

## STILL A BAD IDEA

### *Lottery Would Bring Unstable, Costly Revenues*

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Summary: Gov. Mike Easley and other proponents are reportedly preparing to resurrect the idea of a state lottery for North Carolina. The case for this regressive and unpredictable source of revenue has, if anything, weakened in recent months, as other states with lotteries have experienced significant revenue shortfalls. The fact remains that Easley is overestimating the lottery's potential revenue, thus creating the risk of additional tax increases in the future to make up the difference.

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**A**fter lying dormant all summer, as members of the North Carolina General Assembly debated tax-increase plans that are proving to be unpopular with the North Carolina electorate, the idea of instituting a state lottery is now returning to the foreground. But a state-run lottery was a bad idea last spring — and recent evidence from other state lotteries suggests that the case for the idea is getting weaker, not stronger.

#### *A Review of the Facts*

In his State of the State Address last February, Gov. Mike Easley claimed that a state lottery would raise over \$500 million for North Carolina's state treasury, an estimate that he later modified to \$450 million. But subsequent analysis showed that the governor's projections were based on wild and unsustainable assumptions about the rate at which North Carolina's citizens would play the lottery. Experience shows that, after paying out prize money and the costs of administering the game, most state lotteries net about one third of the gross amount spent on lottery tickets. This means that in order for NC to net \$450 million from a lottery it would have to have over \$1.3 billion in gross sales. This would mean that if half of North Carolina families played the lottery every year, they would have to spend an average of \$870 per family on lottery tickets.

Putting aside the moral question of whether state government should be encouraging North Carolina's families to spend such large sums of money on gambling, this level of lottery activity is completely inconsistent with amounts raised by other southern states that have lotteries. According to analysis done by the Locke Foundation,

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extrapolating from the results that similarly populated southern and border states have had with their lotteries, a North Carolina lottery could reasonably expect to gross about \$933 million annually. After netting out prize money, operating costs, and lost tax revenue (lottery tickets are sold free of sales tax), a state lottery would likely net the state about \$285 million.<sup>1</sup> This means that the state government will be diverting \$933 million from the private market forces of entrepreneurship and consumer demand to raise about one third that amount for the state's treasury. This massive diversion of resources from productive private sector uses would not only be bad for the state's economy but makes very little sense in terms of basic principles of public finance.

### *Investing in a Declining Industry*

Given trends in lottery profits, even the Locke Foundation's estimates may be overly optimistic. According to a report recently published by *Governing* magazine, 20 of 38 states that have lotteries posted declining profits in 2000, with another 6 states posting less than a one percent gain.<sup>2</sup> It is argued that much of this can be attributed to the fact that states are losing the monopoly that they have had over gambling. Casino gambling at Indian reservations and on riverboats is becoming more and more popular and there is no sign that this competitive trend is likely to change. According to David Gale, executive director of the North American Association of State and Provincial Lotteries, "Just about everyone in the United States is within a three hour drive of a casino."<sup>3</sup> This is also true for many living in North Carolina.

The fact is that these results are perfectly consistent with what can be expected in any market that makes a transition from monopolistic to competitive. One of the key differences in monopoly markets as opposed to competitive markets is the level of profits. As new gambling opportunities arise and people have more options, profits throughout the gambling industry, which the state of North Carolina will be a part of if it implements a lottery, will decline. North Carolina will be entering the gambling business just as this trend is taking hold. This fact — coupled with the reality of a possible statewide recession — suggests that, not only are the governor's estimates wildly optimistic but even other estimates that may have seemed reasonable or conservative may now be too rosy.

### *The Private Sector is Not the Problem*

The underlying assumptions behind both the movement for higher taxes and a state lottery is that North Carolina's private sector — workers, consumers, and shareholders — are not handing over enough wealth to the state. In other words, if the argument is that the state does not have enough money for the programs that it wants to implement, then the corollary has to be that the private sector has too much. The governor and supporters of the lottery and higher taxes would like to increase spending this year by hundreds of millions of dollars. These resources have to come from the state's private sector. What they are trying to do is find a politically palatable way to make this happen.

But in fact, North Carolina's private sector is not the problem. We already have the highest-taxed private sector in the Southeast. State government spending in a variety of areas — including corporate welfare, pork barrel projects, and Medicaid — can and should be restrained without affecting essential services or human welfare.<sup>4</sup> Attempts to drain more from the productive citizens of the state, by any means including a lottery are not only unfair but will be harmful to the state's already faltering economy.

— Dr. Roy Cordato, Vice President for Research

### *Notes*

<sup>1</sup> Roy Cordato, "Easley's Lottery Myths," *Spotlight*, No. 187, February 21, 2001, The John Locke Foundation.

<sup>2</sup> Ellen Perlman, "Losing Numbers" *Governing: The Magazine of States and Localities*, September, 2001, p. 46-47.

<sup>3</sup> *Ibid.*

<sup>4</sup> See John Hood, Don Carrington, and Roy Cordato, "Changing Course IV: An Alternative North Carolina State Budget," Policy Report, The John Locke Foundation at [www.johnlocke.org](http://www.johnlocke.org).