocates for a lottery promote it as a revenue stream that would help to fund worthwhile programs for the state. In a time of budget shortfalls and an increase in the perceived needs of the state, the prospect of another revenue source like the lottery remains appealing to some. But the question must be asked: Is putting the state into the gambling business really the best way to address these economic issues?

For more than 20 years, North Carolina lawmakers have rejected a lottery, and rightfully so. There is a mountain of evidence showing that a lottery is bad public policy because it creates multiple social and economic problems. After all, the lottery is gambling. And if gambling becomes the accepted public policy of this state, there will be negative consequences. This paper reviews these consequences, including the social and economic issues, as well as the constitutional case against a statewide referendum.

Real People, Real Effects

Amid talk about the benefits of a lottery, there is a deafening silence from proponents when it comes to the issue of gambling addiction. If statewide gambling is introduced in North Carolina, the question will not be whether gambling addiction will increase, but to what extent this damaging consequence will devastate individuals and families across North Carolina.

Unlike “destination” gambling such as casinos and racetracks, the lottery makes gambling accessible in local venues all across the state. When you add legality, and state promotion to accessibility, this guarantees that many citizens will gamble, including many who have never gambled before and would never go to a casino or racetrack. Unfortunately, a significant number who play will become problem or pathological gamblers, including those who would have never suspected that this “harmless fun” would result in a gambling problem.

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According to a Harvard Medical School study, over five percent of the adult population is addicted to gambling.¹ Among youth, this percentage rises to between 13 and 20 percent.² This means that if statewide gambling is prevalent here, over time approximately 400,000 North Carolinians will develop some kind of a gambling problem.³

Research shows that gambling addicts suffer a multitude of problems such as divorce, crime, unemployment, child abuse and neglect, domestic violence, depression, suicide and even committing murder.⁴ About one-third of problem and pathological gamblers have been detained or arrested by police, and about 21 percent of pathological gamblers and 10 percent of problem gamblers have been incarcerated.⁵ Several studies have found higher rates of depression among pathological gamblers (gamblers with the

most serious form of addiction) and shown that problem gambling actually causes depression.⁶ In one survey of hundreds of Gamblers Anonymous members, two-thirds had considered committing suicide, 47 percent had a plan to take their own life, and 77 percent stated that they wanted to die.⁷

Gambling addiction’s impact is equally devastating to the addict’s family who bears the brunt of the negative consequences. Among Gamblers Anonymous members, between 26 and 30 percent attribute their divorce or separation to their addiction.⁸ Drinking, smoking and overeating among the spouses of compulsive gamblers are common.⁹ In addition, children of problem gamblers are more likely to smoke, drink and use drugs.¹⁰ They also are more likely to develop their own gambling habits.¹¹ Families of compulsive gamblers often suffer from physical and emotional abuse as well. According to one study, 23 percent of spouses and 17 percent of children of problem gamblers are physically and emotionally abused.¹²

This reality puts a new face on the image of “harmless fun” often given to the lottery. It also raises the question: Should the state ever proceed with a policy, which will adversely affect hundreds of thousands of people across the state?

The Regressive Lottery Tax

Lotteries are harmful to lower income citizens, because those who can least afford it spend significantly more of their income playing the lottery than do those with higher incomes. Duke University professors Charles Clotfelter and Philip Cook found that lottery players with annual household incomes under \$10,000 wagered nearly three times as much as those with annual household incomes over \$50,000.¹³ They also found that the highest per capita spending on the lottery

is among those who have not completed high school, with high school dropouts spending almost four times as much annually as college graduates.¹⁴ A study by the Maryland Department of Planning found that the Zip codes with the highest lottery sales were home to the largest minority population, highest poverty rate, lowest educational attainment and lowest median household income.¹⁵ An analysis by the *Atlanta Journal-Constitution* found that lottery players in poor Georgia communities were largely financing HOPE scholarships for students in middle and upper class families (students who would likely attend college without a HOPE scholarship).¹⁶

The regressive nature of the lottery should be a huge red flag to legislators, especially considering that the state government is the agency operating and promoting the lottery. Ironically, the lottery, which is publicized to benefit education and underprivileged children, is the same program that seeks to take advantage of them.

The Economic Costs

The lottery is so often characterized as a way to raise money that the economic costs from introducing state sponsored gambling are never mentioned by lottery proponents. Considering that hundreds of thousands of North Carolinians will become addicted to gambling over time, the costs to the state from crime, lost jobs and wages, bankruptcies and so forth would reach into the hundreds of millions of dollars.¹⁷ This does not include the social costs to individuals and families mentioned above.

A lottery would also hurt retail businesses because money spent on tickets would not be used to purchase consumer goods. One study showed that retail merchants in southeastern Virginia lost \$430 million in sales to the lottery over three years.¹⁸ Another study found that a lottery brings a decline in household expenditures as consumers shift their spending away from items such as food, clothing, and housing to play the lottery (a trend that is more pronounced in low-income households).¹⁹ Lost sales mean fewer businesses and fewer jobs. Every dollar that goes to a lottery is a dollar that cannot be spent somewhere else—or saved.

The lottery also affects state and local tax revenues as lottery players spend money on tickets instead of goods and services. Estimates vary, but a lottery could cost between \$31 million and \$36 million in lost state and local taxes.²⁰ It is

also worth pointing out that the state and local tax burden is higher in lottery states than in non-lottery states.²¹

The Money Myth

Money is always the big selling point of a lottery. After all, the stated purpose of a lottery is to “maximize new revenue to the State.”²² But is the lottery a windfall of cash for the state? The answer is no. The lottery would bring in only a fraction of the money necessary to fund education.

Estimates vary on the exact amount of money that a lottery would generate for North Carolina, but a reasonable figure is around \$366 million a year.²³ This would account for approximately 2.3 percent of the \$15.9 billion 2004-05 state budget²⁴ and approximately 4 percent of the \$9.2 billion that North Carolina appropriated to education this same year. This is far less than the “cash cow” that lottery tax proponents often portray.²⁵ (See chart below)

One of the most common reasons given in support of a lottery is “all that money going to other states.” Lottery proponents claim that hundreds of millions of dollars that could benefit education are being lost to surrounding states. Lottery advocates are misleading the public when they talk about the gross dollars that are spent on tickets, not the net dollars kept by the states. It is important to understand that fifty cents of every dollar spent on a lottery ticket is returned in prizes and the state only keeps a third of every dollar to fund their education programs.²⁶ This means that if North Carolinians spend \$250 million in surrounding states, as has been estimated, net revenues taken in by those states is around \$85 million, which amounts to less than one percent of North Carolina’s education budget.²⁷

People have been sold the idea that a lottery is a way to create additional revenue without having to raise taxes. But the fact is that states with lotteries do not spend more on education. Research shows that lottery states are likely to decrease the rate of growth in education spending, compared to non-lottery states.²⁸ In other words, states that do not have a lottery actually increase education spending at a higher rate than lottery states.

In addition, because citizens believe that the lottery creates a windfall of cash, states have found it difficult to secure additional funds such as school bonds for lottery-funded programs.²⁹ Former Chairman of the North

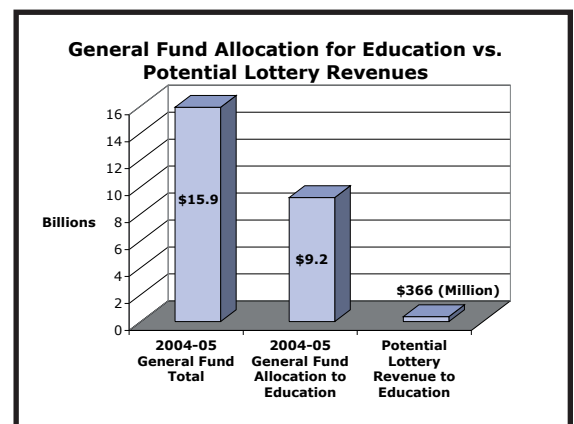
Carolina State Board of Education Phil Kirk expressed his concern saying, “We would never pass another local school bond, and it would erode county commissioner support of extra money to the schools.”³⁰ Frustrated over this same problem, California Superintendent of Public Instruction Jack O’Connell declared that the lottery “has done more to hurt public education than almost anything.”³¹

Unstable and Inefficient Funding

Many states have seen fluctuating revenues and significant drops in income from their lotteries. In 2001 (months before the events of September 11th), *Business Week* reported that 20 of the nation’s lotteries saw profits drop.³² The state of Ohio faced the biggest shortfall that year, with lottery sales off by 11 percent, leaving the state \$52 million short of its projected income for education. The state had to make up the difference from other funding sources.³³ In 2003, Ohio showed a loss of \$45.3 million and was behind in its payment to education by \$26 million.³⁴ Meanwhile, Texas lottery sales in 2001 were a billion dollars below 1997’s record sales, nearly a one-third drop in sales over five years.³⁵

Lottery supporters often point to Georgia as the model of a successful program. However, with ticket sales leveling off and the demand for lottery-funded HOPE scholarships continuing to rise, the Georgia legislature had to pass legislation in 2004 that would gradually cut benefits once revenues begin to drop.³⁶ Georgia illustrates that not even the most idealized lottery can guarantee that it will be able to deliver on its promises.

Another cause of instability of lottery revenues is “jackpot fatigue,” which sets in after the initial novelty of the game wears off. In order to stimulate more sales, states often create new and presumably more exciting games, or increase the jackpot by decreasing the odds of winning,



to invigorate interest in playing the lottery. A payout of \$50 million, once considered substantial, is no longer sufficient to generate excitement from a jaded public.³⁷ In order to beef up jackpots, some states direct a higher percentage of lottery revenues to prizes by cutting the state's profits, meaning less money for education (or for whatever programs the state has earmarked the funds). New York increased the payout from 55 cents per dollar spent on a lottery ticket to 65 cents. Even though the state saw record sales, the lottery's profits to the state fell to seven percent below what the lottery brought in four years earlier.³⁸ States have also decreased player's chances of winning by increasing the amount of numbers they must choose. This results in higher jackpots, but fewer winners, which also causes jackpot fatigue.³⁹

To maintain or increase ticket sales, the lottery must also advertise—a practice that has often proven misleading and deceptive. Lotteries rarely mention the odds of winning the jackpot, which are staggeringly poor.⁴⁰ Typically, the odds of winning are 14-million-to-one in a single state lottery and 80-million-to-one in multi-state games.⁴¹ Lottery advertisements (not bound by the Federal Trade Commission's truth-in-advertising standards⁴²) have also been found to target the poor, convey unrealistic chances of winning and unfairly induced people to gamble.⁴³

State reliance on lottery funds creates a troublesome dependence on revenue that is affected by player participation and economic trends. And when the funding is not there, the state must find ways to increase revenue to deliver on what it has promised. It is important to note that only a small fraction of lottery players supply most of the dollars taken in by a lottery, as the top five percent of players account for 54 percent of total lottery ticket sales. If every lottery player spent the same amount as the median player spends, ticket sales would plummet by 76 percent.⁴⁴

If economic ups and downs aren't enough of a threat, the possibility that lawmakers will divert lottery revenues somewhere else is another. Despite earmarking lottery revenues to specific areas, many states have shifted monies away from education to fund other priorities. For example, Georgia has diverted money to pay for all sorts of projects not related to education including museums, security fences and the renovation of historic buildings.⁴⁵ Even Ohio, which has a constitutional amendment requiring that lottery funds go to education, took funds away

from education to help balance the budget.⁴⁶ After nine years, the Montana legislature completely removed lottery dollars from funding education and designated the money solely to the general fund.⁴⁷

The lottery is also an inefficient way to generate new money for the state. Typically, 16 cents of every dollar spent on the lottery go toward administrative and operational expenses, while 50 cents are returned in prizes and 34 cent goes to the state.⁴⁸ Because the lottery spends 16 cents to raise 34 cents, the effective administrative cost is 50 percent. This is significantly higher than what it costs the state to collect the sales tax. In fact, the \$160 million per year that it would cost to run a North Carolina lottery is almost twice the amount of the revenue other states are reported to keep from North Carolinians who play out-of-state lotteries.⁴⁹

Mixed Messages

Because the state profits from lottery sales, it places itself in the position of having to entice its citizens to continue

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gambling in order to maintain profits. It is difficult to reconcile the state's role as the promoter, regulator and beneficiary of the lottery with its primary responsibility to uphold the public good. The National Gambling Impact Study Commission raised this concern by asking, "How can a state government ensure that its pursuit of revenues does not conflict with its responsibility to protect the public?"⁵⁰

The lottery creates a mixed message that often takes the form of flashy advertising that emphasizes luck and instant gratification over hard work and wise investing. New York's "All you need is a dollar and a dream" ad campaign is one example.⁵¹ These messages are in stark contrast to the messages of responsibility, good judgment and self-discipline taught to students in public schools through character education. Lottery advocates should look at whether they can reconcile their support for education with their promotion of a system that profits from sending a counterproductive message to students.

Unconstitutional Referendum

Lottery proponents continue to appeal to the average citizen's perception that they have a "right to vote" on the lottery. However, almost all constitutional experts agree that a binding statewide referendum on the lottery is an unconstitutional delegation of legislative authority to the people of the state.⁵² According to the North Carolina Constitution, the power of the people to vote is limited to specific areas, such as the approval of certain state or local government debts;⁵³ revising or amending the state Constitution;⁵⁴ and calling a constitutional convention.⁵⁵ At its core, the concept of a referendum subverts a fundamental principle of our elected form of government: that state legislators are elected by the voters in their districts to study the issues and make informed decisions that are in the best interest of the constituents they represent and the state as a whole. It is not practical to expect every citizen of the state to be well informed on all of the issues that come before the General Assembly. This is why 170 members are elected to represent the people by serving in the state legislature. Lawmakers could vote to authorize a lottery at any time, but have resisted doing so because so many members know that a lottery is not good public policy. It is worth noting that a referendum vote is never linked to any other issue such as raising taxes, approving the budget or increasing government regulation.

Conclusion

A necessary role of state government is finding ways to fund worthwhile state programs like education. However, linking that task to an unworthy solution like gambling is bad public policy. As this paper has shown, there are a myriad of social and economic costs associated with a lottery. Real people's lives are negatively affected by the devastation caused by gambling addiction, and the revenues raised by a lottery do not justify putting the state in the gambling business. North Carolina lawmakers should reject the lottery, because it conflicts with so much of what is good about this state. The University of North Carolina's President Emeritus Bill Friday, put it this way: "I do not want to see my state that has done so much for so many—always manifesting strong positive leadership—now to say to its young people: 'Yes, we're going to provide the best educational opportunity possible, but we must resort to gambling to find the dollars to do it.'"⁵⁶

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