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Casinos no cure-all for state budgets, economists say

Many States with casinos find they're not a budgetary cure-all

By John Cheves

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FRANKFORT — Faced with another round of state budget cuts, Gov. Steve Beshear promotes casino gambling as a way "to improve our revenues long-term" in Kentucky.

But the nearly two dozen states that get revenue from casinos have struggled financially during the past three years, just like everyone else, according to a Lexington Herald-Leader analysis.

All of them cut spending; half raised taxes. Some fired thousands of their public workers, including educators and police, and gutted their basic classroom funding.

Experts who study gambling's economic impact said Kentucky should be realistic about what it could win. Casinos are a poor substitute for a strong, stable tax base, they said.

"Casinos will almost certainly increase your revenue to some extent. But there will be offsets and costs that you also need to consider," said Alan Mallach, a visiting scholar at the Federal Reserve Bank in Philadelphia.

Among their concerns, experts said, casinos cannibalize other forms of spending from which the states take a cut, from lottery tickets to gas and consumer goods. That cancels out some of the casino states' financial gain.

"Casino gambling does not create a single new dollar. Every dollar dropped into a slot machine is a dollar not spent on something else," Mallach said. "It's not like you've got an auto plant and you're building cars to be shipped and sold around the world."

Florida, for example, has what some Kentuckians want: "racinos," or casino gambling at racetracks. Florida collected $141 million in casino tax revenue in 2010 and earmarked it for education. Yet it's slashing K-12 school spending by $540 per student this year, and it's suffering through annual tuition hikes of 15 percent at state universities.

Casinos didn't "fix" Florida schools, despite the politicians' promises, said Mark Pudlow, spokesman for the Florida Education Association.

"Everybody makes the argument for more gambling in their state by saying, 'It will help education!' But it just ends up replacing money that then gets shifted to other things — in our case, it was building prisons — and soon, we have less money than we started with," Pudlow said.

"Look, you're either committed to providing education and other essential services for your citizens or you're not," he said. "If you are, the state will raise the necessary revenue. If you're not, it won't. Opening casinos to get your money is just a cop-out."

This winter, scrambling for more cash and loathe to raise taxes, the Florida legislature is debating whether to double-down on gambling with a bill to authorize sprawling "Las Vegas-style casino resorts" in addition to racinos.

"I've given up saying it's not an expansion because I've lost that battle," the casino resort sponsor, Florida state Sen. Ellyn Bogdanoff, R-Fort Lauderdale, told reporters last week in Tallahassee. "Call it what you will."

The move dismays Florida racinos. They're just a few years old and don't relish the prospect of competition. But expansion of gambling is a common trend once states are disappointed by their initial earnings.

History shows that after a state lottery is approved, casino gambling often follows, and a never-ending fight commences for more gambling in more locations.

New York Gov. Andrew Cuomo wants his racino state to get full-fledged casinos. Pennsylvania and Delaware have approved table games to join slot machines at their casinos, and Delaware legalized sports betting. Illinois, a casino state, opted in 2009 to legalize video poker machines in thousands of restaurants, bars and truck stops.

'Politically easy'

Apart from Indian tribal casinos, 23 states allow some form of casino gambling, including all of Kentucky's neighbors other than Tennessee and Virginia. The states' tax rates on casino revenues range from 7 percent to 50 percent. Each state also gets different sums from casino license fees.

Most of the remaining states are discussing whether to expand gambling within their borders, according to the National Conference of State Legislatures in Denver.

"Casinos are the politically easy path. From the politician's point of view, it's a lot easier to do this than it is to raise revenue from your traditional sources, which would be taxes," economist Douglas Walker, author of the book *The Economics of Casino Gambling*, said during an interview last week.

Ohio approved casinos in 2009 and hopes to open the first two in coming months. One casino eventually is planned for Cincinnati, where it could draw Kentucky gamblers over the Ohio River, just as casinos already do in southern Indiana.

Economists said one net benefit to Kentucky casinos would be hanging onto the money Kentuckians now gamble across the state line. A 2005 study by Christian sen Capital Advisors, which works for racetracks and casinos, estimated that Kentuckians spent $671 million the previous year in Indiana and Illinois casinos, with those states pocketing $236 million of that in taxes.

"Kentucky is a key feeder market for the southern Indiana casino industry," the study said.

On the other hand, with so many casino states already operating in the region, Kentucky cannot expect to become a major gambling destination, said Mandy Rafool, a tax-policy specialist who studies gambling at the National Conference of State Legislatures.

"One important question is, who is your market? If you're not bringing in a lot of out-of-state people, then you really are just moving around your own population's discretionary entertainment spending," Rafool said. "Now, there still is some fiscal advantage to casinos in that case because the state probably will get a higher tax rate on that than it would from, say, a movie theater."

Negligible impact

As more states turn to gambling for salvation, a small cottage industry has arisen for academics eager to study casinos' impact on government budgets.

Overall, they say, it's negligible. In 2009, casino states on average drew 4 percent of their revenue from all kinds of gambling, including lotteries, racing and casinos. That same year, Kentucky, without a single casino, got about 2 percent of its revenue from gambling.

"Casino, racino and lottery revenue improve a state's fiscal position primarily when new gambling operations begin," said Robert Ward, director of fiscal studies at the Nelson A. Rockefeller Institute of Government in Albany, N.Y. Ward co-authored a study on states' gambling revenue last June.

"At that point, the state will likely gain some revenue that previously was going to neighboring jurisdictions, or was being spent on other forms of entertainment, or was being invested or put into savings," Ward said. "Once the additional gambling operations are in place, growth in future years is typically slower than growth in income- or sales-tax revenues, the two largest tax-revenue sources for most states.

"So gambling may represent a fiscal benefit in the short run, but it does not necessarily reduce budget problems in the long run."

In a 2010 study for the journal Contemporary Economic Policy, Walker went even further. He concluded that casinos brought "a negative impact on net state revenues" because they diverted resources from forms of spending that are more economically productive for communities and, therefore, for their governments.

By contrast, lotteries and racing seem to yield a net gain for states, Walker wrote.

"We are surprised by the casino results," Walker wrote in the journal. "Our results here indicate that the benefits side of the casino question is less of a certainty than is suggested in much of the public debate or literature."

Casinos cannibalize

Most gambling studies identify the same budgetary limitations:

■ Gambling is not recession-proof. It rises and falls along with everything else that states depend on for money, which makes it an unstable funding source.

The states' gambling revenue dropped 3 percent during the recession in 2009, according to Ward's study at the Rockefeller Institute.

■ States must establish costly new bureaucracies to license and regulate casinos.

For example, in 2010, New Jersey collected $296 million in casino tax revenue. At the same time, it spent $62 million on its two casino regulatory agencies, the Casino Control Commission and the Division of Gaming Enforcement.

■ Casinos eat into money people otherwise would have spent on food, clothing, entertainment and other items, and even on other forms of gambling, such as lotteries and racing, reducing what the state collects from those areas.

A 1998 study of Missouri casino receipts found that nearly half of the money was offset by the gamblers' diminished spending on other goods and services in Missouri.

Another study, in 2002, concluded that a state could expect to lose 83 cents in lottery revenue for every dollar it took from casinos. This was similar to a 1995 study of horse racetracks co-authored by Richard Thalheimer, an equine-industry economist in Lexington.

The presence of lotteries brings "a substantial loss in attendance, as well as in wagering" at tracks, Thalheimer wrote.

"People only have so much money to gamble. With casinos, you'll lose a big chunk of your lottery proceeds and a fair amount of your pari-mutuel racing proceeds," said Mallach at the Federal Reserve Bank.

In Kentucky, the racetracks hope to avoid competition by lobbying the General Assembly to grant them exclusive rights to casino gambling. Although the state would lose tax money if parimutual wagering dropped, the companies that own the racetracks would add to their collective bottom lines.

Churchill Downs in Louisville already owns casinos around the country in addition to its racetracks, and it's poised to earn more from slots than ponies. Last year, it reported $28 million in earnings from casinos and $35 million from racing. That's a dramatic change from two years earlier, when it reported $18 million from casinos and $57 million from racing.

"The popularity of horse racing is declining," Churchill Downs told shareholders last March. "We believe lower interest in racing may have a negative impact on revenues and profitability in our racing business."