Approved 1-17-86
Date

MINUTES OF THE HOUSE COMMITTEE ON FEDERAL & STATE AFFAIRS.

The meeting was called to order by Rep. Robert H. Miller, Chairperson, at 1:30 a.m./p.m. on January 16, 1986 in room 526S of the Capitol.

All members were present except:

Rep. Barr - E.
Rep. Roy - E.
Rep. Peterson

Committee staff present:

Lynda Hutfles, Secretary
Russ Mills, Research
Raney Gillilan - Research
Mary Torrence, Revisor of Statutes

Conferees appearing before the committee:

Russ Mills, Research
Harley Duncan, Department of Revenue

The meeting was called to order by Chairman Miller.

The Chairman called attention to next weeks agenda.

Representative Long made a motion, seconded by Representative Aylward, to approve the minutes of the January 16 meeting. The motion carried.

SCR1609 - Authorizing state-owned and operated lottery

Russ Mills, Legislative Research Department, explained the fiscal, social, and economical aspects of state lotteries; detailed the Wisconsin situation and explained the federal aspect of a lottery in Kansas. He also distributed the June 1985 State Policy Report which gives an overview of lottery. It details policy issues, growth, design and administration, enforcing laws against illegal lotteries. A comparison of state lottery revenues for FY 80-83 was also distributed to the committee. See attachment A.

Harley Duncan, Department of Revenue, told the committee that a Lottery Research Team had been established to research the mechanics of a state lottery organization. He briefly explained the areas of lottery game design, functions a state agency must perform, allocation of lottery revenue, the enabling legislation and start-up reference dates. He also distributed a glossary of lottery terms and a chart of a sample lottery agency. See attachment B.

There was discussion of the passing of enabling legislation, if lottery passes, with appropriations contingent on the outcome of the November election subject to Finance Council approvl.

The meeting was adjourned.

Unless specifically noted, the individual remarks recorded herein have not been transcribed verbatim. Individual remarks as reported herein have not been submitted to the individuals appearing before the committee for editing or corrections.

1

The State of Wisconsin

LEGISLATIVE REFERENCE BUREAU

201 North, State Capitol

Madison, Wisconsin 53702

Telephone Area Code 608

Reference: 266-0341

Bill Drafting: 266-3561

Dr. H. Rupert Theobald, Chief

BEYOND BINGO:
The State Lottery Experience

Informational Bulletin 85-IB-2

November 1985

H. F+SA
1/16/86

Attachment A

BEYOND BINGO:
The State Lottery Experience

Table of Contents

BEYOND BINGO:
The State Lottery Experience

I. INTRODUCTION

In the wake of the spread of state lotteries in recent years, amending the Wisconsin Constitution to permit a lottery in this state has again become a warmly debated topic. Since New Hampshire started the first contemporary state lottery in 1964, an additional 21 states and the District of Columbia have authorized lotteries.

Table 1: Spread of State Lotteries

State	Year Begun	State	Year Begun
New Hampshire	1964	Delaware	1975
New York	1967	Vermont	1978
New Jersey	1970	Arizona	1981
Connecticut	1972	District of Columbia	1982
Massachusetts	1972	Washington	1982
MICHIGAN	1972	Colorado	1983
Pennsylvania	1972	California	1985
Maryland	1973	IOWA	1985
ILLINOIS	1974	Oregon	1985
Maine	1974	Missouri	Projected early 1986
Ohio	1974	West Virginia	Projected early 1986
Rhode Island	1974		

Five of these states began operations in 1985 or anticipate an early 1986 start-up: California, Iowa, Missouri, Oregon and West Virginia. In 1985 the Montana Legislature enacted legislation to put the issue of establishing a state lottery on the November 1986 ballot. In no state has a lottery proposal that made it to the ballot been defeated by the electorate.

State lotteries, formerly concentrated in the Northeast, are now a coast-to-coast reality. The slow spread westward can be seen as an example of the domino theory in action. States without lotteries resent seeing money flow across their borders to neighboring states that have elected to tap this new source of revenue. In a long geographical leap, the Mississippi River was crossed in 1981 when Arizona began operating a lottery. Six more western states have subsequently been added. As a region, only the South is without a state lottery.

The number of states with lotteries authorized is approaching one-half the total number of states. Because they include some of the largest, these states already comprise more than 58% of the total population.

As more states authorize lotteries and as winners of gigantic jackpots receive wide media attention, public pressure in favor of a lottery in Wisconsin appears to be increasing. This public pressure, as well as the attraction of neighboring state lotteries and the revenues they are generating, has not gone unnoticed by Wisconsin policymakers.

The historical development, administrative features and policy issues of state lotteries were described in 2 previous Legislative Reference Bureau publications (RB-73-1, "State Lotteries", 1973; IB-77-2, "State Lottery Update", 1977). This report is an overview of what can be learned from the fiscal, economic and social experiences of other states, as well as a summation of Wisconsin's situation.

Prepared by Dick Pazen, Research Analyst.

II. FISCAL ASPECTS OF STATE LOTTERIES

Revenue

What is the economic justification for a state to conduct a lottery? It is presumably a painless way of obtaining revenue. A lottery provides the public with a popular form of recreation, and, in return, the state collects money that would otherwise come from taxation.

State lotteries are billion dollar operations. They take in more money than gambling casinos. Many of the larger states and states with more mature lotteries have passed the billion dollar mark in net profits since the inception of their games. In fiscal year 1984 gross state lottery revenue in the United States was $6.9 billion, with a total net profit to the operating states of $2.8 billion. The top 4 states in generating funds were Pennsylvania, Illinois, New York and New Jersey (in descending order). With the addition of states that are now initiating lotteries, and the adding of new games to existing lotteries, revenue figures should continue to climb. California, the nation's newest lottery state, has the potential of quickly becoming the biggest. Revenue estimates nationwide for fiscal year 1985 vary, but the gross is projected to be around $9.4 billion, with a net of $3.8 billion. Table 2 charts gross state lottery revenue for a 15-year period.

Table 2: Gross State Lottery Revenue

Fiscal Year	Amount in Billions	Fiscal Year	Amount in Billions
1970	$0.05	1978	1.9
1971	0.2	1979	2.1
1972	0.4	1980	2.4
1973	0.6	1981	2.9
1974	0.7	1982	3.9
1975	1.0	1983	5.4
1976	1.2	1984	6.9
1977	1.5	1985	9.4 (estimated)

Source: Public Gaming Research Institute, Inc. (reported in *Business Week, 9/9/85)*.

The size of lottery receipts in the aggregate, however, can be misleading. A 1985 examination by the Wisconsin Taxpayers Alliance (based on FY 1983 data) found that net lottery revenue averaged only 1.7% of total general revenue in lottery states (*The Wisconsin Taxpayer*, "Lotteries and Other Gambling", February 1985).

What follows is a more detailed description of the performance of a representative sampling of state lotteries based on their fiscal year 1984 annual reports. Illinois, Iowa and Michigan — neighboring states whose games are said to attract "Wisconsin" dollars in large numbers — are examined for obvious reasons. Several of the largest money-making states, and one of the smallest, are also looked at: New Jersey, New York, Pennsylvania and Vermont. Washington has been included because it ranks closest to Wisconsin in population.

Illinois (population 11,466,000) — Illinois' lottery marked the end of a decade of operation with a record-breaking year in fiscal 1984. It now operates 4 different types of games. Gross revenue was $912 million (up 77% from prior year). Net profit was $377 million (up 75%). $433 million was awarded in prizes to winners (up 87%). Operating expenses were $18.5 million (a bit more than 2% of sales).

In the 10 years since its inception in 1974, the lottery has returned a net profit of over $1.1 billion dollars to the state, and prize winners received $1.2 billion (109 millionaires). Although profits go into the general fund rather than being earmarked, the largest proportion was appropriated by the legislature for educational purposes, followed closely by health and social services programs. Other beneficiaries were programs relating to public protection and justice, natural resources and recreation, general government, transportation facilities, and senior citizens.

Michigan (population — 9,116,000) — Michigan's lottery, which began in 1972, also reported a record 1984. It operates a wide variety of games (including daily games, instant games and lotto). In fiscal year 1984 the lottery had gross ticket sales of $585 million (up 6% from prior year). Net revenue to the state was $236 million (up 6%). Prizes to winners totalled $289 million (including 5 millionaires). Operating costs were about 5% of the gross. The $1 billion total net revenue mark should be reached in 1985. Profits were initially deposited in the general fund. Since 1981, however, they have been dedicated to the state's school aid fund, which supports elementary and secondary education. In fiscal 1984, lottery profits constituted 16% of the total aid fund, providing $138 per pupil. In 1984 the legislature passed a law extending the lottery for another 4 years.

Iowa (population — 2,906,000) — Since Iowa's lottery began operation in late August 1985, no meaningful revenue figures are available. It opened with instant games, including a spin-off of weekly jackpot drawings. The lottery is expected to gross about $100 million annually with net profits earmarked for economic development initiatives. The initial reception has been good, with $11.5 million in ticket sales in a bit more than 3 weeks. A 5-year sunset provision was included in the creating law.

New Jersey (population — 7,427,000) — Since its 1970 start-up, the New Jersey lottery has grossed $4.2 billion, awarded over $2 billion in prizes, and returned a net profit of $1.8 billion to the state. In fiscal year 1984 the gross was $848 million (up 22%), prizes totaled $425 million (up 23%), and the state netted $359 million (up 22%). Lottery money is the fourth largest source of revenue for state government. It is earmarked for education and state institutions. In 14 years of lottery operations, state institutions have received $741.8 million, elementary and secondary education $530 million and higher education $528.5 million. 1984 operational and promotional costs were 1.6% of gross revenues. These costs do not include commissions paid to agents or fees to private contractors.

New York (population — 17,567,000) — New York's "new" lottery began operating in September 1976 (the "old" lottery functioned from 6/67 to 10/75 before being suspended). From that date through fiscal 1984 the lottery has grossed $2.96 billion, awarded $1.5 billion in prizes (203 millionaires) and returned $1.3 billion in net profits to the state. In fiscal 1984 the gross was $890.3 million (up 38%), prizes totaled $392 million (up 38%), and the state netted $390.5 million (up 42%). Two net profit landmarks were reached in 1984: 1) the $1 billion aggregate total was achieved, and 2) revenues topped $1 million per day. State revenue is earmarked for education (representing 8% of state aid to local education in 1984); however, 2 exceptions have been made over the years. In 1977 special legislation was enacted whereby $90.7 million in lottery proceeds was used to help balance the state budget. In 1980, legislation authorized $4 million to be diverted to the Winter Olympics Trust Fund.

Pennsylvania (population — 11,879,000) — Pennsylvania, with the nation's biggest lottery, had a most successful year in 1984, surpassing the figure of $1 billion in *annual* sales. Gross revenue amounted to $1.236 billion (up 39%), net revenue was $516.3 million (up 45%) and prize winnings came to $607.1 million (up 38%). Operational costs where given as 2.4% of gross earnings. No cumulative data was provided (the lottery began in 1972). Net revenue is primarily targeted to a variety of programs benefiting senior citizens.

Vermont (population — 520,000) — Vermont is representative of the smaller lottery operations. From its 1978 beginnings through fiscal year 1984, the lottery has grossed $25.7 million and netted $7.2 million. No cumulative prize data was provided. In 1984 the gross was $5.2 million (up 13%), the net was $1.3 million (up 15%) and prizes totaled one-half the gross at $2.6 million. Vermont includes commissions and other fees in its operating expense figures, which came to 25% of the gross in 1984. State net revenue is deposited in the general fund. The original lottery was created with a June 1980 sunset provision. It was extended 3 years in the 1979 legislative session, and extended indefinitely by the 1981 session.

Washington (population — 4,276,000) — The State of Washington has a relatively new lottery (it began in November 1982), but has been included because it is similar to Wisconsin in population (Washington ranks 20th versus 16th for Wisconsin). In fiscal year 1984 it grossed $164.7 million, netted $68.5 million in profits for the state, and distributed prizes worth $75.9 million. Administrative expenses were given as 9.5% of gross, including operating costs (4%), ticket costs (3%) and advertising (2.5%). In its short history, the aggregate totals are: gross $364.8 million, net $148.5 million and prizes $168.8 million (creating 10 millionaires in the process). State profits accrue to the general fund.

Table 3: Selected State Lottery Revenue Data, Fiscal Year 1984*

State	Population (1982 estimate)	Revenue (in millions) Gross	Net	Prizes Awarded (in millions)
Pennsylvania	11,879,000	$1,236	$516	$607
ILLINOIS	11,466,000	912	377	433
New York	17,567,000	890	390	392
New Jersey	7,427,000	848	359	425
MICHIGAN	9,116,000	585	236	289
Washington	4,276,000	164	68	75
Vermont	520,000	5.2	1.3	2.6
IOWA**	2,906,000	N/A ($100 annual projection)	N/A	N/A

*Selected states (see text). Not all states with lotteries included.

**Began lottery August 1985. FY 1984 data not available.

Earmarking Revenues

"Earmarking" state lottery revenue means to dedicate the money for some specific purpose or purposes, rather than intermingling it in the general fund to be appropriated as the legislature sees fit. States which have created lotteries are about evenly split on which approach they have adopted. Eleven states and the District of Columbia simply treat the proceeds as general revenue, although Vermont stipulates that it be used only for debt retirement and capital construction (rather than losing its identity). Arizona has it both ways, with an annual minimum amount set by the legislature devoted to local transportation assistance, and the balance lapsing into the general fund. The remaining states earmark all lottery revenue for one or more specific purposes, including: education, local government aids, programs for the elderly, economic development, conservation and recreation, agriculture, the arts, and even the treatment of compulsive gamblers.

Table 4: Allocation of State Lottery Revenue

State	Disposition
Arizona	Local transportation assistance/general fund
California	Education
Colorado	Capital construction/conservation/parks and recreation
Connecticut	General fund
Delaware	General fund
D.C.	General fund
ILLINOIS	General fund
IOWA	Economic development
Maine	General fund
Maryland	General fund
Massachusetts	Local government aids/arts
MICHIGAN	Education
Missouri	General fund
New Hampshire	Education
New Jersey	Education/state institutions
New York	Education
Ohio	General fund
Oregon	Economic development
Pennsylvania	Senior citizens
Rhode Island	General fund
Vermont	General fund (debt retirement and capital construction)
Washington	General fund
West Virginia	As appropriated by legislature

It is generally believed that designating the revenue to be used for some desirable public purpose aids in initially selling the idea of a lottery to the public (and legislators). Later, it continues to reassure players that their losses at least go for some beneficial program they can identify with, and are not "wasted" by the state.

Putting the revenues directly into the general fund, however, has its advantages. The legislature retains flexibility in appropriating the money where the need is most pressing. Earmarking funds builds a constituency that resists changes. Special interests that are benefited may also try to influence how the lottery is administered.

Earmarked revenue has the most impact in a program that previously received little or no public funds. Adding lottery revenue to an already relatively well-funded program: 1) may only displace appropriated funds which may then be used elsewhere, or 2) may prove to be too small a proportion of the total to have any real effect. The program benefited also trades a fixed appropriation for a source of revenue that will fluctuate and may prove unreliable.

State Taxation of Winnings and Tickets

Is it double taxation for a state to tax winnings in a state-operated lottery? Advocates of the game sell it as voluntary taxation, which makes all players voluntary taxpayers, whether they win or not. A third or more of gross lottery revenue is skimmed off the top into state coffers.

A majority of states currently operating lotteries follow the federal example and make all winnings subject to tax as ordinary income. Jurisdictions that have exempted winnings from taxation include Maine, Michigan, New Jersey, Oregon, Pennsylvania and the District of Columbia. There may be others. Pennsylvania, which originally taxed winnings, acted in 1985 to exempt future winners. Arizona followed the opposite path; originally exempt, a tax was subsequently imposed.

Taxing winnings, either at the personal income rate or with some special lottery tax, is an opportunity for a state to realize maximum revenue from its lottery. Judging from the experience of the states, the jury is still out on how appropriate or advisable it is to tax winners.

Iowa (in 1985) became the first state lottery to require payment of a state sales tax on ticket sales. The 4% tax is not paid separately by each individual ticket purchaser. It is paid by the lottery agency itself into the state's general fund.

Multistate Lotteries

A new development in the state lottery situation made its appearance in September 1985 — the nation's first multistate lottery. Maine, New Hampshire and Vermont entered into an interstate compact to cooperate on a "Tri-State Megabucks" game, agreeing to split the administrative arrangements among the 3 participating states and to divide profits in proportion to the number of tickets sold in each state. The idea of this joint lottery venture is to be better able to compete with larger neighboring lottery states, such as Massachusetts and New York, in offering big jackpots. Lack of the big prize is seen as the reason for the relatively disappointing performances of the lottery games in the operations of the 3 states.

Iowa's new lottery law, also reflecting a concern over the greater drawing power of neighboring Illinois' state lottery, contains a provision to permit the future establishment of joint lottery games with other states.

It is predicted that additional regional games will follow the northern New England precedent. In fact, a "nationwide" lottery — involving only those states that have already created their own lotteries — is being suggested as an antidote to the proposed national lottery to be operated by the federal government in all 50 states.

Public Participation

A lottery is a unique activity for a state because it must be run like a private enterprise; that is, with the goal of producing the maximum profit. To achieve this end, public interest must not be allowed to sag. This is a difficult task because lotteries are not only probably the most uninteresting form of gambling, but also offer the worst odds of any form of gambling — legal or illegal. Sustaining interest when players almost always lose is tough. The lottery's continuing popularity is based on the attraction of risking a small sum of money on the slight probability of gaining a very large amount which a person otherwise could have no chance of obtaining.

Three ingredients have been shown to be necessary to build and maintain an acceptable level of public participation: 1) promotion of the games, 2) surveying to get player feedback, and 3) modifying existing games or introducing new ones. To that list should be added the attraction of an occasional huge jackpot.

Advertising and other promotional expenditures by state lotteries are said to average about 2% of gross revenues. In comparison to the private sector, that is a relatively small amount to budget for this purpose. One suggested reason is that, being a state monopoly, there is no competition to overcome. The largest proportion of advertising money is usually spent for television time, with radio, the print media and billboards also playing an important role. It is worth noting that a $22.2 million advertising contract has been negotiated for the first year of California's new lottery.

Successful lotteries seem to place a big emphasis on trying to be responsive to the ticket-purchasing public regarding the type of games, the prize structure, distribution setup and so on. Their public relations people make extensive use of polls and marketing studies to obtain feedback from players. This effort is viewed as vital to continued public acceptance and goodwill.

Lottery games have life-cycles. Therefore, another important marketing tool is to tinker with existing games and to introduce new games whenever ticket sales show a decline. Various game formats are now available and changing technology holds out many possibilities for enhancing games or developing new ones. Most lottery states offer several different games because it has been demonstrated that players will be attracted to one type, but not others (depending on their age, income and education). Listed below are descriptions of the basic lottery games — and some related terms — useful in understanding the subject. Note that many variations on these basic forms exist.

Instant — Instant games utilize preprinted tickets (usually $1) with symbols or numbers concealed underneath some rub-off material on the ticket surface which, when removed, immediately discloses whether or not the purchaser has won. Sometimes winners of instant games automatically qualify for a grand prize drawing or sweepstakes game held after all instant tickets in a particular game cycle are sold.

Lotto — A centuries-old game in which players select a combination of numbers from a larger group — 6 out of a field of 40, for example — the winning numbers being determined by a randomly selected drawing (usually held weekly). It is a progressive game. If no one has selected the winning combination, the jackpot builds by adding part of total sales to the next game. Winnings are paid on a pari-mutuel system, usually in the form of an annuity over many years.

Numbers — These games are patterned after the illegal, private numbers games. A player chooses his or her own group of numbers (usually 3 or 4 digits, for 50 cents or $1) with winners determined by numbers drawn daily, weekly or biweekly. Payouts are at fixed odds, and vary depending on whether the player has the numbers in exact order or in a variety of combinations.

On-Line — Any of a variety of games using a retail distribution system with ticket-generating terminals directly linked to a central computer. Ticket purchasers select their own numbers, agents send these to the main computer, which registers the pick and prints out a receipt ticket (used in lotto and numbers games, for example).

Pari-Mutuel — A system of wagering in which the odds and winnings are calculated solely upon the amount of money bet. Winners divide all the money wagered by the losers in the betting pool, less deductions for expenses and profit. This system is used in lotto games.

Sweepstakes — A game with many variations, but which is traditionally tied to a horse or dog race. A drawing is held to select ticket holders to be matched with horses or dogs entered in a particular race. The amount finalists win depends on finishing positions in the race. Now almost a generic word, it is used more generally to refer to any of various lotteries. Note that participants may be randomly selected from winners in other lottery games held previously (see instant games above).

Video — Illegal in most states, these devices utilize video terminals that resemble a cross between casino slot machines and amusement arcade video games. Prizes are offered for winning (at random) by the state lottery. They are seen as games of the future, combining more skilled player participation with excitement. It may evolve into video gambling from home or office computers.

Weekly (or Draw) Lottery — The traditional lottery game which closely resembles a raffle. Players simply purchase (for 50 cents or $1) a pre-numbered ticket with a designated drawing date (held weekly or less frequently) where winners are determined by random selection. In addition to weekly prizes of varying amounts, it may include the possibility of being eligible for periodic grand prize drawings (of "instant millionaire" finalist type). This is the most passive lottery game because the player has no active involvement in determining the outcome (like scratching off a coated ticket) and no choice of numbers is made.

It is indisputable that the prospect of winning a very large jackpot will sell a great many lottery tickets. The Illinois and New York experiences demonstrate that point (the 2 largest jackpots to date: $40 million to a single winner in Illinois in 1984 and $41 million split among multiple winners in New York in 1985). People stood in long lines to purchase tickets. Of course, as more tickets are sold the odds against winning increase, but odds seem to be a very secondary consideration with players when a gigantic payoff is in the offing. Logic would suggest that having 50 chances at winning a $1 million prize would have more mass appeal than one chance of winning $50 million against impossible odds. It does not seem to work that way in actual practice. The need to offer bigger prizes produced the nation's first multistate lottery in 1985 (Maine, New Hampshire and Vermont).

Incidentally, these large prizes are frequently in the form of an annuity, a type of insurance policy purchased by the lottery that pays the winner in equal installments over a long period of time (say 20 years). Allowing the balance to accumulate interest over time permits the lottery to offer a prize larger than the cost of the policy. The advantages of this approach are that it produces larger prizes, saves taxes for the winners and makes it easier for winners to manage their new situation. One problem is that it is not always made clear to players that prizes may not be paid in a lump-sum amount.

Figures on lottery participation per person in dollar amounts are not too instructive for several reasons: 1) they are based on total state population (not just players), 2) some people play far more often than others, and 3) the numbers are skewed by nonresident players. In 1984 the average annual per capita gross revenue among lottery states was reported to be $72.02; net revenue was $29.40. Maryland is said to be the highest per capita state, averaging about $3 to $3.75 per week. By contrast, the low-end figure is around 19 cents per person per week in Vermont.

III. SOCIAL AND ECONOMIC ASPECTS OF STATE LOTTERIES

Enough states have had lotteries for enough years for their experiences to provide a record to examine. The environment in which these lotteries have had to operate has been described as a well-regulated fish bowl. Thus far, it can be generalized that lotteries have produced at least a modest amount of revenue, seem popular with the people and appear to be relatively clean and well run. No state has repealed or permanently ended its lottery operations once it has started, even though some laws creating lotteries included provisions for "sunset" dates.

Major Problem States

Lotteries have a fundamental need to maintain an untarnished image because any loss of public trust in their integrity is fatal. For the most part, only isolated cases of alleged fraud, cheating, forgeries or tampering have been reported. These have been characterized as small-time and usually unsuccessful.

Several states, however, have had major problems. The one most frequently cited occurred in Pennsylvania. In 1980 Pennsylvania's state lottery suffered the most serious scandal yet discovered when a drawing was tampered with in an attempt to fix the game. Some criminal convictions followed the discovery that the air blown, numbered, ping-pong balls in a machine used for selecting winning numbers during a televised drawing had been altered to insure that certain numbers would prevail.

The New York lottery was suspended by the Governor from October 1975 to September 1976 for technical irregularities in its operation, including the sale of duplicate tickets and failure to award prizes because winning numbers were on unsold tickets. Poor management and lack of security were blamed for allowing opportunities for fraud. New legislation was needed to reconstitute the lottery before it was revived.

Delaware's lottery got off to a false start in 1975. The original lottery operated only 5 weeks, had low ticket sales, awarded no top prizes, and needed additional state start-up funds. It was temporarily halted as a failure, reorganized and restarted.

More recently, Washington State is reported to be revamping its lottery (it began operations in 1982) because, while a financial success, it caused some disillusionment when projected sales fell below over-optimistic projections.

During its initial year, the Ohio lottery garnered a great deal of bad publicity relating to such matters as hiring practices, use of cars, awarding of contracts, slush funds and partying. Amid charges of partisanship and malfeasance in its administration, the Governor labeled the lottery a scandalous operation. Changes in top Lottery Commission personnel and practices resulted.

Rhode Island had some difficulties with the lottery concerning a building lease that resulted in the Governor providing for more competitive bidding on lottery contracts and opening commission meetings to the press.

The lesson in these case histories is the need for proper advanced planning, realistic expectations, good administration and a "clean" governmental environment.

Who Plays (and Pays)

There is not a lot of uniformity in the plethora of surveys of who plays — and pays — in state lotteries. A report could probably be found to support almost any preconceived notion; however, an attempt to generalize will be made.

A recent Congressional Research Service (CRS) report summarized its examination of demographic studies on the types of people who play state-run lottery games, looking at characteristics such as income, age, sex, occupation, race, education and neighborhood residency ("Overview of State Lottery Operations", January 1985). According to the CRS report, most available data indicated lottery playing is a pastime of middle and upper-income groups. They predominate among players and winners. The average player has at least a high school education, is more likely to be male (although there are indications that females are closing the gap), is usually white, and tends toward middle-age.

Of course, there is no such thing as a "typical" lottery player. Wide variations are reported for such factors as age, race and income. One major variable is the type of lottery game played. Different demographic groups have demonstrated definite preferences. Younger, better educated, more affluent people appear to be attracted to different games than persons in less fortunate circumstances.

The biggest arguments surround findings concerning participation of low-income groups. Lotteries may be a middle-class activity on the average, but obviously the poor also play. Lottery outlets in neighborhoods characterized by low income, minorities and the less well educated receive heavy play. From the perspective of the impact of playing at different income levels, the poor certainly spend a greater proportion of their personal income on lotteries than more affluent players. This is true, however, of all their purchases, whether it be for necessities (food, shelter, clothing, transportation) or for optional items, such as entertainment. That raises the issue of who should sit in judgment on how the poor spend their money. The real question seems to be: Are the poor playing the lotteries out of proportion to their numerical presence in the population? Lottery advocates point to a large body of data saying this is not the case. For many others, the question has not yet been satisfactorily answered.

Crime

The gambling binge that states seem to be embarked upon reflects gambling's new respectability. Unfortunately, researchers have found the rationale that legal gambling will drive out illegal gaming appears to fall into the category of mostly wishful thinking, at least where lotteries are concerned. Illegal gambling continues to be very big business (nobody knows how big), and its links to organized crime are well documented. As yet, after 20 years of experience, state lotteries seem to be untainted.

Investigations such as the 1985 report of the New Mexico Governor's Organized Crime Prevention Commission concluded that state lotteries have not been infiltrated or compromised by organized crime, and, furthermore, that no significant law enforcement problems have been attributed to the creation of state lotteries. Other investigations, lottery officials and law enforcement agencies report similar conclusions. There seems to be something approaching a consensus on that point. Wisconsin's own Attorney General has endorsed a state lottery with assurances that the benefits outweigh any risks.

Illegal numbers games, however, may actually benefit from the existence of a legal lottery. The most obvious way is by utilizing the same numbers selected for payoffs. By "piggybacking" on the state-operated game, illegal games can make free use of the administration, security and publicity provided by the state in selecting winners. In the competition for players the illegal numbers games will probably continue to co-exist alongside the state lotteries as long as they can offer the advantages of better odds, credit, convenience and tax avoidance.

Another possible by-product over which the state has no control is the suspicion that the existence and promotion of the legal lottery produces new players for illegal games. There is a catchy phrase: "Access brings excess". It expresses the fear that persons who had not previously gambled will be enticed into playing the state lottery (through opportunity and advertising), become hooked on gambling and move on into illegal gaming activities. The final report of the Commission on the Review of the National Policy Toward Gambling ("Gambling In America", 1976) emphasized the importance of opportunity as a factor in the gambling problem.

This same opportunity factor associated with state lotteries is also applicable to the issue of compulsive gambling behavior.

Compulsive Gambling

Compulsive — or pathological — gambling has been formally classified by the American Psychiatric Association as a mental illness (listed as an impulse control disorder). It is a psychological addiction that manifests itself as an uncontrollable, exaggerated preoccupation with gambling and the urge to gamble; a chronic behavior disorder of progressively increasing intensity. The condition can be very detrimental to the individual's personal and family situation.

It is advocated that states which legalize some type of gambling as a source of revenue have an obligation to apply a portion of that revenue to mitigating the negative consequences for individuals and society stemming from compulsive gambling. Funds would go for programs of prevention and public education, training and research, and treatment facilities. Some states have committed resources to establishing such programs, at least on a pilot basis, including Connecticut, Iowa, Maryland (the first, in 1978), New Jersey and New York. Iowa's new law, for instance, earmarks 0.5% of gross lottery revenue to assist individuals and families in difficulties because of gambling.

In addition to treatment facilities in Baltimore, Maryland and several other parts of the country, a self-help organization called Gamblers Anonymous (GA) operates a program that has met with some success. GA was founded in 1957 and has shown consistant and rapid growth (there are now over 700 chapters).

Persons who feel that even a token effort by lottery states regarding compulsive gambling is not necessary point out that lotteries are the most passive, unchallenging form of gambling, for the most part based on pure luck. Problem gamblers find it too dull and seek faster games with more action and strategy. A lottery, however, might provide an entry level for those who have never gambled before. No link between state lotteries and increases in compulsive gambling behavior has yet been proven.

Litigation

The *National Law Journal* ("Lottery Suits Face Big Odds", 5/27/85) points out another experience state lotteries are encountering — increased litigation. Law suits, or the threat of legal action, seem to follow whenever large amounts of money changes hands. Sore losers and even disgruntled winners take their complaints against lotteries to court. Similarly, problems between the lottery itself and its consultants, vendors and agents have gone the same route. Most of these cases are small and fairly routine, but some contract matters have been for high stakes.

While suits against state lotteries apparently have not fared well in court, the lottery must devote resources to defending itself. It is said that with the added litigation and winners who seek professional tax and estate counseling, lotteries are good news for lawyers.

IV. WISCONSIN SITUATION

Background

Legal gambling — and in particular a state lottery — is one of those perennial issues in Wisconsin whose time may have arrived. One significant factor pushing the state in that direction is that all 4 of Wisconsin's neighbors permit some type of legalized gambling beyond bingo. State lotteries are now operating in Illinois (1974), Iowa (1985) and Michigan (1972). Minnesota does not have a lottery; however, pari-mutuel horse race betting has been authorized.

The lure is primarily financial. Only rough estimates exist as to how much money Wisconsin residents spend on adjacent lotteries. Indications are that it is a respectable amount. There is considerable sentiment for Wisconsin to capture these dollars that are now flowing into the treasuries of border states by creating its own lottery and, if possible, reversing some of that flow.

Beyond purely financial considerations, polls conducted by newspapers and individual legislators reflect widespread popular support for a Wisconsin lottery for its recreational or entertainment value.

Lottery opponents say it is not a fair or effective revenue source, cite moral objections, are concerned about associated social and economic consequences, and simply feel it is not a proper activity for state government.

Advocates of a Wisconsin lottery confidently predict that this time around economics and public pressure will triumph over these concerns. Time will tell. The Governor has already announced that following the necessary successful constitutional amendment he will sign a state lottery bill if one should eventually reach his desk.

Constitutional Amendment

A lottery prohibition was part of Wisconsin's original constitution. Article IV, Section 24 of the Wisconsin Constitution, adopted in 1848, stipulated that "the legislature shall never authorize any lottery...." In fact, this constitutional provision has been broadly interpreted to exclude all forms of gambling.

Since the constitution must be amended in order to permit the legislature to create a state lottery, a time-frame of several years would be required before a lottery could become a reality in Wisconsin. Joint resolutions proposing the necessary constitutional amendment must be adopted by 2 successive Legislatures and be ratified by the voters in a statewide referendum before it becomes effective. More time would be required for the Legislature to consider and enact implementing legislation following ratification. This action would be followed by a time lag that would be needed to set up and actually start a lottery.

The earliest possible scenario on timing would have a proposed amendment be adopted on first consideration in the 1985-86 session, adopted again on second consideration by the 1987 Legislature early enough to have the question placed on the April 1987 election ballot for ratification by the electorate, and implementing legislation enacted in the time remaining to the 1987-88 session. The rest would depend on the effective date of the lottery law and the lead time necessary to make it operational. An optimistic view still places a lottery at least 3 or 4 years away.

Starting in 1965, the strict gambling prohibition in the state constitution (Art. IV, Sec. 24) has been relaxed by 3 separate amendments. The first, ratified in 1965, authorized the Legislature to create an exception to permit Wisconsin residents to participate in various promotional contests.

In 1973 the voters amended the constitution to authorize the Legislature to permit charitable bingo games. In 1977 a similar amendment relating to raffle games was approved. Legislation to implement each of these 3 amendments was subsequently quickly enacted.

The voters approved the 3 amendments with "yes" votes that ranged from 62% to 70% of the votes cast. No proposed amendment to modify the gambling provision has ever been refused ratification.

Table 5: Amendments to Wisconsin Constitution: "Lotteries and Divorces", Article IV, Section 24

Subject	First Approval	Second Approval	Date of Election	Vote For (%)	Vote Against (%)
Lotteries, definition revised	1963 SJR 42 (JR 35)	1965 SJR 13 (JR 2)	Apr. 1965	454,390 (70%)	194,327 (30%)
Charitable bingo authorized	1971 SJR 13 (JR 31)	1973 AJR 6 (JR 3)	Apr. 1973	645,544 (62%)	391,499 (38%)
Charitable raffle games authorized	1975 AJR 43 (JR 19)	1977 AJR 10 (JR 6)	Apr. 1977	483,518 (62%)	300,473 (38%)

Unlike a state lottery, bingo and raffle games are *privately* conducted by charitable and fraternal organizations under state license. Any profits inure to the benefit of the sponsoring organization. It was never intended that the games produce significant revenue for the state.

1985 Legislation

At the end of Floorperiod IV (October 18, 1985), 13 joint resolutions proposing amendments to the constitution's gambling provision have been offered in the 1985 legislative session. All are first consideration amendments. Five of these measures directly authorize the creation of a state lottery: 1985 Senate Joint Resolutions 1, 6 and 10; and 1985 Assembly Joint Resolutions 12 and 26. One other proposal, 1985 Senate Joint Resolution 7, would substitute a ban only on casino gambling for the much broader existing prohibition, leaving the Legislature free to prohibit or permit other forms of gambling, including a state lottery, under its statute lawmaking power.

1985 Senate Joint Resolution 42 would authorize the county board of any county to propose — and the voters of the county to enact by approval in a referendum — the creation of a county lottery to be operated as regulated by state law.

Following a series of public hearings held throughout the state, 1985 SJR-1 emerged as the proposal that has advanced the farthest. It was recommended for adoption by a Senate committee, on a 5 to 1 vote, and, following several hours of lively debate, was adopted by the Senate as a whole (on October 8, 1985) by a vote of 19 to 14. There will be no further action on 1985 SJR-1 until the Assembly considers it in Floorperiod V of the 1985-86 session, which begins January 28, 1986.

1985 SJR-1 simply authorizes the creation of a Wisconsin state lottery, the net proceeds of which would accrue to the state treasury as provided by law. It was adopted without amendment. Two of the unsuccessful amendments offered to the joint resolution would have put in the constitution language that the net proceeds of the lottery were earmarked for certain purposes: property tax relief and improvement of Wisconsin's business climate, respectively.

Pre-1985 Legislation

Proposed constitutional amendments seeking to legalize lotteries in Wisconsin can be found at least as far back as 1939. It is not clear exactly what some of these earlier ambiguously worded joint resolutions would have done. The first legislation explicitly proposing a Wisconsin state lottery in the contemporary sense was introduced in the 1965 session. (Note that New Hampshire inaugurated the nation's first modern state lottery in 1964).

Actually, 1965 Assembly Joint Resolution 41 authorized a Wisconsin "sweepstakes", the proceeds to be used for the benefit of public education. The optimistic sponsors of AJR-41 — anticipating a successful constitutional amendment effort — introduced a bill on the same day as the joint resolution that would create a state sweepstakes commission to operate the lottery (1965 AB-276). One interesting item in the implementing bill was that it gave municipalities a local option to prohibit the sale of state lottery tickets.

The arguments advanced 20 years ago for and against the proposal are the same as those heard today. Incidentally, the primary author of the proposed amendment and the implementing bill in that 1965 session also introduced another unsuccessful joint resolution (1965 AJR-58) calling for a statewide advisory referendum on whether the legislature should adopt the proposed amendment. This appears to be the only time legislation was introduced in Wisconsin to have an advisory referendum on the lottery issue. (The city of Milwaukee, however, held a referendum in April 1974. The question was: "Do you favor a state lottery as an alternative to the local property tax method of financing education?". While it carried by a large majority, the wording of the question has been criticized as deceptive, since no state lottery has produced enough revenue to become an alternative to the property tax.)

Wisconsin's real gambling push in the Legislature began in the 1970s and continues to this day. Starting in the 1971 session, many joint resolutions to amend the constitution to permit different types of gambling have been introduced. In every session except 1979, some of these proposals would have amended the gambling provision so as to remove the prohibition that prevented the Legislature from authorizing a lottery, either indirectly (by inference) or by direct reference.

Of the legislation over the years that might have permitted the establishment of a state lottery, all have been unsuccessful except 1975 Senate Joint Resolution 15 (Enrolled Jt. Res. 20). 1975 SJR-15 was a first consideration proposed constitutional amendment to permit the Legislature to authorize state-operated lotteries as prescribed by law. It passed the Senate by a vote of 20 to 11 and the Assembly by 67 to 28 (2 paired).

Three second consideration joint resolutions were introduced in the 1977 Legislature to follow up on the successful passage of 1975 SJR-15: 1977 SJR-4, 1977 AJR-15 and AJR-42. The 2 Assembly joint resolutions failed in committee in their house of origin under the terms of the session schedule. 1977 Senate Joint Resolution 4 was recommended for adoption by a Senate committee (4 to 3 vote), but was rejected by the Senate as a whole by a vote of 25 to 8. This was the high water mark of state lottery proposals in Wisconsin.

Revenue Estimates

Revenue estimates of what Wisconsin could realize from operating a state lottery vary widely. *The Lottery Journal* (October 1984), a publication of the Public Gaming Research Institute, projected $138 million in annual net revenue for Wisconsin, extrapolated from their average figure of $29.40 per person of net revenue in lottery states in 1984 times Wisconsin's 1980 population.

According to a National Conference of State Legislatures state lottery finance specialist (*State Legislatures*, "State Lotteries: Roses and Thorns", March 1984), while the annual per capita net proceeds of individual state lotteries vary greatly, the average is about $20, and a state should expect to net at least $10. The $10 *minimum* figure applied to Wisconsin's estimated 1984 population would produce an annual net of about $48 million.

The primary author of 1985 SJR-1 (the state lottery proposal) and chairperson of the committee that held hearings on the measure throughout the state reported estimates ranging from $50 million to $138 million per year in net revenue.

In 1984 the Legislative Fiscal Bureau (LFB) estimated the likely revenue potential of a Wisconsin lottery. It was preceded by a caveat explaining the difficulties in making interstate comparisons because of the variety of state lottery legal provisions, design features, operational systems and uneven life-cycles. That said, the LFB concluded:

> "Based on the average lottery performance in other states, the first one to three years of a fairly simple Wisconsin lottery (one or two games) could generate approximately $15 million in net revenue to the state. As the game matured, revenues up to $25 million might be expected; depending on the games offered and market development efforts, revenues of $50 million or more might be attained".

One unsuccessful amendment (SA-4) offered to 1985 SJR-1 provided that if the state lottery failed to produce at least $40 million in net proceeds to the state for 3 consecutive years, the constitutional amendment would be deemed repealed. (Parenthetically, it might be noted that Wisconsin revenue for fiscal 1984 from the income tax was $2.5 billion and from the sales tax, $1.3 billion.)

The actual performance of Washington — a lottery state with a relatively new game and similar to Wisconsin in size (estimated 1982 population 4,276,000) — might be instructive as to what earnings could be anticipated. In fiscal year 1984 the state generated net revenue of $68.5 million on a gross of $164.7 million.

V. THE FEDERAL ASPECT

Federal Lottery Law

In reaction to 19th century lottery scandals, a series of restrictive federal laws were enacted, including denying lotteries the use of the instruments of interstate commerce. In 1975 Congress modified these laws to provide exemptions for lawful, state-operated lotteries regarding advertising, use of the mails, newspapers and broadcasting facilities within states holding games and between adjacent states that also have lotteries. These changes eased some of the problems state lotteries were having in administering and promoting their games, but Congress is being asked to further relax restrictive laws (see U.S. Code provisions: 18 U.S.C. 1301 to 1307, 1953 (b); 39 U.S.C. 259, 3005).

Federal Taxation

All lottery winnings are taxable as income by the federal government. Gambling *losses* may be deducted (to the extent allowable by law). To help insure that tax liability is satisfied, a deduction of 20% of prizes $5,000 and over is automatically withheld from the winner. On winnings from $600 to $5,000, lottery officials are required to report the information to the Internal Revenue Service, but there is no withholding. Prizes of $600 and under — and that includes most winnings — are neither reported nor withheld. Rumor has it that many winners of these smaller prizes treat them as "free money" and do not declare it on their taxes. A popular method of legally avoiding a tax liability that players have adopted is to purchase several cheaper tickets rather than one expensive one (5 $1 tickets paying $500 each as opposed to one $5 ticket that pays $2500). The theory is that one has more chances of winning something and that several smaller payoffs could net a person more than a single larger prize which is reported to the Internal Revenue Service.

National Lottery Proposed

Congress is considering proposals to study or create a federally operated national lottery, with revenues to be used for deficit reduction, to help support social security or some other popular program. There is precedent because the federal government has sanctioned lotteries in the past, and national lottery games currently exist in many other countries. Individual states have again acted as laboratories for the federal government, in this case demonstrating the revenue potential and a high level of public acceptance for lotteries.

These proposals are still in congressional committee. It is likely that any effort to create a national lottery would face solid opposition from the states, even though the idea would probably be popular with the general public. Those states that operate lotteries know that competition from the federal government would diminish their revenue or even kill their games, while the remaining states which, for whatever reasons, have not created a lottery of their own would no doubt resist having one imposed upon them at the national level.

VI. SOURCES

American Academy of Political and Social Science, *The Annals,* "Gambling: Views from the Social Sciences", July 1984 (174.6/Am3).

Connecticut Office of Legislative Research, "Compulsive Gamblers", 1979 (174.6/C76d).

Council of State Governments, "Gambling on Revenues — State Lotteries", April 1983 (174.6/C83b).

---, *State Government News*, "More States Look to Lottery Profits", August 1985 (029/St2b).

Farnsely, D.C.E., "Gambling and the Law: the Wisconsin Experience, 1848-1980", *Wisconsin Law Review* (Vol. 1980, No. 5), 1980 (174.6/F23).

Illinois State Lottery, *1984 Annual Report* (174.6/IL6).

Michigan Bureau of State Lottery, *1984 Annual Report* (174.6/M5).

National Conference of State Legislatures, *State Legislatures*, "State Lotteries: Roses and Thorns", March 1984 (328.11/N214).

National Council on Compulsive Gambling, (Compulsive Gambling Information Packet), 1980-85 (174.6/N211).

New Jersey Lottery, *1984 Annual Report* (174.6/N35c).

New Mexico Governor's Organized Crime Prevention Commission, *Lottery Report*, January 1985 (174.6/N463).

New York Lottery, *1983-84 Annual Report* (174.6/N48d).

Pennsylvania Department of Revenue, *The Pennsylvania Lottery 1983-84 Annual Report* (174.6/P3).

Public Gaming Research Institute, *The Lottery Journal: A Legislative Reference on State Lotteries*, October 1984 (174.6/P96).

U.S. Commission on the Review of the National Policy Toward Gambling, *Final Report: Gambling in America*, October 1976 (174.6/X4).

U.S. Congress, Senate Subcommittee on Intergovernmental Relations of the Committee on Governmental Affairs, *State Lotteries: An Overview* (hearing), October 1984 (174.6/X14).

U.S. Library of Congress, Congressional Research Service, *Overview of State Lottery Operations*, January 1985 (174.6/X12).

---, *Should the Federal Government Sponsor a National Lottery?*, March 1985 (174.6/X13).

Vermont Lottery, *1983-84 Annual Report* (174.6/V5).

Washington State Lottery, *1984 Annual Report* (174.6/W2b).

Weinstein, David and Lillian Deitch, *The Impact of Legalized Gambling: The Socioeconomic Consequences of Lotteries and Off-Track Betting*, 1974 (174.6/W43).

Wisconsin Legislative Reference Bureau, *Clippings:* LOTTERIES, STATE LOTTERIES AND LOTTERY-STYLE CONTESTS; REGULATION AND CONTROL; ANTI-LOTTERY LAWS (174.6/L91z).

---, Research Bulletin 73-1, "State Lotteries", May 1973 (174.6/W7b).

---, Informational Bulletin 77-2, "State Lottery Update", September 1977 (174.6/W7a).

Wisconsin Legislative Reference Library, "The Origin of Article IV, Section 24 of the Wisconsin Constitution", May 1943 (State Documents - LRL/o).

Wisconsin Taxpayers Alliance, *The Wisconsin Taxpayer*, "Lotteries and Other Gambling", February 1985 (174.6/W75).

RECENT LEGISLATIVE REFERENCE BUREAU PUBLICATIONS

Many of the titles are still available for distribution.

Research Bulletins

RB-78-2	Product Liability. September 1978
RB-78-3	Legislation "Show and Tell": The Enactment of 1977 AB-351. December 1978
RB-78-4	Authority and Functions of the Wisconsin Legislature. December 1978
RB-80-1	The Removal of State Public Officials from Office. January 1980
RB-84-1	Summary of the 1983-84 Wisconsin Legislative Session: 1983 Wisconsin Acts 1 to 550. June 1984
RB-85-1	A Legislative History of Shared Revenue In Wisconsin. January 1985

Informational Bulletins

IB-78-2	Gubernatorial Succession in Wisconsin and the Other States. January 1978
IB-78-3	The Regulation of Recombinant DNA Research. April 1978
IB-78-4	A Thumbnail History of Wisconsin Veterans' Legislation. July 1978
IB-78-6	The Documents of the Legislative Process. December 1978
IB-79-1	Public Service Commissions Today. January 1979
IB-80-1	Economic Impact Statements. January 1980
IB-80-2	Reapportionment in the 1980s: A Summary of Recent U.S. Supreme Court Decisions. January 1980
IB-80-5	The Recent History and Current Status of Abortion Law. September 1980
IB-81-2	Guidelines for Establishing Municipal Wards Following the 1980 Census of Population. March 1981
IB-81-3	Gun Control: A Look at the Various State and Federal Laws. May 1981
IB-81-4	Wisconsin Legislative Innovations. September 1981
IB-81-5	Drug Paraphernalia: State Laws and the Courts. December 1981
IB-82-1	State Tax Laws: Major New Taxes and Rate Changes Enacted by the 1947 to 1981 Wisconsin Legislatures. January 1982
IB-82-2	Not Guilty by Reason of Insanity State Legislative Alternatives. September 1982
IB-82-3	1983 Legislative Session: Fiscal Estimate Manual. November 1982
IB-83-1	Blueprints for Educational Reform. December 1983
IB-84-1	1983 Wisconsin Act 186 — Marital Property Act: A Compilation of Materials. May 1984
IB-84-2	Comparable Worth: The Pay Equity Issue. June 1984
IB-84-3	State Steps Toward Educational Improvement. August 1984
IB-84-4	Ask the L.R.B. November 1984
IB-85-1	Issues Related to Utility Diversification and Holding Companies. October 1985
IB-85-2	Beyond Bingo: The State Lottery Experience. November 1985

Wisconsin Briefs

Brief 83-2	The Story of Wisconsin in Capsule Form. September 1983
Brief 83-3	Current Trends in Teen-Age Drinking Laws. September 1983
Brief 83-4	The "Lemon" Law: Wisconsin's New Motor Vehicle Warranty Act. November 1983
Brief 83-5	Chapters Reprinted from the 1981-82 Wisconsin Statutes. December 1983
Brief 84-1	Wisconsin's Strategy to Spur Economic Development. January 1984
Brief 84-6	Wisconsin Laws Affecting the Blind, 1945-1983. May 1984
Brief 84-7	Compensation of Wisconsin Legislators 1836 to 1985. July 1984
Brief 84-9	Post-1980 Reapportionment of Wisconsin's Congressional and Legislative Districts. August 1984
Brief 84-10	What Is A Private School? October 1984
Brief 84-12	1985 Wisconsin Officers. December 1984
Brief 84-13	Brief Biographies: 1985 Wisconsin Officers. December 1984
Brief 85-1	Profile of the 1985 Wisconsin Legislature as of January 1, 1985. January 1985
Brief 85-2	Wisconsin Women Legislators — A Historical List. July 1985
Brief 85-3	Seat Belts and Air Bags: A Summary of Issues. August 1985
Brief 85-4	Executive Partial Veto of 1985 Assembly Bill 85. August 1985
Brief 85-5	The Sale of Cigarettes to Minors: Wisconsin's Legislative History. October 1985
Brief 85-6	Dram Shop Laws: Liability for Accidents Caused by Intoxication. October 1985

Vol. 3, Issue 11 June 1985

SPR STATE POLICY REPORTS

State Policy Reports is published 24 times a year by State Policy Research, Inc.'
7706 Lookout Court
Alexandria, Virginia 22306
(703) 765-8389
Annual subscription rates: $360 Full Service; $240 Publication only.

AN OVERVIEW OF THIS ISSUE

This year at least five states will be starting lotteries, increasing the pressures on the others to adopt this revenue source. This issue examines the increasing popularity of state lotteries and the opposition they have encountered.

Other articles in this issue review a text on state and local government, count economic development agencies, examine the costs of clean water, review patterns of transit finance, update the Whoops story, and speculate on the effects of ending the deductibility of state and local taxes on the taxation decisions of state and local officials.

THE POLICY ISSUES

How can state governments raise substantial amounts of money without raising taxes? How can states fight crime without spending more on law enforcement? How can states increase economic activity without extra economic development spending? How can a state's leaders provide citizens with something they want and benefit those who don't use the service as well? How can a state stem the flow of money from its residents to the treasuries of other states?

Some say state lotteries are the answer to all these questions. But opponents say lotteries answer other questions: How can a state encourage gambling and erode the morality of its people? How can a state start down a road that leads to more and more forms of legal and illegal gambling? How can a state hurt existing legalized gambling and legitimate businesses?

Lotteries are generating controversies in every state. Officials of states that don't have them are facing the issue of whether to adopt them. Officials of states that have them are facing attacks on their advertising practices, issues over how to spend the revenues, and decisions on authorizing new games.

Lotteries are potentially important to corporate and individual taxpayers as well. They can reduce the amount of money that otherwise would be raised by taxes. The other possibility is that they can finance spending that otherwise wouldn't happen, making lotteries of interest to those interested in education, economic development, and other areas of state spending.

THE GROWTH OF LOTTERIES

The lottery concept is sweeping through state government. Lotteries now exist or are being started in 22 states, up from 12 in 1974.

Lotteries are not a new concept. Private lotteries were used to raise money for such worthy causes as the Jamestown settlement, the Colonial Army, and Ivy League schools. Thomas Jefferson set up a lottery late in life to pay off his personal debts. However, the concept of allowing private lotteries was gradually rejected in state policies which typically ban them. Since the linkage of crime and gambling in the Kefauver crime hearings in the 1950s, federal law banned them as well.

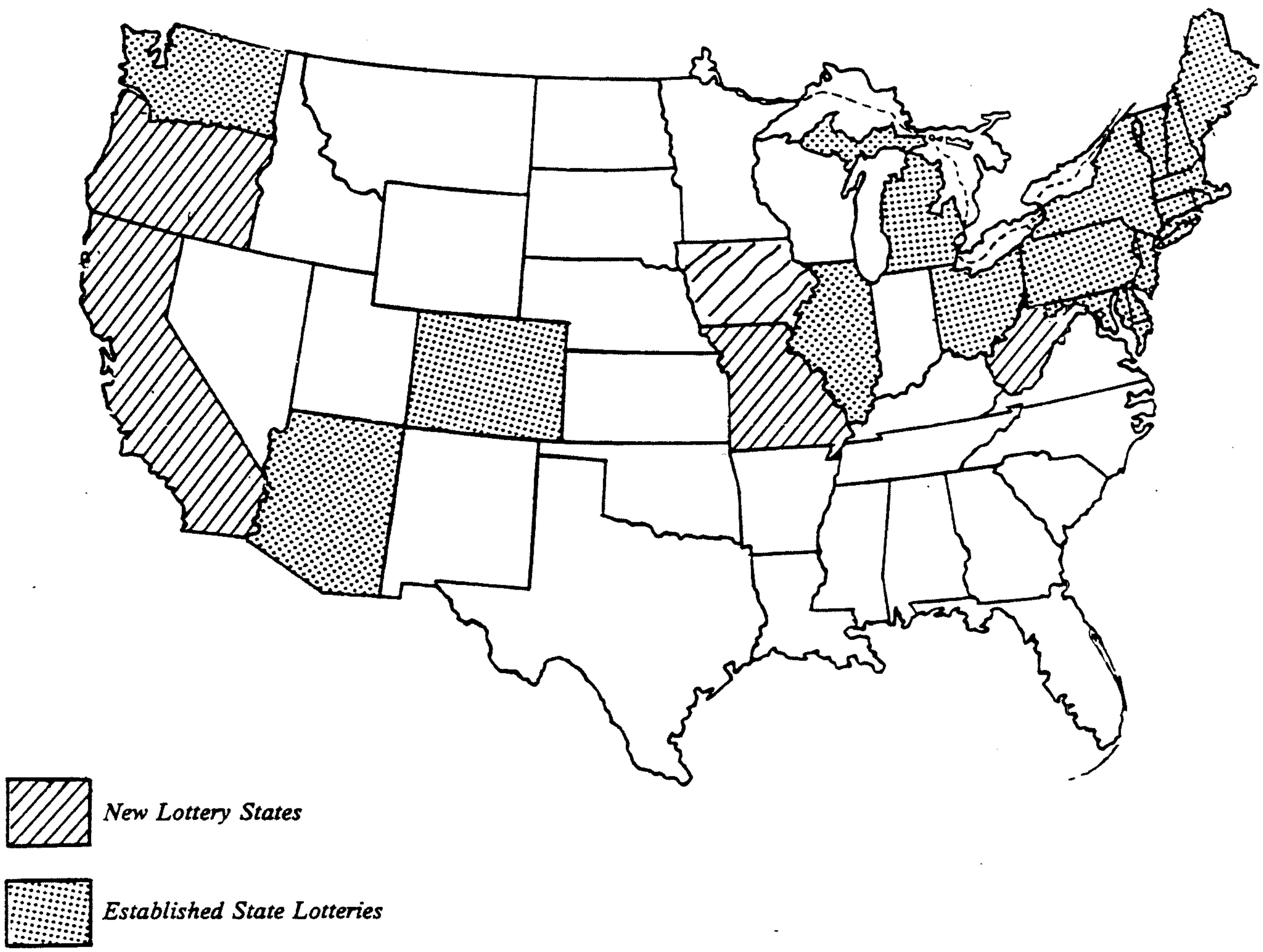
The first state lottery was the New Hampshire sweepstakes, started in 1964. Other states soon followed. After tension developed between the lottery states and the Department of Justice, Congress passed legislation in 1975 which clearly authorized lotteries run by state governments. Table 1 shows the states that have adopted lotteries and when they began operating or are scheduled to do so.

Table 1: Dates of First Lottery Operation

State	Year Operating	State	Year Operating
New Hampshire	1964	Rhode Island	1974
New York	1967	Delaware	1975
New Jersey	1971	Vermont	1978
Connecticut	1972	Arizona	1981
Massachusetts	1972	Washington	1982
Michigan	1972	Colorado	1983
Pennsylvania	1972	California	1985
Maryland	1973	Iowa	1985
Illinois	1974	Missouri	1985
Maine	1974	Oregon	1985
Ohio	1974	West Virginia	1985

Until Arizona's adoption in 1981, lotteries were an East Coast phenomenon. Now adoption by the three West Coast states and two on the West bank of the Mississippi River mean there are lottery states everywhere but the Southeast. In the Southeast, serious consideration is being given to lotteries in several states. The geographic distribution (minus Iowa which adopted recently) is shown on Figure 1 which was provided by the Public Gaming Research Institute (51 Monroe St., Suite 1500, Rockville, MD 20850).

Figure 1: The Geographic Pattern of Lottery Adoption, 1985



State Policy Reports is published twice a month for $240 per year by State Policy Research, Inc., 7706 Lookout Court, Alexandria VA 22306. Application to mail at 2nd class postage rates is pending at Alexandria VA. POSTMASTER: Send address changes to: State Policy Reports, 7706 Lookout Court, Alexandria VA 22306

The growth in ticket sales revenue has paralleled the growth in participating states. That growth is shown in Table 2.

Table 2: Growth in Lottery Revenues, FY 1978-FY 1984
($ billion)

Fiscal Year	Gross Revenue
1978	$1.6
1979	1.8
1980	2.1
1981	2.7
1982	3.5
1983	4.8
1984*	6.8

*Data for FY 1984 from the Public Gaming Research Institute are not perfectly comparable with Census data from prior years.

THE DEBATE OVER LOTTERIES

Introduction: The concept of a lottery is simple enough, and there are only a limited number of arguments made for and against it. The sections below indicate the arguments, facts that may bear on each, and, where relevant, cite the informed opinions of Daniel B. Suits, a professor of economics at Michigan State, who is one of the few academics to study the subject.

Lotteries Dupe the Public: The public certainly understands that lotteries are gambling and knows each wager will be lost most of the time. However, it is unlikely that the public knows the exact odds of winning, although these are not hard to find out. Those odds are very long. For example, to finance one million dollar prize with one dollar tickets would make the odds of winning with a single ticket a million to one, even if there were no administrative costs and no net proceeds to the state.

While the public may have some feel for these odds, amateur gamblers probably don't have a good feel for the number that determines what it will cost them to participate — the expected value of return. This varies substantially from one form of gambling to another. The expected value is the percentage of the amount bet the gambler with random luck could expect, on average, to win back with one play. It is calculated as the total prize money divided by the total amount bet. It varies from game to game as shown on Table 3.

Based upon what limited survey information exists, Professor Suits believes that gamblers seem to have a general feel for the odds, but don't require precise knowledge of the subject because, for most people, it isn't relevant to why they gamble. For many, he says, gambling is viewed as entertainment. For them, the losses at a track are simply expenditures like buying dinner or going to a movie. Winning is unexpected; so it is pleasurable. Because losing is expected, even losing less rather than more may give pleasure.

Table 3: Likely Result of One Bet in Various Games
Average Amount of Bets Returned as Payoff

Type of Bet	Payoff %
Sports Betting in the Office	100
Private Poker Parties	100
Casino Craps Line Bet	95-98
Casino Blackjack Bet	95-98
Casino Roulette	95
Sports Betting, Bookies	85-95
Typical Horse Racing	80
Slot Machine	80
Numbers Bets, Private	50-60
Bingo Games	50
State Lotteries	40-50

The payoffs shown on Table 3 are reduced by tax consequences. Casual bets among individuals and illegal betting have no practical tax consequences because winnings are not customarily reported, nor are small payoffs at racetracks or in state lotteries. However, large winnings are reported and taxable just like business income, with losses in the year deductible from the gains. However, because people do not believe they will be winners, many cannot prove their losses.

Partly to avoid the serious tax consequences of a large payment in one year and partly to inflate the stated prizes, many lotteries make payments over a period of time. This can somewhat distort value, depending on how the lottery is advertised. For example, the value of a prize of one million to be paid out over 20 years is considerably less than a million now. Lack of candor in dealing with this subject has made some non-lottery state officials critical of state lotteries. For example, last October, Texas Governor White told the press that of all the possible ways to raise state money by gambling, he liked lotteries "least of all." He continued:

> One of the confusions in the lottery, and one of the really consumer frauds that is sponsored by a state, is when you see these so-called $20 million winners. They don't give the winner a check for $20 million like it appears. What they do is give them $20 million over a number of years, sometimes longer than the life expectancy of the winner, and then the discounted value of that is below the $20 million.

The grand jackpots in state games come at truly long odds. Money magazine calculated the odds for the major state games in its October 1984 issue. The odds in these games depend upon (1) the field of numbers from which a bettor's number is picked -- the larger the field, the more difficult to win, (2) the number of numbers to be picked -- the larger the number, the more difficult, and (3) the percentage of bets returned as the top prize. In Maryland and Michigan, the odds of winning the big lotto prize are 3.8 million to one. Other games give somewhat better odds, but better odds are typically associated with lower top prizes.

Lotteries Are Regressive: Lotteries, like taxes, are ways to finance state government. One way to examine their merits is by comparing them with taxes. One criterion for taxation is how it affects persons of different incomes — with a tax that tends to take higher proportions of income from lower income persons defined as regressive.

Professor Suits has updated a table from a previous article (his "Gambling Taxes: Regressivity and Revenue Potentials," National Tax Journal, Vol. 30, No. 1, 1977). Table 4 shows for each income class, the percentage of total income received and his estimate of the percentage contribution to state lottery revenues. For example, his calculations indicate that persons with income below $20,000 receive 2% of the nation's personal income, but contribute 6% of lottery proceeds.

Table 4: The Distribution of Income and Lottery Spending, Estimated 1985

	Percentage of Total	
Income Grouping	Income	Lottery Losses
Under 20,000	2	6
20,000-29,999	9	19
30,000-39,999	19	29
40,000-60,000	23	18
60,000-90,000	24	20
Over 90,000	23	8
All Groups	100	100

The table shows lotteries to be regressive. Those with incomes of $40,000 or less provide over half of all lottery revenues, though they have only 30% of the income.

Another way of looking at this question is to use data on lottery sales for subareas of states with known demographic characteristics. For example, Baltimore is a typical Eastern city with high concentrations of poor and low middle income individuals. Its residents comprise 17.8% of Maryland's population, but a third of the PICK 3 (a popular lottery game) sales are there. Montgomery County, a Washington suburb that is one of the most affluent counties in the nation, accounts for 13.7% of the state's population but only 8% of its PICK 3 sales.

Another lottery expert is Charles Clotfelter, a Duke University professor. He looks on state lotteries as two separate decisions. The first is the decision to legalize gambling. That decision being made, the question is how much to raise from it as a percentage of total sales. That decision he views as tax policy — "if it looks like a tax and walks like a tax, then it is probably something like a tax." From that perspective, the "tax" on legalized gambling is much higher than state taxes on alcohol and tobacco and considerably higher than general sales taxes. The state take as a percentage of the amount bet is also considerably higher for lotteries than from casinos or horse racing.

The Congressional Research Service, which recently examined lotteries, also concludes that they take a higher proportion of the incomes of lower income people than of higher income persons.

State lottery directors and lottery equipment suppliers are sensitive to the regressiveness argument and attempt to deal with it in a variety of ways. One is by shifting attention from the percentage of income paid to the state to the percentage of persons in each income class who play lotteries.

Maryland Lottery Director Martin Puncke discussed regressivity before a U.S. Senate committee last year by citing a variety of studies which "clearly and consistently verify the fact that lower income persons do not play the lottery in greater proportion than their income group is in proportion to the general population." Using this concept, rather than the percentage of income devoted to a tax, would show that the sales tax, conceded to be regressive by all experts, is not regressive because it is paid by the same proportion (100%) of persons in all income brackets.

Scientific Games, a major seller of lottery tickets and equipment, commissioned a survey of lottery participation with the results shown in Table 5.

Table 5: Percent of Population Participating in Lottery by Income Class, 1982 Unweighted Average of Five Large Lottery States

Income Class	Percentage Participation
Under $6,700	14.7%
$6,700-10,999.	9.3
$11,000-17,999	10.5
$18,000-22,999	18.6
$23,000-33,999	25.3
$34.000-56,000	16.7
Over $56,000	4.8

This evidence is consistent with studies conducted by individual state lottery agencies. These tend to show the highest participation rate among middle income blue collar workers. The National Conference of State Legislatures takes the same view (State Legislatures, March 1984): "Statistical profiles of lottery players, however, show that the poor and the rich play lotteries, particularly the instant ticket games, in numbers smaller than their share of the population."

There are some logical reasons for such patterns. Many poor persons, no doubt, feel they don't have money to spare for gambling and, in urban areas, those who want to gamble seriously have illegal games available, often with better odds. The affluent also avoid state lotteries — presumably preferring not to gamble or to take their chances in Las Vegas and Atlantic City, on Wall Street, or at the Chicago Board of Trade.

The disproportionate players of state lotteries are the middle class — the secretaries, factory workers, retail clerks, and construction workers. A logical explanation for this phenomenon is that lotteries have some value as entertainment. Picking numbers can be fun; discussing picks with the car pool or neighbors can be fun;

watching numbers being selected on TV can be fun; and, of course, winning can be fun. Viewed this way, lotteries are competing with other forms of entertainment and can't be analyzed as one would analyse either a tax or more serious gambling. This is the view that many state lottery directors tend to take.

Another plausible hypothesis is that the charitable aspect of state lotteries is significant for the middle class — as a rationalization at a minimum and a motivation at maximum. At best, players increase their wealth; but at worst they contribute to education or whatever other cause the proceeds finance.

Thus, proponents of lotteries have established that participation is not concentrated among lower income groups, but have not directed their attention to the share of income spent on lotteries, leaving the work of economists cited above as the most authoritative word on regressivity. However, the question is whether regressiveness is an important consideration in deciding state lottery policy.

There are several answers to the regressiveness argument. One is that the impact on different income groups of a new revenue source can only be considered along with the effects of the corresponding expenditure. For example, a lottery used to finance programs for poor elderly persons would not be regressive, considering both the revenues and the spending.

Another answer is to view the revenue situation of a state as a whole. Individual revenues — such as lotteries, cigarette taxes, beer taxes, and gas taxes — might be regressive. But if these were combined with a highly progressive income tax, the revenue system as a whole might satisfy someone's criterion for progressivity.

The third argument is that a lottery does not cause the poor to gamble. It simply satisfies a need that already is felt which will be satisfied by illegal and/or other forms of legal gambling if not indulged by the lottery. If it is assumed that lotteries don't cause gambling, then it is the fact of gambling that hurts the poor, but lotteries don't add to the problem. The rebuttal is evidence that lotteries do cause some gambling to take place that otherwise wouldn't.

A fourth argument is that the state is only supplying the object of a discretionary consumption expenditure. The lottery costs to households are not a tax, because the payment is a voluntary one. Therefore whether the poor spend a larger proportion of their income on lotteries than the rich is of no more concern than whether they disproportionately consume hot dogs.

Gambling is Immoral: By definition, the "immorality" of lotteries and betting is a value judgment. As Steven Gold, fiscal expert for the National Conference of State Legislatures, puts it: "... the moral questions are never answered."

Much of the opposition to legalized gambling comes from religious groups. When a Virginia legislative committee held hearings on a proposed lottery earlier this year, representatives of various denominations expressed concern that lotteries promote the "idea of getting something for nothing" and "appeal to the human desire to get rich quick." One commented, "Parting the sucker from his dollar is not the job of government."

In testimony to Louisiana's Joint Lottery Subcommittee, the leader of lottery opposition argued:

> The lottery like other forms of gambling is contrary to our state and nation's Judeo-Christian ethic. Even though there are no "Thou shalt nots" concerning gambling in the Bible, it does offer many principles which indicate that gambling is wrong. The Bible instills a work ethic; gambling instills a something-for-nothing attitude. The Bible condemns covetousness and materialism, both of which are the heart of the gambling process. The Bible teaches love for God and neighbor whereas gambling defies the sovereignty of God in the direction of human events and seeks personal gain and pleasure from another man's loss and pain.

Some of the other arguments analyzed in this article (e.g., regressivity, stimulation of illegal gambling, producing compulsive gamblers, disproportionate appeal to minorities) are also offered as moral arguments.

Most Americans do not find moral arguments against gambling persuasive in their personal decisions. Participation is very high in promotional sweepstakes and most Americans bet money on something. Many churches sponsor gambling, such as Bingo games.

A more sophisticated form of the morality argument recognizes the gambling decision as an individual one, but suggests that government should not promote gambling by becoming a vendor and advertising its joys. Those who advocate this perspective suggest that if government must sell sin, it should do so in ways comparable to state liquor stores. State liquor stores do not try to promote drinking in any way. Lotteries advertise aggressively, often suggesting their product promotes fun and happiness.

Lotteries Appeal Disproportionately to Minorities and the Poor: Those who believe that lotteries are patronized principally by poor people also sometimes make the argument that they are particularly harmful to one or more ethnic groups. **Reports** knows of no statistical information which holds income constant and compares gambling participation by ethnic characteristics.

The argument that lotteries appeal primarily to the poor can be made separate from the regressivity argument. Someone who thinks regressivity is irrelevant because lottery payments are voluntary may still want to avoid a state activity he believes will disproportionately encourage gambling by the poor. However, separated from the regressivity argument, this argument is not particularly strong. First, percentage participation is highest among the middle class, and denying a state lottery to the poor means denying it to this segment of the population also. Second, accepting the argument is tacit acceptance of the concept that governments, not the people involved, are best equipped to choose spending patterns.

This perspective is provided by testimony of an elderly woman who had played the Maryland game and then moved to lotteryless North Carolina. She testified to a committee of the legislature:

> I'm an old lady. I'm on social security. I guess I'm one of "the poor" that these gentlemen want to protect. Where do they get the right? I can

protect myself ... played the Maryland lottery. I won and lost. But I enjoyed it. It gave me something to look forward to. It's fun and I have a right to play and not have somebody tell me I'm wasting my money and hurting myself and my family when I'm not.

Gambling Will Take Place With or Without Government Involvement, So Government Should Act to Make it as Clean As Possible and Take for Public Purposes the Profits that Now Go to Crooks: A national commission on gambling commented in its 1976 report: "It is not a question of whether people will or will not gamble, but it is only a question of who they will game with — a legal or illegal activity."

The key question is the extent to which lottery betters come from the ranks of former illegal betters. The available evidence is ambiguous. Claims run all the way from some lottery chiefs who claim to have diverted most of the illegal play to some experts who believe the hype given the legal game may have helped the illegal game. Professor Suits concludes that illegal operators have not been hurt, and may have been helped, by the state games.

The illegal operators have several things going for them. First, their payoffs are non-taxable in fact, though not in law. Second, they can sell on credit, which states don't do. Third, they don't finance a large state take of profits, so they can offer better odds. Fourth, they can deliver tickets and payoffs, so some customers will not have to go somewhere to buy them. Therefore, some bettors of illegal numbers will stay with them, rather than (or in addition to) playing a state lottery.

There are, no doubt, some things that happen to gamblers in the illegal market that don't happen in lotteries — numbers runners skipping off with payoffs and the like. No one is fully aware of the incidence of these problems. Professor Suits argues that these problems almost never occur because those who run illegal lotteries recognize that they can't sell tickets without a reputation for running an honest and reliable game.

But the main objection Suits has to this argument is that, if one accepts it, it doesn't suggest a state lottery — it just suggests that states should legalize lottery-type betting. Then it could be handled by new operators, the local bank, or department store — whatever the customer and suppliers decided in the free market. To legalize numbers betting only for state government leaves the field to illegal operators and state government. As Suits puts it, "the state shares the monopoly with the mob."

Legalization is not entirely far-fetched. Harper's (July, 1983) ran the following comment:

> But legalization might eliminate the organized-crime problem by forcing numbers running above ground. Bernard Rome, former chairman of New York City's Off-Track Betting Corporation, proposes that the state issue franchise to illegal numbers operators. He argues that the operators are more efficient than the state and would provide more state revenues than the state-run games do. A Harlem attorney adds that regulated numbers would reduce the police corruption in current numbers rackets. And as accountable, publicly chartered corporations, numbers franchises would tend to divorce the business from other activities of organized crime.

The Decline and Fall Theory: Another argument against lotteries is that they lead to bigger (and presumptively worse) forms of gambling. Arizona's Governor Babbitt used this argument in campaigning unsuccessfully against the California lottery last year. Arizona has a lottery adopted by popular vote, which Babbitt is not trying to repeal. According to press reports, he said:

> What it has created in Arizona is a culture of gambling. It has put the state in the unhappy position of being the sponsor and promoter of gambling, of pushing this lottery business on TV, billboards, and radio.
>
> This culture of gambling is really sending us down a long slope toward casino gambling.

There is no way yet to gain empirical evidence on this proposition. New Jersey had a lottery before it adopted casino gambling but Nevada has had casino gambling and doesn't have a lottery. No other states have casino gambling.

Another version of the decline and fall theory is that state officials will get so hooked on maximizing lottery income that they will stop at nothing to part fools and their money. In opening hearings last October on state lotteries, U.S. Senator Durenberger commented:

> And, once into the gaming business, are the elected officials of state government able to draw any line in the sand at all -- to insist, that despite their desire for revenue without pain, there are some schemes so gross that they are not a public good under any circumstances? Or is every dreamer, rich or poor, fair game because the flim-flam man works under the dome of a public building?

A special case of the decline and fall approach concentrates on the involvement of a single firm. This argument was made by California Attorney General John Van de Kamp in an OpEd piece in the March 8, 1984 Sacramento Union:

> Lottery proposals have been introduced before in California, and they have failed. The difference today is money. For this year a powerful consortium of individual and corporate interests — with primary funding reportedly coming from a firm that manufactures lottery tickets — is financing an intensive, expensive and sophisticated effort to qualify a lottery proposal...
>
> The firm "Scientific Games, Inc." of Atlanta helped sponsor successful ballot drives in Arizona, Colorado and Washington, D.C. According to the Times, it is a subsidiary of Bally Manufacturing, which is the nation's largest manufacturer of slot machines.
>
> That latter fact alone should prompt concern. There is considerable evidence to indicate that gambling — once allowed to have a legal life of its own under the aegis of the state — becomes a kind of monster. States that once held lottery drawings annually begin to hold them monthly, then daily.

Somewhat the same argument was made by Arizona's Governor Babbitt in urging an Iowa audience to avoid a lottery:

> I'm telling you lotteries amount only to the state stepping in and endorsing gambling as a way of life. The revenue is disappointing, and it attracts all kinds of flakey characters who hang around the fringes.

Apparently, Arizona's "flakey characters" are not from Scientific Games. The state lottery board in Arizona was awarding a new five-year contract to the firm while the governor was in California making his arguments against lotteries.

Lotteries Cause Compulsive Gamblers: The American Psychiatric Association recognizes compulsive gambling as a diagnosable and treatable disorder. It can have dramatic effects — most significantly loss of money for food, shelter, and clothing for any affected family. For lotteries to cause it, they would have to cause a person to gamble who otherwise would never have become exposed to a chance to find out how much he liked gambling, or, if gambling is gradually addictive, to gamble more than he otherwise would. The evidence on this point is ambiguous, but serious gamblers often stick with the best odds games shown on Table 3, of which state lotteries are not one.

In an article prepared recently, the director of the Maryland lottery, a former law enforcement official, handled the subject this way:

> A compulsive gambler must have a fast or immediate result from his act with little regard to the result of winning or losing. A lottery is too passive a game. Dr. Robert Custer, medical advisor to the National Council on Compulsive Gambling, and one of the nation's foremost experts on the subject, says that no reliable studies have been done linking lotteries to compulsive gambling...

Some states with lotteries have special programs to help compulsive gamblers. The philosophy behind these is reflected in Maryland's statute:

> Maryland with its extensive legalized gambling has an obligation to provide a program of treatment for those who become addicted to gambling to the extent that it seriously disrupts lives and families.

Maryland's compulsive gambling program was the first. It was followed by adoptions in Connecticut and New York (1981) and New Jersey (1983, for help call 800-GAMBLER).

Public Opinion Favors Lotteries: All available evidence suggests that state lotteries enjoy the support of a majority of the population. Nationwide, the approval percentage is around 70%. The people who vote like them too. Table 6 shows the results of the four lottery referendums last November.

Table 6: Results of Lottery Referendums in November of 1984

State	For	Against
California	58%	42%
Oregon	66%	34%
West Virginia	66%	34%
Missouri	70%	30%

Referendums on lotteries are the result of three situations. First, many legislators want the people to have the chance to vote on this controversial issue. Second, establishing a lottery in some states requires a constitutional amendment. Third, initiatives have been used in some states where public opinion supported the lottery, but the legislature would not adopt one.

Lotteries Will Interfere With Other Forms of Legalized Gambling: Some of the stiffest opposition to lotteries has come from those with interests in horse racing and Bingo games. They fear the state as a competitor.

Casino operators share this fear. A 1983 report by the Legislative Counsel Bureau of Nevada commented:

> The overriding concern relates to the impact of a state lottery on Nevada's gaming industry. Nevada's gaming industry has gone on record in opposition to a state lottery. Both the Gaming Industry Association of Nevada and the Nevada Resort Association hold the position that a Nevada state lottery would have a detrimental impact on gambling. They believe that a lottery would compete with gaming and, consequently, reduce the industry's earnings.

However, there is little statistical evidence on the effects of lotteries on other forms of legal gambling. The horse racing take in states that have started lotteries generally seems to be unaffected by the creation of lotteries. A study in New Jersey showed that 84% of the serious race fans (two or more visits to a track in the last year), had never bought a lottery ticket. Several consultant reports suggest no relation between lotteries and horse racing.

The Nevada legislative staff's conclusion was: "Some believe the potential impact of a lottery on gaming needs to be determined through a marketing survey and a detailed financial analysis based on a definite lottery proposal."

If the amount of money people want to gamble is a fixed quantity, then any new competitor will reduce the share of old competitors, which is a concern of some who are interested in horse racing. On the other hand, if publicity about state lotteries increased public acceptance of, and desire to participate in, gambling, lotteries might increase interest in horse racing.

Lotteries Raise Substantial Amounts of Needed Money in Ways Preferable to Taxes: "If a state doesn't need revenue, then it doesn't need a lottery" is the way the President of Scientific Games explained the situation to a joint subcommittee studying possible lottery adoption in Louisiana.

While there are arguments about predicted revenues, there can be no reasonable dispute over the basic question of whether lotteries can raise lots of money — they can and do. The California Journal (March 1985) calculated that the new California lottery should raise more money than the budgets of six states and more money than the combined gross national products of Chad, Laos, and the Solomon Islands. The Journal reports that Colorado's lottery director commented that: "In terms of net revenues, California's lottery will become one of the nation's top 50 corporations."

Lotteries in FY 1984 provided over $500 million to the State of Pennsylvania and over $350 million in net state revenues to Illinois, New Jersey, and New York. However, the net state revenues vary considerably among states as shown on Table 7, which puts FY 1984 net revenues on a per capita basis.

Table 7: Per Capita Lottery Revenues for State Government, FY 1984

Rank	State	Revenue Per Capita	Rank	State	Revenue Per Capita
1	Maryland	$48.1	9	Delaware	22.8
2	New Jersey	47.9	10	New York	22.0
3	Pennsylvania	43.4	11	Rhode Island	19.1
4	Connecticut	33.4	12	Washington	16.3
5	Illinois	32.8	13	Colorado	12.8
6	Massachusetts	29.2	14	Arizona	5.9
Weighted Average		**29.0**	15	New Hampshire	5.8
7	Michigan	27.5	16	Maine	3.9
8	Ohio	23.3	17	Vermont	2.5

Lottery advocates are fond of tables and graphics which show potential net revenues for the states that have not yet started lotteries. Table 8 shows in its middle column what each non-lottery state government would net from a lottery that raised the national average per capita (FY 1984 net divided by July 1984 population). The maximum number shown assumes a lottery could raise $50 per capita, slightly higher than Maryland's leading revenue production of $48.1 per capita in FY 1984. The minimum column assumes each state would mimic Vermont's performance. It understates what a larger state should be able to raise and what Vermont expects to raise by adding a New England regional game.

Table 8: Total Lottery Revenue Potential, Non-Lottery States ($ million)

Rank	State	Max.	Avg.	Min.	Rank	State	Max.	Avg.	Min.
1	California	1,281	743	64	18	Oregon	134	78	7
2	Texas	799	463	40	19	Mississippi	130	75	6
3	Florida	549	318	27	20	Kansas	122	71	6
4	North Carolina	308	179	15	21	Arkansas	117	68	6
5	Georgia	292	169	15	22	West Virginia	98	57	5
6	Virginia	282	163	14	23	Utah	83	48	4
7	Indiana	275	159	14	24	Nebraska	80	47	4
8	Missouri	250	145	13	25	New Mexico	71	41	4
9	Wisconsin	238	138	12	26	Hawaii	52	30	3
10	Tennessee	236	137	12	27	Idaho	50	29	3
11	Louisiana	223	129	11	28	Nevada	46	26	2
12	Minnesota	208	121	10	29	Montana	41	24	2
13	Alabama	200	116	10	30	South Dakota	35	20	2
14	Kentucky	186	108	9	31	North Dakota	34	20	2
15	South Carolina	165	96	8	32	Wyoming	26	15	1
16	Oklahoma	165	96	8	33	Alaska	25	14	1
17	Iowa	146	84	7					

The estimates on Table 8 reflect the performance of established state lotteries. Lags in getting lotteries started and having them understood by the public would cut the estimates for the initial year of operation. For example, Missouri officials are not assuming any revenue in FY 1986 from their new lottery in their budget projections, although there will likely be some.

The differences among states in per capita revenues are a function of a number of factors. One is the demographic differences in population. A state with a disproportionate number of persons religiously opposed to gambling will likely not reach average sales. Another variable is whether the full range of games is offered. Yet another is how well the lottery is promoted.

The revenue potentials are large enough to be significant. Table 9 expresses the "average" lottery potential from Table 8 as a percentage of each state's general fund revenues in FY 1985 as reported in the most recent fiscal survey of the National Association of State Budget Officers.

Table 9: Potential Lottery Earnings as Percent of FY 1985 General Revenue

Rank	State	Percent	Rank	State	Percent	Rank	State	Percent
1	Montana	6.5	12	Indiana	4.8	23	Iowa	3.9
2	South Dakota	6.3	13	Arkansas	4.7	24	Georgia	3.9
3	Idaho	6.0	14	Oregon	4.7	25	West Virginia	3.9
4	Nevada	5.8	15	Virginia	4.4	26	North Dakota	3.5
5	Nebraska	5.8	16	Texas	4.4	27	New Mexico	3.1
6	Oklahoma	5.6	17	Kentucky	4.3	28	Louisiana	3.1
7	Tennessee	5.6	18	Kansas	4.3	29	Wisconsin	3.1
8	Missouri	5.3	19	North Carolina	4.2	30	California	2.8
9	Mississippi	5.3	20	South Carolina	4.1	31	Minnesota	2.3
10	Alabama	5.2	21	Wyoming	4.0	32	Hawaii	2.0
11	Florida	5.1	22	Utah	4.0			

Because the numerator for this calculation is about $29 times population for each state, differences in the general fund denominator control the results. The states near the top have: (1) relatively low spending and revenue levels, (2) a high proportion of expenditures in special funds (e.g., Montana), or (3) both.

The money argument is especially persuasive with officials of states that already have lotteries. Where it exists, state officials who have doubts about state lotteries have been reluctant to propose elimination. As Governor Hughes of Maryland is quoted as having commented in a news conference:

> The lottery has grown to be the third largest revenue producer for the state ... it is some $200 million of revenue to the state. So, from a practical standpoint, even though you may not like it, it makes it difficult to do something about doing away with it.

Ben Cardin, Speaker of Maryland's House, a lottery opponent, puts it this way (State Legislatures March 1984):

> We're hooked on it. We're dependent on it. If we wanted to halt it, we couldn't. I don't mind people gambling. It's just not a good way to raise money. If the needs are there, for the elderly or the handicapped or students, then we should provide the (tax) money for it. And over the long haul, it's not a reliable source of revenue. It's a very big money maker, very quickly, but it has changed the state. It has increased the appetite for gambling.

An anonymous Colorado official put it this way to the Arizona Republic (October 9, 1984):

> The lottery is a massive statement that good in life comes to you by being lucky, not what you put into it. I see the hyped-up Colorado lottery ads and tell my daughter they make me embarrassed to be associated with the state. But as a politician, I'm not fighting it; I swallow my tongue.

While there are some officials in states that have adopted lotteries that don't like them, some state officials are clearly happy with them. For example, in Vol. 1, No. 2 of The Lottery Journal, Illinois Governor Thompson calls the lottery "a very good deal" for everyone in the state.

To deal with this revenue argument, lottery opponents typically return to one of the other arguments cited above. For example, the Rochester attorney and former state senator who heads an anti-gambling group in New York argues:

> Sure it raises money, but it takes it from those least able to afford it ... If the only goal was to raise money, you could take it from houses of prostitution.

Lottery Revenues Are Unpredictable: Opponents argue that lotteries are not a satisfactory state revenue source. For example, in his June 1984 press release opposing the California lottery, Lieutenant Governor Leo McCarthy argued:

> It does not offer a predictable source of income on which to decide the state's spending priorities. As a source of education funding, it makes the future of our children dependent upon the public willingness to buy lottery tickets. Experience shows that lotteries are not a steady revenue source; they start off big and then diminish in succeeding years.

One premise of this argument is that, other things being equal, a revenue source with sharply fluctuating yields is worse than one with more stable yields. The validity of this premise is not obvious. States encounter financial problems when yields are less than forecast, no matter how stable the source. If revenue estimators are careful to estimate revenues conservatively, instability of yields is not a problem. For example, estate taxes are notorious for unstable revenues because one very large estate can affect revenues considerably, but deaths of millionaires are not very predictable.

More important than the predictability of a single revenue source is the predictability of total revenues. Thus, the real concern is about a revenue system in which major taxes all respond in the same way to the same unpredicted event — which is what happens to sales and income taxes in a recession. In this context, lotteries are a plus because their revenues don't seem to be much influenced by business cycles.

The second premise is that it is a common pattern for lottery revenues to decline. To check this, **Reports** looked at data for three years on the sales of the 14 state lotteries that have been in operation since FY 1981 and found steady growth in every one of them. In addition, it is not obvious that a revenue that will exceed $600 million in the first year and then drop to a steady $300 million a year is worse than one that would simply raise $300 million a year from its start.

Declining revenue possibilities are more troublesome if the lottery revenue is earmarked. In that case, spending levels may have adjusted to revenues, so declines will force cutbacks.

Lotteries Are an Inefficient Way to Raise Money: This argument compares the lottery to a tax and calculates administrative costs as a percentage of revenues. Typically, collecting taxes costs from 1% to 3% of revenues while administrative costs of lotteries were 12.5% of net state revenues in FY 1983. In small states, the administrative costs are considerably higher as a percent of revenues. While Pennsylvania spent 8.5% of net revenues on administration in FY 1983, Vermont spent 68% and Maine, 77%.

The reasons why lottery money costs more to collect than taxes are clear. States advertise their lotteries and don't advertise their taxes and pay their collectors (e.g., retail stores selling tickets) something like five percent of gross, while they pay their tax collectors (e.g., employers who withhold, merchants who collect sales taxes) little or nothing.

While the lotteries have high costs when compared to taxes, they have very low costs when compared to private business. Lotteries yield profits of around 40% of sales, but in most industries, a firm that can get 5% of sales as profits is doing well.

However, taxes cause inefficiencies that are not measured by their administrative costs. All taxes distort economic choices and impose deadweight costs on the economy. Economists differ on the significance of these costs for various forms and levels of taxes, but the effects are real and substantial. Because lotteries reflect buying decisions, not involuntary payments, they do not cause such distortions.

Lotteries Reduce or Increase Revenues of Other Businesses: Lottery proponents and opponents like to stress their impact on the general level of business activity in a state.

Lottery proponents claim lotteries increase business activity. A paper by an executive of Scientific Games (Economic Benefits from A State Lottery) comments on the money retailers make from selling tickets and notes further:

> In addition, the availability of lottery tickets often increases a retailer's "traffic" and, hence, his gross sales.
>
> The lottery creates jobs. Besides additional jobs that may be created as an ancillary effect of money spent on advertising and the activities of retailers, the lottery will require between 50-150 full time employees in areas of administration, security, data processing, field reps, etc.

The point is that a state lottery is not just a revenue raiser. It is a business which has economic benefits for many people and small businesses in the state.

Lottery opponents see a different effect. As put by the Executive Director of the Coalition Against Legalizing Lotteries:

> California business foresees a major dislocation of the purchasing dollar. Hard-earned wages that should be spent on food and clothing will go for lottery tickets. As the result of the lost business, the state will receive less sales tax.

These arguments reflect parallel omissions. Scientific Games looks at where the money goes without looking at where it comes from. The Coalition looks at where it comes from without looking at where it goes.

There is no reason to expect that a lottery would have any significant effect on the overall level of economic activity within a state.

A lottery just redistributes purchasing power. The 40-50% of revenues paid out as prizes simply reflect redistribution from losers to winners. The state share reflects redistribution from the losers to the public sector, where revenues are used to pay teachers, provide tax relief for the elderly, or other designated purposes. The administrative costs, retailer commissions, and advertising dollars are all spent within the state, with limited exceptions.

As a result, some people are worse off and some are better off, but in the aggregate, the income of the people of the state hasn't changed. Like an increase in taxes, the state share of the lottery leaves less money for private consumption. So sellers to private consumption, such as clothing stores, will be slightly less well off. But their loss will be the gain of those who sell public services, such as teachers and lottery employees. The retailers who sell lottery tickets may increase their sales of cigarettes and milk, but others must lose what they gain because nothing about a lottery will cause statewide consumption of either to increase.

A State Might As Well Get Money From A Lottery As Residents Already Play Ones in Neighboring States: In the 1974 edition of his Complete Guide to Gambling, John Scarne predicted that all states would be forced to adopt lotteries:

> In 1963, the day New Hampshire voted a statewide lottery, I predicted that New York and all states adjoining New Hampshire would quickly adopt statewide lotteries. My reasoning was obvious. If only one state has a legalized lottery, this takes away large sums of lottery money from residents of adjoining states. In order to keep that money for their own needs, ever increasing numbers of states are legalizing state lotteries — and now that these lotteries have started to operate, I believe they will spread across the country. By 1980, every state in the country with a fair-sized population will operate its own statewide lottery.

His prediction missed the date, but did seize on an argument that many state officials are finding persuasive.

A substantial number of players of existing state lotteries are from out-of-state, so adoption of a lottery diverts in-state dollars from financing out-of-state public programs, a consummation devoutly wished by in-state officials. If those state citizens are already playing lotteries in other states, some steam is taken out of the moral argument. For those players the question is not whether they will play, but where they will play.

As a practical matter there is apparently no way to isolate one state from another when it comes to lotteries, despite the requirement of federal law that lottery tickets not be sent by mail. There are many stories of border stores in states with lotteries picking up substantial business from customers with no lottery in their states, and the resulting complaints of the in-state stores.

An example is a story the Des Moines Register ran on September 1, 1984. It featured a picture of a Gulfport, Illinois liquor store with a line of lottery ticket buyers stretching out of sight. Items from the story:

- Their fists bulging with cash, Iowans once again were pouring across the Mississippi River to sin. And some were standing in line the better part of four hours to do it.

- These (Illinois) border towns have not seen anything like this since the days before Gov. Harold Hughes signed a law giving Iowans the right to buy liquor by the drink in their home state.

- An Ottumwa (Iowa) man bought 3,000 tickets, driving the 75 miles to place bets for friends and co-workers.

- Of the hundreds lined up in the store, it was impossible to find an Illinois resident.

- Richter (Iowa resident) said he would love to play an Iowa lottery game and keep his money in his home state rather than taking it to Illinois where it goes for that state's education and public assistance funds.

An Iowa Congressional candidate took his campaign to Illinois, working the ticket lines to explain that he was encouraging the adoption of a lottery in Iowa. Despite a reluctant governor, Iowa has adopted its own lottery.

In addition, there are many ways to play by mail. The obvious, and probably most common way, is to use friends and relatives in lottery states. However, there are other ways which some states promote and some don't. **Reports** got a list of play-by-mail states from a major metropolitan daily and wrote for information. The results both illustrate the ease of play-by-mail and the extent to which lotteries are promoted aggressively.

Maryland offered us the lotto subscription game and reminded us that a West Virginia resident recently won $1.6 million by mail in its lottery. We can pick our own numbers or ask their computer to do the selection as we try to become a "mail-ionaire." Rhode Island sent the kind of form letter one would expect when seeking a copy of a birth certificate — "Enclosed please find the applications that you requested."

Massachusetts did about the same thing. New York's material included a letter explaining the games and the odds, a colorful brochure with instructions on how to play and complete disclosure of procedures and odds, a booklet on how to play by mail, and another booklet showing how to set up to play by mail with a group of players sharing in costs and prizes. Michigan sent an informative fact sheet and a colorful brochure, both disclosing that we have one chance in 3,838,380 of hitting the Lotto jackpot and a 444 out of 445 chance of not getting any prize on an individual play.

The other states didn't respond by press time, perhaps because the Postal Service has accused lottery officials in several states of violating a prohibition against sending such materials across state lines and has asked them to stop.

The opportunity for people in non-lottery states to play by mail is well publicized. For example, Business Week (February 14, 1983) alerted its readers as follows:

> Write to the lottery commission in each state's capital for an application to be returned with your check. If you win, "we have no problem mailing winnings," says a Michigan lottery executive. Some states say they don't mail applications to out-of-state residents. Officials often seem to wink at this stricture, but if your application is denied, simply forward it to a friend to mail within the state so it bears the proper postmark. "It's easy," says an Internal Revenue Service employee who lives in Virginia and plays the Maryland lottery by mail.

While the obvious impact of a new lottery in Iowa would be to cut Illinois revenues by drawing Iowans to purchase tickets in Iowa, the available empirical evidence suggests this may not be true. In "The Lottery as a Source of State Revenue" (Chapter 7 in Center for Tax Policy Studies, Purdue U., Indiana's Revenue Structure), Larry DeBoer concludes from a review of the limited literature that, "The introduction of lotteries in nearby states does not tend to reduce sales, and may increase them to a small extent."

LOTTERY DESIGN AND ADMINISTRATION

Advertising and Sales: The subject of how much and how to advertise gets considerable attention in lottery administration because of sensitivity to using state government to promote gambling.

One point of view is simply to treat the lottery as a business seeking to maximize profits. This typically is the view of the lottery directors. For example, Pennsylvania's director told the Sacramento Bee: "My charge is to maximize our profits." To do this, a lottery would advertise when the incremental revenues from doing so exceed the incremental costs of advertising.

If this view is accepted and the competence of lottery officials assumed, neither legislatures nor state constitutions should specify anything about advertising. However, two of the new lotteries adopted in November go a different route. The Missouri amendment says, "At no time shall the Missouri state lottery be advertised in a manner designed to induce persons to participate in the Missouri state lottery." It is difficult to imagine a reason for advertising other than this, so the Massachusetts lottery director advised the Missouri legislative committee considering implementing legislation that "it is going to be tough" for Missouri to run a successful lottery. In California, the amendment requires that 3.5% of projected gross sales be used for promotion in the first year, more than many states spend.

Prizes as a Percentage of Amounts Bet: A key question in designing a lottery is deciding what percentage of money bet should be returned as prizes to maximize net state revenues. If states return all money but administrative costs, they presumably would encourage the maximum amount of betting but get zero revenues. On the other hand, if only token prizes were given, few would play. State policies on this matter vary considerably.

Jon Vasche analyzed the subject in an article in the Journal of Policy Analysis and Management (Volume 4, No. 2) by looking at what caused different levels of betting in different states. He considered seven possible factors affecting how much is bet — per capita income, the number of years the lottery had been in existence, whether the proceeds are earmarked, "whether a state has a history of administrative problems or corruption in the management of its lotteries," state unemployment rates, the availability of alternative types of legal wagering, and the percentage of bets paid off as prizes. Interestingly enough he found the first six all had value in explaining how much was bet in each state, but the prize-wager relationship didn't. However, these results were based on a small group of states that then had lotteries and the relatively small variation in state take and wouldn't necessarily be valid for takes outside that range.

Table 10 shows the state shares of total amounts bet. These numbers are set by two factors: (1) the policy decision on the percentage split between the state and the prizes and (2) administrative costs.

Table 10: Revenue to States as Percent of Total Lottery Sales
FY 1984

State	Percentage	State	Percentage
New York	43.9	Illinois	41.4
Washington	43.1	Michigan	40.3
Maryland	43.1	Rhode Island	34.8
New Jersey	42.4	Colorado	33.9
Delaware	42.4	Massachusetts	33.4
Pennsylvania	41.8	New Hampshire	30.5
Ohio	41.5	Arizona	30.0
Connecticut	41.4	Maine	28.1
		Vermont	25.5

Independent Boards or State Line Agencies: The states have adopted a variety of administrative arrangements for running their lotteries. In Delaware, Michigan, and New York, lotteries are managed by single heads; in the other lottery states, boards or commissions are used. The usual arguments apply. Use of a single accountable person is argued to promote responsiveness and accountability and to make it possible for the relevant department head and governor to be held unambiguously accountable. Use of a board or commission is said to insulate the activity from politics and promote public confidence in lottery operation.

The question of whether to use a board or commission is partly isolated from the question of where to place the lottery agency administratively. Lottery agencies are in the tax-collecting agency in Colorado, Connecticut, Delaware, Illinois, New Jersey, New York, and Pennsylvania, but independent agencies elsewhere.

The Lottery Games: New forms of lottery games are constantly being invented, but there are a few basic forms. The **instant** lottery provides a card with a covering that is scratched off to reveal the prize, if any, that is won. The payoffs are typically small, but winners may be put in a pool for large prizes. The **numbers** is simply the private sector numbers game, where each player picks three or four digits prior to a winning number being selected at random. **Lotto** involves trying to select a winning group of numbers out of a larger group.

The newest form of lottery game is designed to capitalize on the attractions of video games and slot machines. It features instant payoffs and gives the customer something active to do. The machines are called video-lottery terminals or player-activated lottery machines. Illinois has been trying some on an experimental basis.

Dedication of Revenues: The proceeds of some lotteries are dedicated to particular purposes because proponents believed in the purpose and often because they believed that earmarking would help to sell tickets, and/or help to sell voters on the lottery. According to a phone survey by the Texas Comptroller, New Hampshire, New York, Ohio, and Michigan earmark proceeds for education. New Jersey earmarks proceeds for a combination of state institutions and education. Pennsylvania lottery revenues go to the aged. Massachusetts distributes $3 million to the arts and the rest to local government. Colorado puts half into capital outlays, 40% to a conservation trust fund, and 10% to parks and recreation. Oregon's new lottery is being used to fund economic development programs such as capitalizing a business loan fund. Other states simply put the money in their general funds.

As is the case with any earmarking or dedication of a state receipt, it is highly likely that the earmarking will, sooner or later, distort priorities gauged against what the persons then in office would do with money. This happens except when the earmarked money is less than the total that state decisionmakers would spend anyway, in which case the earmarking is meaningless. Resource allocation distortions are caused by earmarking because, over time, the needs for which funds are earmarked change, and the revenues change, not necessarily in lock step with each other. Pennsylvania has encountered this situation with a lottery that is very profitable, but with earmarking to the elderly and handicapped. One result has been to trigger consideration of policies that probably wouldn't be adopted in a climate without earmarking. An example is splitting a service — such as providing alcoholism clinics for the elderly rather than serving them in regular clinics.

This earmarking problem goes away when lottery proceeds are devoted to something where they would be swamped by regular general fund appropriations in an inflationary world. For example, the new California lottery will provide funds for education and has safeguards to prevent corresponding cuts in state appropriations.

However, there is no practical way to prevent state officials from considering lottery proceeds when deciding on how much to increase education spending in the future.

The advice of Steven Gold, the National Conference of State Legislature's expert on the subject, is:

> Politically, if you want to get a lottery adopted, if you do earmark, it may give you a potential lobbying ally. But if the states engage in too much earmarking, they can hamstring the budgetary process. If you don't have a particular axe to grind, it's best to let the legislature decide each year.

ENFORCING LAWS AGAINST ILLEGAL LOTTERIES

The classic form of an illegal lottery is a numbers game. In this game, the players pick a sequence of digits, usually three. The payoff occurs when that sequence is chosen as the winning number. There are many variations, such as four digits with big payoffs for all four and lower payoffs for three in sequence. Bets are sold by retailers (runners) who may be small business people taking bets on the side or people working the streets in regular rounds. Bets are taken to "banks" which pay off through the runners. A random method not under control of the banks is used to designate the winning numbers, such as the last digits of the daily volume on the New York Stock Exchange, the total amount bet at a track, or the number selected in some state lottery.

In states with legal lotteries, there is an economic interest in state government in stamping out the competition of illegal ones. But this interest lies in state officials, while local officials are responsible for enforcement of anti-gaming laws. As a practical matter, state officials do not campaign against their illegal competitors by trying to put them out of business through local law enforcement. The law enforcers are in a difficult position because all the numbers players, runners, and bankers are doing is competing with the state illegally. Law enforcement officers are likely to get about as much sympathy as federal officials do when they threaten prosecution of persons competing with the post office — an economic crime may be involved, but it's hard to argue there is a moral one.

In states without legal lotteries, this problem does not exist, but enforcement is not easy. There is so much legal gambling and so much public acceptance of betting that there is a tendency for police, prosecutors, and judges not to pay much attention to cracking down on numbers. There is no way to prove this, but the treatment of a group of arrests by the Charlotte Observer (December 17, 1984) gives some idea of the climate of opinion even in the Carolinas, where one would expect less tolerance of gambling than most states because of the absence of legalized gambling.

Charlotte police rounded up 26 people. Two were described as the lottery owners and were, among other things, charged with a serious crime (attempted bribery of public officials). The Observer left their case alone but played the cases of the "middle managers" who were also arrested. Several were willing to be interviewed. One took bets out of his home, making about $300 a week, and said he planned to stay with numbers the rest of his life. On getting arrested he said, "If you're doing something illegal you have to expect it." Another, "like many of those arrested," is retired. He didn't think he should have been arrested as he was just trying to make a living and stay off welfare. The story portrayed numbers as "an institution in some Charlotte communities." Some balance was provided to the story by the police chief who argued that the lotteries generate untaxed dollars, exploit poor people, encourage other illegal activity, and open the door to national organized crime. However, the chief said that it was impossible to eradicate numbers. The middle managers were all promptly released on bonds of less than $1,000.

While **Reports** has no interest in the fate of this case, we cannot imagine that the Charlotte police are going to place a high priority on eradicating numbers so long as they are given this treatment in the local press and courts.

The situation is even more difficult when illegal lotteries have proceeds designated for charity. Last year, the Zachary Scott Theatre in Austin Texas sold over a thousand chances, at $100 a chance, to win a new Porsche — a clear violation of Texas law. The local district attorney attempted to prosecute, which in Texas begins by an indictment by a grand jury chosen from the community. The grand jury refused to indict, stopping the prosecution in its tracks. The grand jury did accede to a statement that people doing such things in the future face prosecution. The local lawyer who was chairman of the theatre's board of directors said (Austin American Statesman, October 20, 1984):

> I assure you we really weren't trying to run afoul of the law. We were just trying to institute what we saw as an innovative way to raise funds because, quite frankly, there are a lot of people soliciting for organizations, especially arts organizations.

A major study of the enforcement of gambling laws (F. Fowler and others, Gambling Law Enforcement in Major American Cities, GPO, 1977), concluded that the laws were largely unenforceable.

A FEDERAL LOTTERY?

One of the risks of high reliance on lottery revenues is the possibility of new competition from the federal government. It can be (and has been) argued that a national lottery would make the lottery concept more popular and would therefore increase the popularity of the state lotteries as well. However, the conventional wisdom is that a national game would cut into the popularity of state games. This is the view taken by the North American Association of State Lotteries, the organization of state officials who run lotteries. A national lottery would certainly gain more attention as it could have truly prodigious payoffs compared with state lotteries.

At least four bills to create a national lottery have been introduced in the Congress. The usual rationale is that a lottery would provide a painless way to reduce the nation's budget deficits.

FOR MORE INFORMATION

The most useful single source of information on lotteries is published hearings (State Lotteries: An Overview) of the Subcommittee on Intergovernmental Relations of the U.S. Senate Committee on Governmental Affairs. This is a 627-page document consisting of the transcript of a day of hearings last October plus many materials provided for the record. It includes a variety of articles and studies.

The Public Gaming Research Institute (51 Monroe St., #1500, Rockville MD 20850) publishes the Lottery Journal and other materials generally supportive of lotteries. Scientific Games, Inc. (135 Technology Parkway, Norcross GA 30092) is also a good source of pro-lottery materials. Anti-lottery forces (e.g., religious groups and those involved in other forms of legalized gambling) are not prolific producers of materials. This article in **Reports** is about as complete a collection of anti-lottery arguments as readers are likely to find.

For a review of the history of lotteries, try Stephen Thomas and Deal Webb, "The Use and Abuse of Lotteries As a Revenue Source," Journal of Education Finance, Winter 1984. There are a variety of publications that cater to lottery players, such as Lottery Players Magazine. The definitive work on gambling and government is the report of the U.S. Commission on the Review of the National Policy Toward Gambling (1976), Gambling in America.

STATE AND LOCAL GOVERNMENT IN THE CLASSROOM

Public Policy and Federalism (St. Martin's Press, 1985) by George Washington University political scientist Jeffrey Henig is a new state and local government textbook. It is reviewed here to give readers an impression of what is being said about state policies in the classrooms.

One conclusion is obvious from the first page of the preface — welfare mothers may know more than some college professors. Henig talks about welfare mothers picketing city hall. What welfare mothers know is that welfare policies and administration are controlled by states and welfare is administered by state officials in some states and county, not city, officials in others. City officials administer welfare only when the city happens to have state functions (the District of Columbia) or county ones (e.g., New York).

Chapter 1 begins on a less-than-positive note:

> A tour of state legislatures and city councils can take one from the ridiculous to the absurd. Consider the Illinois legislature in the summer of 1981, for example. One legislator, calling the presiding officer a "son of a bitch," threw aside his chair and stormed the front, apparently intent upon making his point with a physical flourish. Another legislator slowed him down with a punch.

While finding that the federal government has increased its role since 1789, Henig comments:

> ... this does not mean that states and localities have become insignificant actors. They are not simply water boys for the government in Washington, D.C. Broad policy shifts and dramatic pronouncements emanate from the White House, the Congress, and the Supreme Court. But these often have more to do with policy-in-theory than with policy-as-fact. For although the

TABLE 75--A COMPARISON OF STATE LOTTERY REVENUES--FY 1980-1983
(Amounts in millions of dollars, unless otherwise indicated)

State	Started	Gross Revenue 80	81	82	83	Prizes 80	81	82	83
U.S. Total		$2107.4	$2713.0	$3532.1	$4761.7	$919.8	$1420.6	$1842.3	$2480.8
Arizona	July 1981	N/A	N/A	$114.1	$74.9	N/A	N/A	$51.4	$36.4
Colorado	Jan. 1983	N/A	N/A	N/A	128.7	N/A	N/A	N/A	70.5
Connecticut	Feb. 1982	129.9	141.8	159.7	178.0	65.3	78.0	87.9	93.8
Delaware	Nov. 1975	15.9	19.1	23.5	27.6	8.1	10.1	13.3	15.6
Illinois	July 1974	91.0	197.5	310.5	461.5	45.8	100.5	158.0	231.4
Maine	June 1974	6.0	5.7	9.7	13.1	2.8	3.1	4.7	6.4
Maryland	May 1973	372.3	366.4	434.1	444.0	174.3	182.7	211.0	227.4
Mass.	March 1972	192.5	184.8	210.0	261.9	90.5	104.2	121.2	155.0
Michigan	Nov. 1972	487.9	463.6	483.1	512.8	241.0	253.2	270.2	269.5
N.H.	March 1964	9.0	11.2	13.3	14.5	3.4	5.5	5.9	6.7
New Jersey	Jan. 1971	331.9	396.2	480.8	654.3	173.8	208.1	258.4	340.3
New York	1967-1975 Sept. 1976	182.8	219.4	386.9	578.5	72.8	101.3	191.0	284.6
Ohio	Aug. 1974	57.2	280.2	345.3	377.8	10.3	150.2	174.6	204.1
Pennsylvania	March 1972	194.7	393.6	523.8	825.0	15.7	205.5	274.1	439.9
Rhode Island	May 1974	33.4	31.2	33.8	38.5	14.7	17.0	18.7	22.0
Vermont	Feb. 1978	2.9	2.3	3.5	3.8	1.3	1.2	1.9	2.1
Washington	Nov. 1982	N/A	N/A	N/A	166.8	N/A	N/A	N/A	75.1

State	Administration 80	81	82	83	Net Proceeds 80	81	82	83
U.S. Total	$130.3	$132.5	$163.5	$255.1	$1057.4	$1159.9	$1526.1	$2026.2
Arizona	N/A	N/A	$16.8	$15.4	N/A	N/A	$45.9	$23.1
Colorado	N/A	N/A	N/A	11.2	N/A	N/A	N/A	47.0
Connecticut	$3.9	$8.3	9.3	10.4	$60.8	$55.5	62.5	73.8
Delaware	1.5	1.4	1.7	2.0	6.3	7.7	8.5	10.0
Illinois	9.5	10.0	10.9	15.2	35.8	87.0	141.5	214.9
Maine	2.5	1.5	2.5	2.9	0.7	1.1	2.4	3.8
Maryland	12.6	12.4	14.8	18.4	185.4	171.4	208.3	198.2
Mass.	9.4	15.7	19.4	22.6	92.5	64.8	69.4	84.3
Michigan	10.9	13.6	14.6	28.6	236.0	196.8	198.3	214.7
N.H.	1.9	1.8	2.1	2.2	3.7	3.9	5.3	5.7
New Jersey	15.7	6.7	7.4	18.6	142.4	181.4	214.9	295.4
New York	26.7	21.0	16.8	25.2	83.3	97.0	179.0	268.8
Ohio	11.2	17.8	21.1	27.2	35.7	112.2	149.6	146.5
Pennsylvania	21.0	19.3	23.1	30.3	158.0	168.8	226.7	354.8
Rhode Island	2.1	2.4	2.3	2.1	16.6	11.8	12.8	14.4
Vermont	1.4	0.6	.7	.7	0.2	0.5	1.0	1.1
Washington	N/A	N/A	N/A	22.1	N/A	N/A	N/A	69.7

State	Annual Percent Increase in Gross Revenue 81	82	83	Net Proceeds as a % of Total State Own Source General Revenue 80	81	82	83	Annual Bet Per Capita 80	81	82	83
Arizona	N/A	N/A	52.3%	N/A	N/A	N/A	.9%	N/A	N/A	$39.45	$25.28
Colorado	N/A	N/A	N/A	N/A	N/A	N/A	1.9	N/A	N/A	N/A	41.00
Connecticut	9.1%	12.6%	11.5	2.6%	2.1%	2.1%	2.2	$41.80	$45.21	51.09	56.72
Delaware	19.9	23.0	17.4	0.9	1.0	1.0	1.1	26.79	32.02	39.17	45.54
Illinois	117.0	57.2	48.6	0.4	1.0	1.0	2.4	7.97	17.26	27.08	40.18
Maine	-5.0	70.7	35.1	*	0.1	0.3	0.4	5.36	5.00	8.54	11.43
Maryland	-1.6	18.6	2.8	5.1	4.4	4.9	4.3	88.32	86.04	101.66	103.16
Mass.	-4.0	13.6	24.7	2.0	1.3	1.2	1.3	33.55	32.00	36.52	45.41
Michigan	-5.0	4.2	6.1	3.2	2.5	2.4	2.4	52.70	50.31	52.99	56.54
N.H.	25.5	18.4	.9	0.9	0.9	1.0	1.0	9.72	11.99	15.30	15.12
New Jersey	19.4	21.3	36.1	2.7	2.9	3.0	3.7	45.07	53.40	64.74	87.61
New York	20.0	76.4	14.5	0.6	0.6	1.0	1.4	10.41	12.47	22.02	32.74
Ohio	390.0	23.2	9.4	0.6	1.7	2.0	1.7	5.30	25.96	32.06	35.16
Pennsylvania	102.2	33.1	57.5	1.9	1.9	2.4	3.5	16.40	33.14	44.09	69.36
Rhode Island	-6.6	8.3	13.9	2.0	1.3	1.2	1.2	35.24	32.70	35.47	40.31
Vermont	20.7	52.7	8.6	*	0.1	0.2	0.2	5.58	4.51	6.73	7.24
Washington	0.0	N/A	N/A	N/A	N/A	N/A	1.4	N/A	N/A	N/A	38.79

*Percent less than one-tenth.

Source: ACIR staff compilations based on Bureau of the Census, State Government Finances in 1980, 1981, 1982, 1983.

U.S. Advisory Commission on Intergovernmental Relations

From Significant Features of Fiscal Federalism, 1984 Edition, ACIR 3/85 seed costs back within 30 days–while others simply waited until the end of the fiscal year. Lottery directors in states that waited to pay are quick to point out that their lotteries had the capacity to pay back within a few months, but waited for bookkeeping reasons. But when considering the lotteries as a whole, average payback time is 6.7 months.

LOTTERY STARTUPS: HOW MUCH; HOW LONG?

State	Startup Time	Seed Money	State Repaid
Arizona	7months	$1,400,000	12 months
Colorado	8 months	$2,000,000	2 months
Connecticut	7 months	$2,150,000	10 months
Delaware	7 months	$ 250,000	18 months
D.C.	17 months	$ 628,000	1 month
Illinois	9 months	$2,000,000	1 month
Maine	7 months	$ 400,000	12 months
Maryland	6 months	$2,300,000	1.5 months
Massachusetts	6 months	$2,000,000	3 months
Michigan	3 months	$4,400,000	6 months
New Hampshire	11 months*	$ .250,000	2 months
New Jersey	12 months	$1,500,000	12 months
New York	5 months	Not avail.	Not avail.
Ohio	14 months	$2,000,000	4 months
Pennsylvania	6 months	$1,000,000	10 months
Rhode Island	1.7 months	$ 500,000	2 months
Vermont	10 months	$ 250,000	12 months
Washington	4 months	$1,500,000	5 months
Average	7.8 months	$1,400,000	6.7 months

**The nation's first lottery was delayed waiting for a public vote after legislative approval.*

Source: Interviews with state lottery officials.

Legislation: The First Step

For new lottery states West Virginia and Missouri, the time was obviously right for the introduction of legislation to legalize lotteries, and the pro-lottery arguments in the floor debate were solid enough for passage. Legislators contemplating lotteries in other states can now study the cases of West Virginia and Missouri as examples of successful lottery campaigns utilizing the legislative avenue.

West Virginia

For years, West Virginia lawmakers supporting a lottery have sat and watched neighboring Pennsylvania, Ohio and Maryland reap huge profits from their state-supported betting. At the same time, the lottery proponents could see the potential of tapping markets in their bordering non-lottery states–Virginia, Kentucky and Tennessee–as well as the state's own 2 million residents, who per-capita projections indicate will spend approximately $140 million per year on a lottery (see "Lottery Revenues Continue to Climb," LJ, Oct. 1984).

According to State Senator J. Robert Rogers, who sponsored the resolution to amend West Virginia's constitution to allow a lottery, lottery legislation had been introduced for a number of years prior to its passage. Rogers said the measure had consistently passed the House, but was never taken up for consideration in the Senate because the leadership was opposed to lotteries.

Rogers said he decided the time was right to sponsor the legislation when the Senate leadership changed. When he felt the largest hurdle had been cleared–obtaining the required two-thirds vote in the Senate for passage of a constitutional amendment–the measure failed passage in the House by one vote in 1982. But in 1983, the measure passed both houses, placing the question on November's ballot. The voters approved the amendment by nearly a 2-1 margin.

Legislation to enact the lottery, including how the lottery income will be distributed, still needs to pass the legislature in West Virginia, a process Rogers says he hopes to speed up by requesting funding for a subcommittee to meet before February 1985 to draft the bill.

Missouri

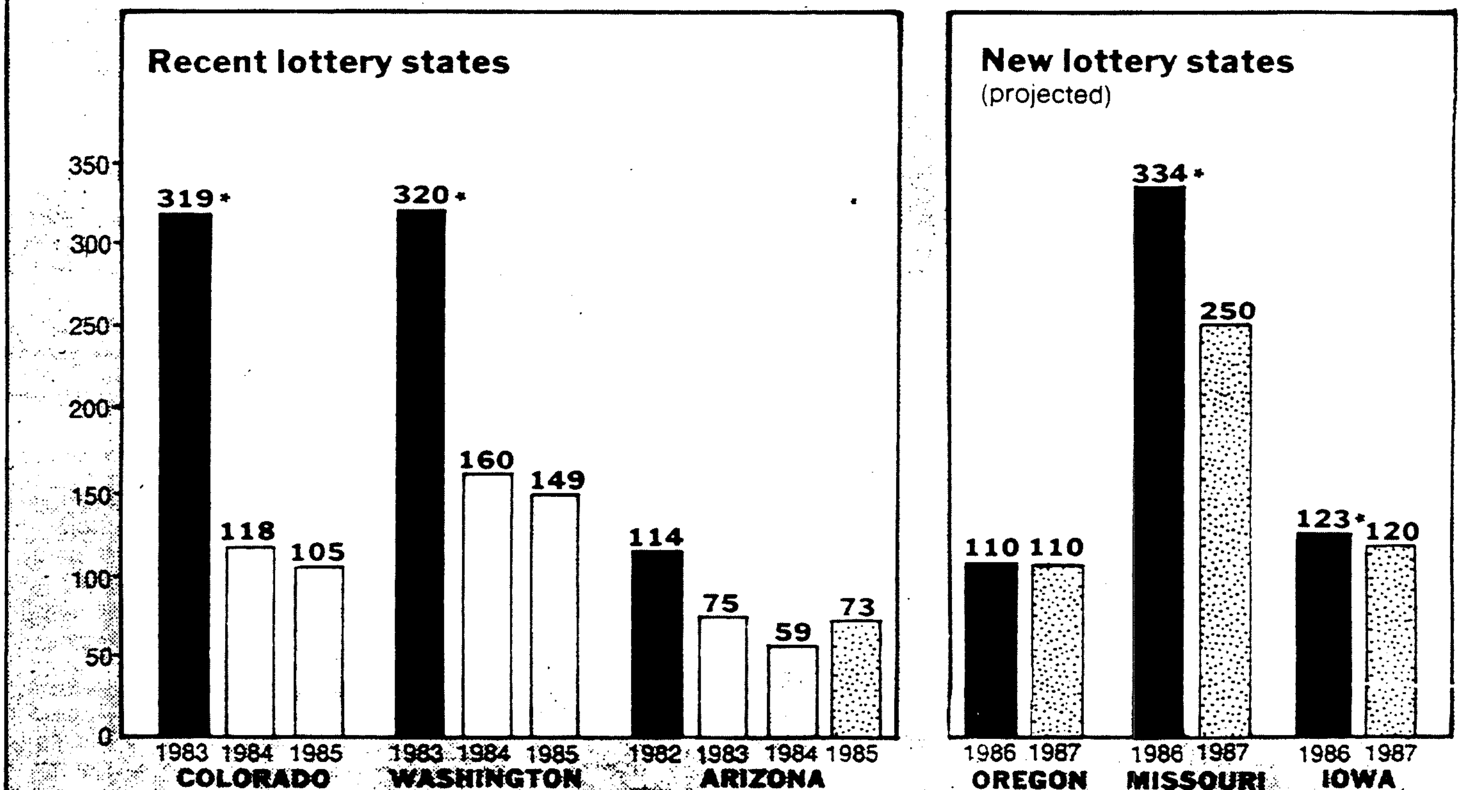
As with West Virginia, Missouri lawmakers witnessed a bordering state benefiting from an enormously successful lottery. Neighboring Illinois was setting records for sales transaction rates with its lotto jackpots, and a significant amount of the revenue was coming from its neighboring states without lotteries, including Missouri.

According to State Senator Edwin L. Dirck, who sponsored the measure to amend Missouri's constitution to permit a lottery and will sponsor the enabling

Jan 85

RISING EXPECTATIONS

Gross revenues of states that have started lotteries since 1981 (In millions of dollars)



*First-year revenues are annualized figures based on partial-year sales.

Star ch

KC STAR 12-27-85

B

STATE LOTTERY OVERVIEW

Presentation Before The
House Committee on Federal and State Affairs
by the Kansas Department of Revenue

January 16, 1986

H. F+SA
1/16/86

Attachment B

INTRODUCTION

Kansas is one of many states facing the issue of whether to adopt a public lottery in 1986. Lotteries now exist, or are undergoing start up in 22 states and the District of Columbia. 1985 was a year of tremendous growth and expansion in the lottery industry with 5 new lottery states: California, Iowa, Missouri, Oregon, and West Virginia. National sales figures for FY 1985 are estimated at $9.3 billion compared to $8.1 billion in calendar year 1984.

Last November, the Department of Revenue established a Lottery Project Team to research the mechanics of a state lottery organization. The team has been collecting information from various lottery states, is becoming familiar with the industry, and visited the Iowa Lottery in December. What I would like to briefly share with you today are the results of this effort in the areas of lottery game design, functions a state agency must perform, allocation of lottery revenues, the enabling legislation, and start-up reference dates.

GAME DESIGN

Lottery games can be divided into two categories, active and passive. Active games are those in which the player participates in the bet by choosing a number or set of numbers. Passive games are those in which the player takes no action to determine whether he has won or lost;instead a ticket is purchased and the outcome is then revealed.

There are currently several types of lottery products being played. The first is what is commonly referred to as the "weekly game" or draw lottery. Though rare in the United States, this is the game which was used when the modern lottery first started in 1964 in New Hampshire and remains the main game in overseas lotteries. Similar to a raffle ticket in appearance and in play, the player purchases a pre-numbered ticket and waits for a weekly drawing.

The second type of lottery product is the <u>instant lottery ticket.</u> The instant ticket has play data which is concealed by a removable latex material. A player buys the ticket, usually for $1, and scrapes off the material to reveal whether or not it is a winner. With the Iowa instant ticket you have before you, the game has a match three theme; match three dollar figures and you win that amount as a prize. In addition, states have introduced jackpot prize drawings which use the instant ticket as a method to gain entry. Using Iowa again, $100 instant winners are entered in the weekly drawing and if selected can "spin the wheel" for prizes such as $5,000, $10,000, $25,000, or the jackpot which increases each week if not won. In addition, one individual per week can go to the wheel to spin for a player who has submitted five losing tickets by mail. This player is selected by random drawing. The weekly drawing and "spin the wheel" is generally a televised event.

The third type lottery product is the "online system". This was introduced in the mid 1970s. The online system is a series of computer terminals which are similar to cash registers in appearance and are geographically located throughout a state. The terminals are linked by phonelines to a central computer site, usually in the state capital. There are currently three online games. The first online game to be introduced was the three-digit game, commonly referred to as the "numbers game". Numbers games were originally designed to compete directly with Eastern illegal numbers games. A player approaches the agent who has a terminal and selects three digits. The agent enters those three digits at the terminal and the play is recorded at the central site. Every day there is a random drawing of a number and matching that number in prescribed ways wins prescribed prizes. The second game is the pick four or four-digit game, which is basically run the same way as pick three.

The third on-line game is the increasingly popular lotto game. A player picks six numbers out of a specified field of numbers, such as 36, 40, or 44. A certain percentage of the revenues is placed in a grand prize fund which is only paid when an exact match of the six digit numbers is made. Drawings of the winning numbers are held once or twice a week and if there is no winner, the jackpot "rolls over" to the next drawing. If no one wins for several weeks, the jackpot can become enormous, as evidenced by New York's $41 million lotto jackpot. Most lotto games also include lesser prizes for matching four or five out of six numbers, for instance.

START-UP

New lottery states have started with instant games. State lottery directors testify that to ensure successful and timely start-up, instant games have proven to be the most efficient direction to take. Vendors in the on-line business promote starting with a lotto game, since this particular type of game represents over two-thirds of all lottery sales in mature states. Whereas instant games commonly start off strong and then gradually decline, online games start slowly but increase at a rate that quickly surpasses instant game sales; part of "lottomania". This is particularly true when the prize money begins to "roll over" several times.

Both approaches should be examined carefully, since the goal should be not to simply copy what other states have done, but to establish a lottery that reflects the needs and desires of the citizens of the State of Kansas. It is likely, however, that we would begin with an instant game (s) but should be prepared to move to an on-line game within 9 to 18 months. In part, this is necessary to educate the public.

If a lottery resolution is passed by this Session of the Legislature and approved by the voters in November, it is possible that ticket sales could begin on or before July 1, 1987. This is, however, contingent on three factors: (a) lottery enabling legislation must also be passed this session; (b) a core staff group must be available from April to November to work on such matters as developing requests for proposals for start-up consultation services, planning the administrative organization and procedures, and developing Requests for Purchases for lottery games and services; and (c) appropriations must be made so that staffing and implementation can proceed immediately upon voter ratification.

ALLOCATION OF LOTTERY REVENUE

Lottery revenues are divided into three categories: operating expenses, prize payments, and net proceeds. Operating expenses include commissions to retailers (usually 5-6%), and actual administrative costs such as ticket production, consulting services from private lottery firms, advertising, computer services, salaries, and other support services. These costs will vary with size and maturity but commonly run 10 to 15%. After deducting operating costs, and prize payouts

(45-50%), the remaining portion (30-40%) represents the net proceeds to the state.

FUNCTIONS A STATE AGENCY MUST PERFORM

Most state lotteries are operated in generally the same way with day-to-day administration resting with a Lottery Director. Major units within the organization include Security, Aministration, and Marketing, as shown on the attached sample organization chart. Lottery staffs can range in size from Iowa at 125 to California's with over 500.

ENABLING LEGISLATION

Although you will first hear testimony on Senate Concurrent Resolution 1609, it is our recommendation that if approved, the 1986 legislature should also consider the enabling legislation which would allow the lottery to begin the start-up process immediately after the November vote, if favorable. Such action would avoid a potential one year loss of lottery revenue through delayed implementation.

A lottery is a unique entity in state government, in that it is the only state agency with a mission identical to a private business-selling a product in a fashion which maximizes revenue. In drafting the enabling legislation, three key ideas need to be addressed in the operation of a lottery: flexibility, integrity, and security. Fortunately, we can learn from the mistakes made by established lottery states in molding our legislation.

Specific issues and potential problem areas that will need to be examined are:

1. Location of the lottery operation. Although most states have a lottery commission to advise and govern lottery activities, they differ as to the lottery being a part of a state Department of Revenue or a separate state agency. Regardless of where it is located, it must have its own identity and be clearly responsible for its decisions, both from an efficiency and public relations standpoint.

2. The lottery must be provided with the authority to enter into contracts within established state procedures its own bid specifications must be provided. Additionally, would strongly advise that the lottery be allowed to use a negotiating procedure for entering into contracts with vendors (much as is done for architectural or engineering services) rather than being required to accept only the lowest bid.

3. Since it is a business, all normally acceptable business policies dealing with the presentation of the games, advertising, promotion, accounts receivable, accounts payable, bonding, personnel employment, agent incentives, budget flexibility, etc. should be accomplished without the handicap of time approval restraints. In particular, limits on advertising and

promotion must be avoided if you wish the lottery to be successful.

4. References to specific expenditure percentages for prizes, expenses, advertising, and commissions should be avoided to allow flexibility and not create needless constraints on management decisions.

5. Security and integrity of operation requires that the lottery have an independent fault- tolerant computer system that is not under a central computer service agency. None of the lottery states share computer facilities or equipment with other state operations.

6. Specific references to types of games to be played should be avoided to allow lottery management the opportunity to make strategic marketing decisions that will cause lottery revenues to be constant and hopefully increase as new techniques become available.

7. Specific dates for the implementation of certain games and for repayment of "seed money" should also be avoided.

8. Questions regarding the taxability of lottery transactions--i.e., sale tax on ticket purchases and withholding requirements on winnings--will need to be answered. (High tier winnings are subject to a 20% federal tax off the top.)

In reviewing percentages of the lottery states, administrative expenses of the smaller states are well above the national average, and the costs of the larger states fall well below the average. There appears to be evidence of economies of scale, especially in advertising and computer expenses. Therefore, it is inappropriate to take at face value, the administrative costs of a large, mature lottery such as New Jersey and New York and compare that to a new lottery state.

In 1985, in the nine lotteries with less than $200 million in gross sales, net proceeds amounted to less than 40% and in six cases the net was less than 35%.

We are not prepared at this point to present a definitive plan to administer and operate a lottery in Kansas. We intend, however, over the course of the next two to four weeks, to prepare a recommended approach with costs.

Glossary

active game: a lottery game in which the player takes action to determine the outcome by choosing a number or set of numbers to bet on, attempting to match the numbers later drawn.

agents (sales, ticket): retail merchants chosen by the lotteries to sell tickets, using either a computerized ticket generator (for on-line games) or a ticket supply furnished by a vendor (for instant games).

annuity: a type of insurance policy purchased by lotteries that pays off a large jackpot to the winner in equal installments, which allows the balance to accumulate interest over time, thereby permitting the lottery to offer a prize larger than the policy cost.

audit features: an accounting system built into video lottery terminals that logs all sales transactions and cash received.

back pair: a betting feature used in three-digit and four-digit numbers games that allows the player to bet on what the final two digits in the number drawn will be.

box bet: a betting feature in numbers games allowing the player to bet on all possible combinations of three or four digits.

central site computer: a computer in one location that controls ticket-producing terminals or video lottery games at various locations around a state.

dial-up: a system of communications between video lottery terminals and a central site computer that permits the sending of electronic messages over telephone lines.

downloading: the transfer of a store of plays from a central computer to a video lottery terminal.

draw lottery (also "traditional lottery" and "weekly game"): a lottery game similar to a raffle, involving the sale of pre-numbered tickets, with the winners chosen at random in a weekly drawing.

electronic survey: a computerized demographic questionnaire built into video lottery terminals that awards a free play for answering questions regarding age, education, income level, etc.

fixed payout: a prize that remains set at the same odds regardless of how much money is bet for a particular drawing.

front pair: a betting feature used in three-digit and four-digit numbers games that allows the player to bet on what the first two digits in the number drawn will be.

game format: the individual games offered on the computer software used with video lottery terminals.

game mix: the complete collection of games offered by a state lottery.

instant game (also "instant lottery"): a lottery game that offers pre-printed tickets, normally selling for $1 each, that indicate immediately whether or not the player has won.

line of credit: money lent a lottery bureau by the state's legislature for use in initiating operations.

lotto (also "Pick 6"): a lottery game originated in Europe that offers the player a choice of four, five or six numbers out of a field ranging from 30 to 49 numbers, the winner being determined by a drawing.

lotto boards: the betting slips used in lotto games.

mini-pool: the store of plays in a video lottery terminal, which is replenished via telephone line from a central computer.

numbers games (also "Pick 3" and "Pick 4"): lottery games permitting the player to choose his or her own three-digit or four-digit number, the winner being determined by a drawing.

on-line: hooked up to a central computer via telecommunications lines, as with ticket-generating terminals used in numbers and lotto games.

P.A.L.M.: Player-Activated Lottery Machine–the stand-alone terminals used in video lottery games.

parimutuel: a system of prize payouts in which the jackpot is created solely with money wagered.

parimutuel industry: term used to describe all legalized wagering that involves prizes created on a parimutuel basis, including horse racing, dog racing, and off-track betting parlors.

passive game: a lottery game in which the player takes no active part in determining the outcome; the ticket sold is either a winner or a loser, and no choices of numbers are made.

payback schedule (or payback time): the time it takes a lottery bureau to repay the state legislature money appropriated to initiate operations.

payout (or "payoff"): the amount of a prize or the odds by which a prize is paid.

pool: the cash amount in a parimutuel jackpot, or the total money wagered.

pool size: the amount of cash one would need to purchase all possible combinations of numbers in a lotto game.

Glossary

prize tiers: various levels of prizes in lotto and instant lottery games–lower tier prizes are normally paid out by lottery agents at retail locations.

"Quick Pick": betting feature for lotto games consisting of a machine that electronically selects random numbers for a player.

rollover: the situation where money in a lotto jackpot is carried over to two or more drawings when no one wins the grand prize.

rub-off: type of instant lottery ticket with a latex spot which, when removed, reveals whether or not the ticket is a winner.

seed money (also seed cost): the amount of money appropriated a lottery by a state's legislature for the purpose of initiating operations.

6/40: a term describing the choices offered in a lotto game; 6/40 means a choice of six numbers from a field ranging from 1 to 40 (same formula applies for 6/36 and other such terms).

spillover sales: lottery sales made to residents of a bordering non-lottery state.

straight bet: betting method used in numbers games that requires an exact match of the number drawn to win.

subscription game: a lottery game for which tickets are purchased in advance, entering the participant in a series of drawings lasting a specific time.

"System Betting": a betting method used in lotto games that involves choosing eight numbers, and having the computer record bets for all possible combinations of those numbers.

telecommunications: the linking of a main computer with lottery terminals around a state for the transmitting of information and programs, via telephone lines.

transaction rates: the amount of transactions recorded by one or more of the lottery terminals in a state during a specific time frame.

video lottery: a lottery game involving a stand-alone machine designed similar to a video amusement game, but with prizes offered for winning (at random) by the state lottery.

SAMPLE LOTTERY AGENCY