

10-1980

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### Recommended Citation

Strecker, Mary F. (1980) "Not For Profit: Lotteries," *Woman C.P.A.*: Vol. 42 : Iss. 4 , Article 8.  
Available at: <https://egrove.olemiss.edu/wcpa/vol42/iss4/8>

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# Not For Profit

## Lotteries

Guest Editor:  
Mary F. Strecker

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This paper attempts to review the problems inherent in accounting for a rather unusual area of not-for-profit accounting — the State Lottery. The accounting treatment is brief and is not intended to be a comprehensive treatment of the accounting procedures. The article is intended to acquaint readers with an area of "Fund Accounting" often overlooked in rather traditional treatments.

Man seems to have been born with an instinct to solve problems by chance. Historically, chance and lottery are evidenced in many of our ancient writings. Biblical texts of our Judeo-Christian heritage give examples of "casting lots." It was in such manner that the clothes of the crucified Christ were disposed of as well as the filling of the place left empty by the betrayal of Judas. With the coming of immigrants to the New World we find the settlement of Virginia in the 1600s financed by lottery. The trend, in fact, in all of the thirteen original colonies seemed linked to chance or lottery for fund raising purposes. In more modern times, various states in an effort to put a lid on taxation have turned to lotteries to help placate their constituents and alleviate tax burdens.

With the increasing generation of General Fund revenues through the operation of state-run lotteries there arises a need to examine this unusual area of not-for-profit accounting. The accounting treatment described below is brief and is intended only to acquaint readers with an area of "Fund Accounting" often overlooked.

### Modern State Lotteries

Since the mid 1960s, more and more states are looking to games of chance as a means of replenishing

their coffers. Some state legislators have argued that the states entering the gambling business would squeeze out the lottery activities of organized crime. In addition, money would be raised and channeled to the public good.

Following this line of reasoning came a "rebound action." Persons who previously viewed gambling as wrong, now believed it to be legally sanctioned. Hence, organized crime increased rather than relinquished its hold on the numbers racket. Experience has proven that the revenues so generated are substantial, but the costs associated with conducting a state-run lottery are also substantial, exceeding by many times the cost of collecting the tax dollar through more traditional channels. The administrative function of collecting the tax dollar through the usual levying procedures costs about \$.015 — \$.05 per tax dollar raised whereas a dollar of lottery-raised revenues costs in the range of \$.45 — \$.50 per dollar raised. Too, experience has shown that while initial interest in lotteries is great, over the long term interest diminishes and administrative costs increase in an attempt to promote the purchase of lottery tickets.

States which have had recent experience with lotteries include: New Hampshire, New York, New Jersey, Connecticut, Pennsylvania, Massachusetts, Michigan, Maryland, Rhode Island, Maine, Ohio, Delaware, and Illinois. Much of the discussion that follows relates to the Illinois experience with its state-run lottery. Anyone passing through O'Hare Field, the world's busiest airport, cannot help but encounter the various wall placards enticing the traveler to take part in games of chance.

## The Illinois State Lottery

From July 1, 1974, the time of its inception, the Illinois State Lottery Commission has attempted to conduct the game as a "business operation in the public domain." Forty-five percent of total revenues received by the Illinois State Lottery is designated for prize money. Several states, along with Illinois, have found that something less than 50% of "the take" is paid out in prize money. Prizes are generally about 45% of sales, while another 10% is used for administrative costs.

In the first year of operations (July 1, 1974-June 30, 1975) prize money in Illinois was allotted to 1,322,240 persons with prizes ranging from a \$20 one-time prize to a grand prize of \$50,000 per year for life. These 1,322,240 winners were broken down as follows:

1,317,513 winners of \$20 - \$250
4,584 winners of \$250 - \$25,000
52 winners of \$50,000
27 winners of \$100,000
51 winners of \$300,000
6 winners of \$400,000 (\$1,000 a month for life)
6 winners of \$1,000,000
1 winner of \$50,000 a year for life

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1,322,240 Total winners

In its first year of operation, the Illinois lottery exceeded expectations and generated General Fund Revenues of \$60,000,000.

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## Mechanics of the Lottery

In exploring the mechanics of a state-run lottery one finds several elements common to the various states. There must be a determination of the type of tickets (cost; prize combinations; expiration dates; control of ticket alterations, counterfeit, and fraud) and a network of sales outlets with sales personnel. The State of Illinois has utilized a combination of several types of lottery

tickets: the regular fifty-center; the seasonal ticket, e.g., Spring Stampede, the Grand Slam and the Instant Winner. The Instant Winner has proved attractive to persons who may just be passing through (the O'Hare traveler) and wouldn't be interested in the regular weekly drawing.

In addition to the types of tickets, the sales network and personnel, there exists a need for a method of accountability. Just as with most documents requiring accountability, a system of pre-numbered tickets is a universal requirement. A central

### Costs associated with conducting a state-run lottery are substantial

distribution office must record the numbers sent to the various smaller outlets. A system is needed whereby members of the distribution network must account for all tickets placed in their jurisdiction. This must take place at a time just prior to the drawing; tickets are accounted for either as sold or returned intact.

Generally a bank is the center of the distribution network. From there the lottery tickets go to such varied agents as drugstores, grocery stores, gas service stations, restaurants, lounges, liquor stores, and bars. These agents must pay a license fee to be a state lottery distributor. In turn, these network entities generally receive a commission on the tickets that they sell.

#### Accounting for "Sales"

When all ticket distribution is properly accounted for; both sold and unsold tickets, a basic sales entry is made. In summary form, this entry is:

	Dr.	Cr.
Cash—State Lottery Fund	xxxx	
Lottery Commissions	xxxx	
Lottery Sales		xxxx

So one has a winning ticket? How does she claim her prize? If a ticket is a winner for \$50 or less, most states permit the ticket-selling agent to award the prize. About five percent of the total lottery winnings go

unclaimed. Generally a prize of over \$50 must be claimed at a given center. When a prize exceeds \$10,000 it generally is not paid in a lump sum but rather over the span of a year. A "Prize Journal" is maintained by the State of Illinois and in the case of larger prizes (\$10,000 or over) the total winnings are given recognition. Monthly reductions to the accounts are made as the prizes are distributed to the winners.

In the State of Illinois, lottery monies are General Fund revenues which are allocated in approximately the following pattern:

Education	34%
Public Health & Social Services	26%
Public Aid	23%
Natural Resources, Environment, and Transportation	6%
Other	11%
	<hr/>
	100%

#### Conclusion

While this was not intended as an in-depth study, we can abstract some inherent problems in the accountability of state-run lotteries as follows: (1) In recent years there has been a growing trend for more states to evaluate them as a means for increasing revenues. (2) There is a strong temptation on the part of non-lottery states that border a lottery state to give it a try because legislators see monies drifting across state lines and feel these could be put to use in their own domain. (3) State lotteries do not lessen organized crime's "numbers racket" within state boundaries and they may, in fact, increase the involvement. (4) Most states that have participated in lotteries for revenue purposes have found that the revenues obtained are substantial. (5) Costs to raise a dollar of tax by lottery far exceed the cost to raise the same dollar by tax levy because the state must set up a well-defined and controlled distribution network as well as controlled claim centers.

This paper does not attempt to explore the ethic or moral principles involved in lotteries, but only to view the facts which may be summarized from the foregoing. Ω

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## The Educational Foundation of AWSCPA-ASWA

The Woman CPA is a joint endeavor of the two societies as is the Foundation. We should like to share with you, the readers, an exciting and new concept for honoring professionally your peers, friends and family.

Accolades are due Connie Barcelona, previous editor of our prestigious journal. She has given us a title and purpose for funds contributed in memory of Sally Self. Here is her explanation of the Laurels Fund:

Not until the latter half of the twentieth century have women of distinction been tacitly acknowledged, especially within the accounting profession. Eminent among these was the late Sally J. Self, CPA, a member of American Society of Women Accountants and a former national president of American Woman's Society of Certified Public Accountants.

In recognition of her contributions to both the stature of women and the field of accounting, her many friends have established a fund to be called Laurels Fund as symbolic of her lifetime of outstanding achievement. The laurel has roots in the fables of Greek mythology when it became the sign of achievement with its twined leaves circling the brow of one gifted in arts, athletic competition and ultimately the Roman emperor.

It is the trustees' intention to retain intact the principal of the Laurels Fund as a separate fund within the Educational Foundation of AWSCPA-ASWA. Income flowing from the fund will be used to further the education of selected women accounting students who show promise of significant achievement in the profession.

It is hoped that the Laurels Fund will be kept ever green by gifts as a tribute in life or a memorial in death.

Connie with her "gift" of expression has echoed all our thoughts and ideas.