

Let's Really Reform New Mexico's Lottery Scholarships

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Introduction

New Mexico's lottery scholarship program has the potential to be an incredible boon to students throughout the state who are looking to better themselves and their economic opportunities through education. The good news is that since 1996, more than 82,600 students from across the state have attended New Mexico public colleges, universities and technical colleges with the help of Legislative Lottery Scholarships.¹ The Lottery provided more than \$528 million for scholarships over that time period.²

The program pays 100% of tuition for eight consecutive semesters of eligibility beginning with the second semester of college enrollment as long as those students maintain a 2.5 GPA in their college studies. The scholarship may be used at 25 public colleges, junior colleges or universities in New Mexico, including:

- 7 four-year institutions;
- 10 two-year branch institutions;
- 8 two-year independent institutions.

The lottery scholarship is a popular program for several reasons. Unlike most government programs, the proceeds to fund it are not collected in a coercive process through taxation. Rather, it is, as the name implies, funded out of revenues from the New Mexico Lottery. Also, given the rapidly-rising price of a college education – at a rate far faster than inflation and even health care over the last several decades³ – the scholarship program offers peace of mind for middle class families concerned about saving funds needed for a higher education.

Of course, that peace of mind for middle class families comes at a price. There is no such thing as a free lunch and there are serious issues associated with it the Lottery Scholarship program and its funding mechanism. There are also serious questions over whether the program, as currently formulated, provides maximum benefits in terms of economic and educational outputs. Eligibility for students in military families is just one issue that has been reported on recently in the media.⁴

¹ New Mexico Lottery, Legislative Lottery Scholarships, <http://www.nmlottery.com/legislative-lottery-scholarships.aspx>.

² New Mexico Lottery, "Financial Statements," June 2012, <http://www.nmlottery.com/annual-reports.aspx>.

³ Niraj Chokshi, "Education Costs Rising Faster than Health Care," *The Atlantic*, August 24, 2009, <http://www.theatlantic.com/business/archive/2009/08/education-costs-rising-faster-than-health-care/23705/>.

⁴ Mike Bush, "Losing the NM Lottery," *The Albuquerque Journal*, January 7, 2014, <http://www.abqjournal.com/332240/news/military-transfer-cuts-off-nm-scholarships.html>

As the Legislature considers reforms essential for extending the financial solvency of the Lottery Scholarship program, there are several important considerations that we believe must be considered. It is hoped that these reminders and guidelines will be useful in assisting policymakers as they attempt to make the Lottery Scholarship sustainable.

1. **The Lottery Scholarship is NOT free money and there are real-world costs to gambling**, especially when it is sponsored by the government. The Rio Grande Foundation does not oppose gambling, however, it is worth noting that gamblers disproportionately come from lower income and education levels. One study from Carnegie Mellon found that “Lotteries set off a vicious cycle that not only exploits low-income individuals’ desires to escape poverty but also directly prevents them from improving upon their financial situations.”⁵

While money spent by low income and poorly-educated gamblers may have otherwise been spent in an Indian casino, the government’s explicit endorsement of lotteries combined with the support of socially-beneficial things like college scholarships undoubtedly increase lottery participation among some groups.

Funds spent on the lottery could have been consumed in other ways for immediate benefit, saved, invested, or spent directly on attaining an education for oneself or one’s offspring. This is not to say that all other uses would be superior to planning the lottery, but to make clear that there *are* alternatives to playing the lottery, many of which result in superior societal outcomes.

Notably, less than 25 percent of New Mexicans graduate from college. At the outset, these individuals tend to be wealthier than average and certainly wealthier than the gamblers who fund their scholarships. That disparity grows dramatically once the salary premium garnered by college graduates is accounted for, which means that college graduates make on average 180 percent of what high school graduates do.⁶

2. That “college premium” sounds like a good reason for government to do anything it can to increase the number of college graduates, but as currently designed, the Lottery Scholarship program achieves mediocre results. This is according to the report, “New Mexico Lottery Scholarship Program is Bad for New Mexico Students,” by Derrick Kapchinsky.⁷

5 Kelli McElhinny, “Why Play a Losing Game? Carnegie Mellon Study Uncovers Why Low-Income People Buy Lottery Tickets,” July 24, 2008, http://www.cmu.edu/news/archive/2008/July/july24_lottery.shtml.

6 “The College Premium,” *New York Times*, November 12, 2013, http://www.nytimes.com/interactive/2013/11/12/business/the-college-premium.html?_r=0

7 Derrick Kapchinsky, *New Mexico Lottery Scholarship Program is Bad for New Mexico Students*, Omnic Education, March 9, 2011, <http://www.omnieducation.com/education-blog/bid/26642/The-New-Mexico-Lottery-Scholarship-is-Bad-for-New-Mexico-Students>.

According to this report, the **NM Lottery Scholarship encourages students to slack off in high school** because The Lottery Scholarship is all about lowered expectations. By making the only requirements for eligibility a New Mexico high school diploma or GED, the Lottery Scholarship assumes that New Mexico high schools prepare students for college. The fact that roughly half of all New Mexico students need remedial classes proves that New Mexico high schools are not sufficiently educating students.

Because the students are not ready, between 25% and 35% of New Mexico high school graduates will lose the Lottery scholarship after their first semester of college. And only 15% of all people who lose their Lottery scholarships will graduate in 6 years. The rest of the students, unprepared by their high schools and without funds, will not finish a college degree within that time.

The **NM Lottery Scholarship does not help low-income students succeed in college.** The low-income students only receive the scholarship half as often as more affluent students, and those low-income students who do receive it lose it twice as often. The Lottery is designed to help students who need it pay for school. In reality, those students are not the beneficiaries of the program.

It keeps (too many of) our best students in New Mexico. New Mexico is a geographically-isolated and culturally-unique state. This isolation and uniqueness can lead to an undue suspicion of outsiders and their ideas.

Unfortunately, by offering “free” educations to only in-state institutions, the Lottery Scholarship program incentivizes some of the top students in the state to remain close to home rather than pursuing educational options elsewhere. The lack of exposure to outsiders further reinforces New Mexico’s geographical and cultural isolation.

Kapchinsky’s report is a quick, easy read and covers these ideas from its own perspective while making several salient points that must be considered by policymakers.

- 3. The Lottery Scholarship Encourages Price Inflation in Higher Education:** As previously discussed in Rio Grande Foundation reports and elsewhere, the cost of a higher education has spiraled out of control in recent years. The fact that scholarships pay the full-freight of an education regardless of institution type or level leads to the proverbial “moral hazard” problem in economics. Students are not price sensitive and actually have the perverse incentive to pursue the most costly education option available to them rather than pursuing the option that is correct for them.

Institutions have similar, perverse incentives. With 26% of New Mexico’s full-time undergraduates having their tuition paid for by the Lottery Scholarship program, the schools have little incentive to compete for scholarship students based on price.⁸ Rather,

⁸ NM Legislative Lottery Scholarship,
http://www.unm.edu/~gpsa/GPSA/ADVOCACY_files/WHITEPAPERLotteryScholarship.doc.pdf.

they will inevitably design their pricing system in such a way as to maximize the per-student return to the institution.

Policy Recommendations

The following are our recommendations for the Legislature regarding the Lottery Scholarship:

- 1. Do not use General Fund revenues to prop up the program.** New Mexico taxpayers already spend disproportionately to fund institutes of higher education in our state. According to Table 5 of the report “State Education Finance,” New Mexico taxpayer funding for higher education per student is among the top-ten nationally among states.⁹ They, especially low-income taxpayers of limited means, should not face the additional expense of financing scholarships for wealthier-than-average citizens of their state.

Further, there are serious questions as outlined above regarding the effectiveness of the Lottery Scholarship program. Before blindly deciding to pour more tax money into the program, the Legislature should commission a study of the program’s effectiveness. Recommendations could be used to strengthen the program and understand how limited funds might best improve the educational outcomes of New Mexico students and economic outcomes for our state as a whole.

The Legislature and Gov. Martinez, during the 2013 legislative session, have already taken the fateful step of moving the program beyond reliance on lottery proceeds to include reliance on the tobacco severance fund. Now, according to media reports, during the 2014 legislative session, legislators will be asked to allocate General Fund revenues to the program.

Such moves will inevitably have the impact of severing scholarship provision from lottery revenues and expanding the law from a strictly-limited program to a potentially-open-ended entitlement.

The recommendation not to expand the program to rely on General Funds is of paramount importance. Having limits on the program incentivizes policymakers to develop innovative ways to allocate limited resources for the benefit of the largest number of students and New Mexico’s economy. The following recommendations are designed to leverage limited lottery funds for the best educational and economic outcomes.

- 2. Transform the Lottery Scholarship to a limited tuition voucher:** A voucher system would provide many benefits for students and educational outcomes as a whole. A voucher would be nothing more than a scholarship that would allow students to attend the

⁹ State Higher Education Executive Officers, “State Higher Education Finance FY 2012,” 2013, <http://www.sheeo.org/sites/default/files/publications/SHEF%20FY%2012-20130322rev.pdf>.

school of their choice. Ideally, the choice of school would be up to the discretion of the student and would not be limited to New Mexico institutions.

The voucher would, depending on the school, likely not cover the entire cost of a four-year education; rather it would cover a portion of overall tuition costs. The size of the voucher could be based on lottery revenues in a given year. Ideally, students would be further empowered to use excess scholarship funds for education-related items such as room and board. Such a plan has several significant benefits:

- a) It encourages price shopping and aggressive efforts on the part of students to obtain alternative financing including scholarships and parental assistance on the part of students;
 - b) Students would no longer be incentivized to “slack off” in high school under the assumption that a free college education will be waiting for them;
 - c) Rather than encouraging students who might otherwise be lured to attend a New Mexico school for the simple fact that it is “free,” students would be encouraged to attend the school that makes the most sense for them regardless of location;
 - d) Students are currently incentivized to pursue more costly educational opportunities at four-year institutes because the scholarship program insulates them from cost differences between two and four-year institutes. At UNM, to take one example, 15 credit hours and student fees run approximately \$4,000 per semester for an in-state student.¹⁰ At CNM, 15 credit hours can be taken for less than \$600 with fees ranging from \$40 to more than \$1,000 depending on program of study.¹¹
- 3. Be judicious about relying on college grades in allocating scholarships:** A voucher would be our preferred reform however, given political limitations in New Mexico and inertia within the existing; they may not be a realistic option.

One option that has repeatedly come up is to reduce the number of scholarships by increasing the GPA requirement while attending college. This sounds like a simple enough solution, but there are a few serious issues to consider:

- a) The meaning of a GPA differs by institution. New Mexico Tech is one of the most demanding Science, Technology, Engineering, and Math institutes in the entire nation. A 2.5 or 3.0 GPA in engineering or physics at this school is an incredible achievement. Without belittling the achievements of students in other fields, the demands of a maintaining a similar GPA in a General Studies is simply not the same;
- b) Already, concerns abound over grade inflation at institutes of higher learning. The last thing needed is for college professors to face additional pressure from students struggling to maintain their college scholarships.

¹⁰ UNM Bursar’s Office, Spring 2014 Tuition and Fees, <http://bursar.unm.edu/docs/2014SpringUndergraduateTuitionandFees.pdf>.

¹¹ CNM Tuition 2013-2014, <http://www.cnm.edu/depts/enrollment/registration/Tuition.html#fees>

4. **Don't turn the program into another wealth transfer program:** Some advocates, especially on the political left have expressed a desire to emphasize “financial need” in allocating funds for the Lottery Scholarship program. Such a move would be unwise for several reasons:

- a) There are already a number of scholarship programs available for low-income students. Redoubling the program's focus on such students would reduce the program's effectiveness as it would simply “crowd-out” other scholarship funds;
- b) If policymakers wish to develop a high-performing 21st Century workforce, they need to incentivize high-performing students to obtain an education and to live and work in New Mexico. Unfortunately, as mentioned above, low-income students who receive the Lottery Scholarship drop out of the program at twice the rate of other students. Lottery Scholarship drop outs represent a significant loss of limited scholarship resources.

About the Author

Paul Gessing is the President of New Mexico's Rio Grande Foundation. The Rio Grande Foundation is an independent, non-partisan, tax-exempt research and educational organization dedicated to promoting prosperity for New Mexico based on principles of limited government, economic freedom and individual responsibility