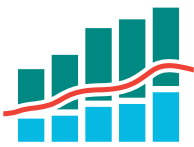




# SHEEO

STATE HIGHER EDUCATION EXECUTIVE OFFICERS ASSOCIATION



# SHEF

STATE HIGHER EDUCATION FINANCE

# 2022

## ISSUE BRIEF: ANALYZING LOTTERY PROCEEDS AS AN ASPECT OF STATE SUPPORT FOR HIGHER EDUCATION

PEARSON BROWN

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## INTRODUCTION

Researchers have examined lottery earmarks' impact on higher education and the societal effects that gambling can engender, yet there is much more to learn about the relationship between state lotteries and higher education across the United States. With lotteries representing a medium that policymakers have frequently promoted to generate revenue for public projects without raising taxes, SHEEO agencies and state policymakers can benefit from knowing more about state lotteries' nuances and how this funding stream relates to other aspects of state support. To this end, this issue brief focuses on the role lotteries play in providing state-level support for higher education, as well as ways funding structures and areas of higher education that receive lottery proceeds differ by state.

Each year, state agencies report non-tax support for higher education which includes lotteries, as well as other gaming proceeds and tobacco settlements, for SHEEO's annual State Higher Education Finance (SHEF) data collection. In states that report non-tax support for higher education, the components making up this source vary. For some states, such as Maine and Tennessee, their non-tax support for higher education solely consists of lottery proceeds, whereas non-tax support in other states, such as Colorado and Maryland, does not since these states do not utilize lottery proceeds for higher education. In fiscal year (FY) 2022, non-tax support represented 4.0% of total state and local support for higher education in the United States (approximately \$4.85 billion). South Carolina had the largest percentage of state and local support for higher education that came from non-tax revenue (34.4%), and higher education in 23 states and Washington, D.C., did not report any funds from non-tax related areas. Six states (Florida, Georgia, Kentucky, Missouri, South Carolina, and Tennessee) where non-tax support made up at least 10% of the state's financial support for higher education in FY 2022 had a lottery that earmarked higher education as a revenue recipient. Although Nevada's non-tax support made up at least 10% of its financial support, it does not have a lottery, but has adopted essentially all other forms of gambling. Since non-tax support encompasses several funding sources, narrowly focusing on lotteries (a component of non-tax support) shines light on an area of inquiry that the annual SHEF report does not address and can help state higher education agencies better understand how lotteries contribute to total state and local support for higher education.

## HISTORY OF LOTTERIES AND HIGHER EDUCATION

The relationship between lotteries and higher education funding predates the United States. Many colonial colleges, such as Harvard, Yale, Dartmouth and Williams either benefited from or facilitated lotteries as a fund-raising strategy.<sup>1</sup> Colonial colleges received little financial support from their colony's legislature and were heavily tuition dependent, leading our nation's earliest colleges to leverage lottery proceeds to finance building projects and bolster their endowments.<sup>2</sup> Colonial-era lotteries invited a sense of public participation to contribute toward advancing the public good, though moral objections and lottery organizers' corruption eventually led lotteries to fall out of favor.<sup>3</sup> Several gambling-based scandals that gained national notoriety resulted in nearly every state outlawing their lottery by the early 1900s.

Our modern concept of state lotteries began in 1964 when New Hampshire adopted a lottery to augment K-12 education funding. New Hampshire lacked a state income tax and subsequently ranked last amongst the states in terms of public spending, which led its legislators to propose a lottery as a mechanism for raising money for education.<sup>4</sup> Despite New Hampshire's lottery yielding small proceeds in its initial years, lottery adoption diffused throughout the Northeast; New York operationalized a lottery three years later (1967), and New Jersey and Massachusetts soon followed in 1969 and 1971, respectively. By the end of the 1980s, nearly 75% of the U.S. population lived in a state that hosted a lottery.<sup>5</sup> The rapid ascent of lotteries is largely due to policymakers framing lotteries as a means of procuring funds for charitable and honorable causes, such as education, while keeping other tax rates constant.<sup>6</sup> Mississippi was the most recent state to adopt a lottery (2019), meaning as of FY 2022, 45 states operate a lottery and each state transfers a portion of its lottery's proceeds to at least one beneficiary.

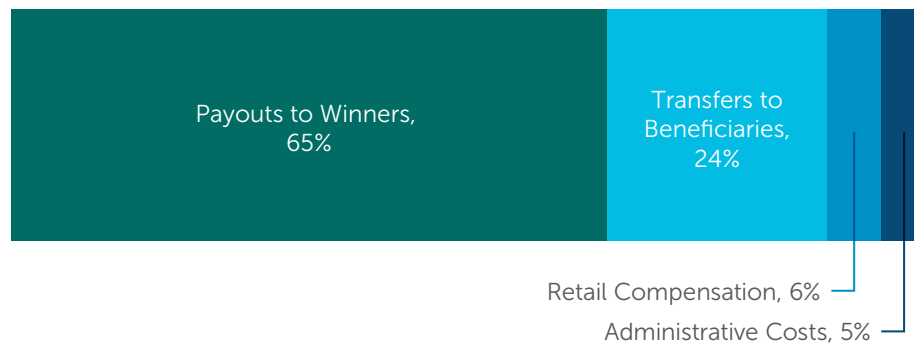
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  2. Brubacher, J. S., & Rudy, W. (1976). Higher education in transition: *A history of American colleges and universities, 1636-1976*. (3rd ed.). Harper & Row.
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  4. Weiss, A. E. (1991). *Lotteries: Who wins, who loses?* Enslow Publishers.
  5. Clotfelter, C. T., & Cook, P. J. (1989). *Selling hope: State lotteries in America*. Harvard University Press.
  6. Nelson, M., & Mason, J. L. (2007). *How the South joined the gambling nation: The politics of state policy innovation*. Louisiana State University Press.

## LOTTERIES AS A FUNDING STREAM

The North American Association of State and Provincial Lotteries (NASPL) states that at the national level, lotteries transfer around 24% of their total revenue to beneficiaries,<sup>7</sup> though funding formulas vary by state. State lotteries' largest expense is payouts to winners, and lottery agencies also incur relatively minor administrative and retail compensation costs. *Figure 1* represents the national-level percentage distribution of lottery revenue.

**FIGURE 1**

### **DISTRIBUTION OF STATE LOTTERY AGENCIES' TOTAL REVENUE, U.S., FY 2022**



**NOTE:**

1. Percentages are based on estimates from the North American Association of State and Provincial Lotteries at the national level. Revenue distribution may vary across states.

**SOURCE:** North American Association of State and Provincial Lotteries

SHEEO agencies should consider how a state lottery's revenue distribution protocols affect the amount of financial support that higher education receives from its state's lottery. Implicit within state lotteries' capacity to award funds to beneficiaries is that individuals must purchase a projected number of tickets. Contingency on ticket sales means beneficiaries should note lottery profits are not guaranteed and may fluctuate year over year. States use proceeds from their lottery to support a range of public programs such as capital projects, health and human services, and all levels of education. Within education, the distribution of lottery proceeds varies. Many states exclusively earmark K-12 education to receive their lottery's profits, while some states prioritize higher education, and several disperse lottery proceeds to both levels of public education.

7. North American Association of State and Provincial Lotteries. (n.d.). Myths, FAQ & History. *North American Association of State and Provincial Lotteries*. [naspl.org/mythsandfaq](https://naspl.org/mythsandfaq)

## DATA AND ANALYTICAL STRATEGY

To parse out lotteries' role in providing funds for higher education, SHEEO staff contacted agencies that provide SHEF data in 30 states that the NASPL lists as transferring proceeds from their lottery to education (at any level). SHEF data providers then gave SHEEO staff information on whether their state distributes any of its lottery proceeds to higher education. Data providers in 24 states responded, 14 of which said their state distributes lottery revenue to higher education. These data providers gave SHEEO staff the amount of funds their state's lottery transferred to public higher education each year from 2001-2020 and how their state used those proceeds to benefit public higher education. *Table 1* contains the 14 states that stated they transferred lottery funds to higher education.

This dataset consists of financial information from three data sources: (a) NASPL data on each state's annual lottery revenue and the amount each lottery agency transferred to beneficiaries, (b) the annual amount of lottery profits that higher education received and areas within higher education's budget that these funds support, acquired directly from SHEEO agencies' SHEF data providers, and (c) SHEEO's SHEF dataset, which contains every state's total support for higher education as well as funding amounts for specific areas (e.g., financial aid, four-year institutional appropriations, etc.). For reasons including that some states recently adopted a lottery and/or state governments only recently earmarked higher education as their lottery's revenue recipient, some state-level data begins after 2001. All financial data are adjusted to 2022 dollars using the Consumer Price Index.

Combing data from three sources presents a limitation for calculating lottery support for higher education on an annual basis. Lottery agencies may transfer funds to higher education at times that do not coincide with a fiscal year, and SHEEO agencies may not immediately dispense all proceeds they receive, leading higher education to spend a year's lottery proceeds across multiple fiscal years. To match annual lottery transfers to areas of a state's investment in higher education, SHEEO staff assumed that lottery transfers from one fiscal year are entirely reflected in the next fiscal year's higher education appropriations. Therefore, readers should view the subsequent calculations as estimates and use caution when associating changes in lottery transfers to higher education appropriations the following year.

# STATE LOTTERIES AND HIGHER EDUCATION

While this is not an exhaustive list of states that use lottery proceeds to support higher education, *Table 1* illustrates the range of amounts that higher education receives from state lotteries and areas within higher education that these funds support.

**TABLE 1**  
**STATE LOTTERY SUPPORT FOR HIGHER EDUCATION**

STATE	YEARS INCLUDED IN ANALYSIS	TOTAL TRANSFERRED TO HIGHER ED., FY20	% OF LOTTERY REVENUE TRANSFERRED TO HIGHER ED., FY20	AREA OF HIGHER ED. THE LOTTERY SUPPORTS
ARKANSAS	2011-2020	\$100 MILLION	89.6%	FINANCIAL AID
CALIFORNIA	2001-2020	\$430 MILLION	20.3%	INSTITUTIONAL APPROPRIATIONS
FLORIDA	2001-2020	\$1,480 MILLION	67.8%	INST. APP. & FINANCIAL AID
GEORGIA	2003-2020	\$955 MILLION	69.8%	FINANCIAL AID
KENTUCKY	2004-2020	\$302 MILLION	93.9%	FINANCIAL AID
MAINE	2006-2020	\$5 MILLION	7.4%	FINANCIAL AID
MISSOURI	2001-2020	\$105 MILLION	29.1%	INST. APP.
MONTANA	2016-2020	\$560 THOUSAND	4.0%	FINANCIAL AID
NEBRASKA	2004-2020	\$12 MILLION	23.3%	FINANCIAL AID
NEW JERSEY	2018-2020	\$146 MILLION	11.7%	FRINGE BENEFITS
NEW MEXICO	2001-2020	\$50 MILLION	102.8%	FINANCIAL AID
OREGON	2003-2017	N/A	N/A	FINANCIAL AID & OUTDOOR SCHOOL
SOUTH CAROLINA	2004-2020	\$473 MILLION	85.4%	INST. APP. & FINANCIAL AID
TENNESSEE	2008-2020	\$482 MILLION	95.2%	FINANCIAL AID

**NOTES:**

1. All transfer amounts and corresponding percentages that higher education received from its state's lottery are estimates based on the assumption that lottery proceeds in one fiscal year are entirely reflected in the next fiscal year's higher education's appropriations.
2. Oregon utilizes a biennium budget and their last available year of data comes from their FY 2017 biennium budget, therefore Oregon is excluded from FY 2020 calculations.
3. New Mexico's lottery proceeds in FY 2020 included a special legislative appropriation, thus explaining why higher education received more than 100% of lottery proceeds.
4. All financial data are adjusted to 2022 dollars using the Consumer Price Index.

**SOURCES:** North American Association of State and Provincial Lotteries, state higher education agencies, and State Higher Education Executive Officers Association

The percentage of lottery proceeds that higher education receives varies by state, with states such as Maine and Oregon receiving less than 7% (on average for the range of years that these states provided) of the annual amount that a state's lottery transfers to beneficiaries, and states such as New Mexico and Tennessee benefiting from close to the entirety of their state's lottery's transfer amount. State systems typically use lottery proceeds to support higher education in one of two ways: institutional appropriations and student financial aid. When looking at institutional appropriations, the California State Lottery allocates a portion of its proceeds to the state's three higher education segments (the University of California System, the California State University System, and the California Community College System) based on enrollment numbers. These funds go toward educational purposes, with some funding restricted to instructional materials. Georgia exemplifies a state where higher education receives the majority of its state's lottery



proceeds, which Georgia higher education then uses to finance the state’s merit-based scholarship, Helping Outstanding Pupils Educationally (HOPE). Lottery proceeds in Kentucky have provided funds for financial aid that students can use at the state’s public two-year and four-year institutions, proprietary institutions, private four-year institutions, as well as at out-of-state institutions. Lottery earmarks for higher education are not necessarily bound to one area; Florida uses proceeds from its lottery to fund its merit-based scholarship, Bright Futures, and to provide appropriations to Florida’s two- and four-year institutions. Missouri allots funds from its lottery to enhance institutional appropriations, which Missouri’s public institutions use to fund salaries, purchase equipment, and award institution-based student financial aid.

## PORTION OF LOTTERY TRANSFERS THAT HIGHER EDUCATION RECEIVES

After first discerning whether higher education receives funds from a state's lottery, a useful next step for understanding the role lotteries play in providing state-level support for higher education is to consider what proportion of lottery profits that lottery agencies transfer to beneficiaries goes to higher education. While state lotteries transfer approximately 24% of their annual profits to beneficiaries, in some states, higher education is the lottery's sole recipient of charitable donations, and in others, states' policy designs position higher education as one of many beneficiaries. Indeed, SHEF data providers from 10 states said that higher education in their state does not receive lottery proceeds, which adds to the importance of discerning whether earmarks for "education" include higher education or instead refer to states' K-12 systems.

In FY 2020, lottery agencies in five states within this sample transferred at least 85% of their proceeds to higher education (Arkansas, Kentucky, New Mexico, South Carolina, and Tennessee). Each of these states use lottery proceeds to help subsidize their financial aid programs. South Carolina's legislature also allocates a portion of lottery proceeds to the state's two- and four-year institutions. Lottery proceeds in these five states typically represent the entirety of non-tax support for higher education and these funds produce a substantial amount of funding that goes toward designated line items within higher education's overall budget, primarily financial aid. Higher education in three states within this sample (California, Missouri, and Nebraska) received between 20-30% of their respective state's lottery's proceeds in FY 2020, thus positioning higher education as a prominent, yet not the exclusive beneficiary of lottery revenue. Montana and Oregon's lotteries each transfer less than 5% of their proceeds to higher education each year (FYs 2017-2020 for Montana and FYs 2005-2017 for Oregon).<sup>8</sup> State lotteries accumulating varying amounts of profits and following their own monetary distribution protocols helps SHEEO agencies understand how a state lottery's earmark structure affects a lottery's capacity to support higher education.

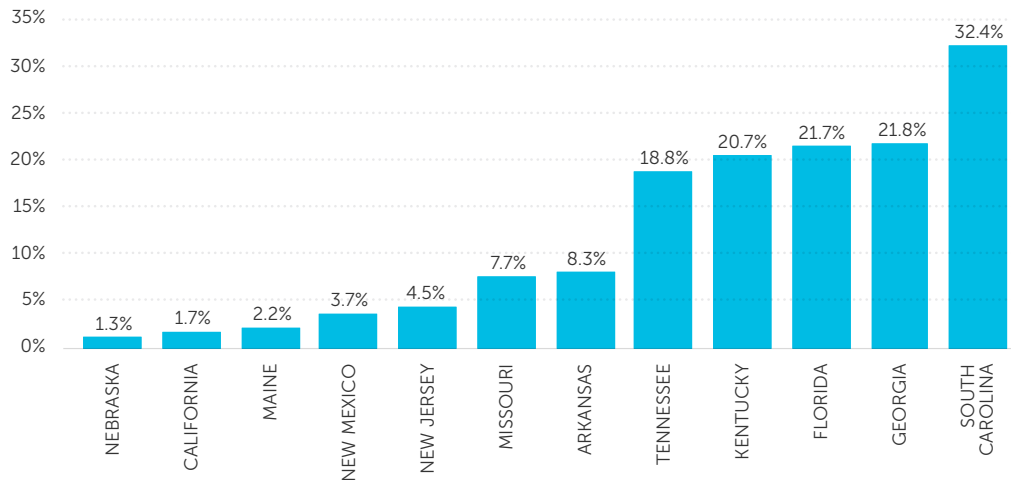
State lotteries transferring different percentages of their revenue to higher education shows the initial amount higher education receives from its state's lottery, though placing these transfer amounts in conversation with overall funding levels is the next step for understanding lotteries as a funding stream. For the five states where higher education received the near entirety of its state's lottery's proceeds, these states vary in terms of what percentage of their overall support for higher education comes from lottery proceeds. For example, lottery proceeds represented around 20% of Georgia's, Florida's, Kentucky's, and Tennessee's total state and local support for higher education in FY 2020 yet comprised 3.7% of appropriations to higher education in New Mexico. As seen in *Figure 2*, New Mexico was one of five states<sup>9</sup> where lottery proceeds represented less than 5.0% of state and local support for higher education, with California, Maine, Nebraska, and New Jersey aligning with this funding bracket.

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8. Oregon utilizes a biennium budget, and their last available year of data come from their FY 2017 biennium budget.

9. Montana did not receive lottery proceeds in FY 2019 to be used in FY 2020 and FY 2020 data are not available for Oregon, therefore these states are excluded from *Figure 2*.

**FIGURE 2**  
**LOTTERY REVENUE AS PERCENTAGE OF STATE AND LOCAL SUPPORT**  
**FOR HIGHER EDUCATION, FY 2020**



**NOTES:**

1. To match annual lottery transfers to areas of a state's investment in higher education, SHEEO staff assumed that lottery transfers from FY 2019 are entirely reflected in a state's FY 2020 higher education's appropriations. Therefore, readers should view the above calculations as estimates. SHEEF defines state and local support for higher education as state tax appropriations and local tax support plus additional non-tax funds (e.g., lottery revenue) that support or benefit higher education, and funds appropriated to other state entities for specific higher education expenditures or benefits (e.g., employee fringe benefits disbursed by the state treasurer).
2. State and local support for 2020 includes federal stimulus funding provided to stabilize these sources of revenue for higher education.
3. Montana did not receive lottery proceeds in FY 2019 to be used in FY 2020 and FY 2020 data are not available for Oregon, therefore these states are excluded from *Figure 2*.

**SOURCES:** North American Association of State and Provincial Lotteries, state higher education agencies, and State Higher Education Executive Officers Association

Analyzing how lottery transfers and line-item appropriations evolve longitudinally sheds light on higher education's reliance on its state's lottery. For 10 states within this analysis (Florida, Georgia, Kentucky, Maine, Nebraska, New Jersey, New Mexico, South Carolina, and Tennessee),<sup>10</sup> lottery proceeds represented a higher percentage of total state and local support for higher education in FY 2020 than in the first year in which these states provided lottery data. Lottery proceeds becoming a larger funding source in several states could suggest that some states with lotteries are increasing their reliance on this source of state revenue to fund higher education. However, it is important to note that lottery proceeds represent a relatively small portion of funding to public higher education in several states, so the actual growth might be less impactful than changes in other sources of state support. For example, the percentage of state and local support for higher education in Nebraska that comes from lottery proceeds increased by 0.5 percentage points from FY 2005 to FY 2020. After adjusting for inflation, Nebraska's lottery transferred \$7.3 million of FY 2004 proceeds to higher education, making up 0.8% of state and local support when used in FY 2005. In FY 2019, Nebraska's lottery transferred \$14.4 million to higher education, which represented 1.3% of state and local support when used in FY 2020. Lottery revenue as a percentage of state and local support for higher education in South Carolina, the state that had the largest proportion of state and local funding derived from lottery proceeds in FY 2020, also had the greatest percentage point increase (11.8) since FY 2005, the first year in which

10. Oregon utilizes a biennium budget, and their last available year of data comes from their FY 2017 biennium budget.

South Carolina distributed lottery revenue to higher education. In FY 2004, South Carolina's lottery transferred \$314 million (in 2022 dollars) to higher education, which equated to 20.6% of South Carolina's state and local support when used in FY 2005, and in FY 2019, South Carolina's lottery transferred \$485 million to higher education, which equated to 32.4% of South Carolina's state and local support when used in FY 2020. Even if lottery proceeds are not the sole funding source for an area of higher education's budget, connecting changes in lottery transfer amounts that policymakers earmarked to support higher education can help SHEEO agencies compare how state governments have used lottery funds.

## AREAS OF HIGHER EDUCATION FUNDING

After learning about state lotteries' policy structures and the level to which higher education may access lottery profits, SHEEO agencies and policymakers should consider the areas of higher education that lottery proceeds support. It is likely that changes in one budgetary area spur adjustments to another line item, though looking at trends for line items that receive lottery proceeds is a useful practice for assessing lotteries as an aspect of non-tax support. Out of the states this analysis focuses on, 11 used lottery proceeds to help subsidize their financial aid programs, four allocated lottery proceeds to higher education in the form of institutional appropriations, and three directed lottery proceeds to multiple areas within their state's higher education's budget (see *Table 1*). Additionally, New Jersey higher education uses proceeds from its state's lottery to support fringe benefits of state-supported employees at its senior public institutions and community colleges.

Many policymakers who have advocated for their state to adopt a lottery have touted a lottery's potential to expand financial aid as justification for their state to start a lottery, so it is no surprise that the state governments that direct the highest percentage of their lottery's charitable contributions to higher education tend to earmark these funds to support scholarships. For example, between 2012 to 2020, lottery profits stayed above 69% of the amount Arkansas' legislature allocated to the state's financial aid offerings with a high point of 94.6% in 2014. Arkansas' legislators named their state's lottery the "Arkansas Scholarship Lottery," making it easy to connect ways policymakers designed Arkansas' lottery with the intent of supporting higher education through student financial aid.

In some states, changes in the amount of lottery profits higher education receives and the amount state governments allocate to earmarked line item(s) have increased or decreased in unison. For instance, Georgia and South Carolina's lotteries largely support their state's merit-based scholarships, and the amount these states received from their respective lotteries has grown at similar rates to the amount these states allocated to student financial aid. A similar pattern occurred in Arkansas; however, changes in this state illustrate volatility. In FY 2010, the fiscal year before Arkansas earmarked lottery funds for higher education, the state allocated \$88.5 million to financial aid (in 2022 dollars). In FY 2011, the first year in which the Arkansas Legislature earmarked higher education as a lottery revenue beneficiary, they awarded more than double that amount (\$193 million) to financial aid. Though some policymakers also expressed concerns that the lottery would produce revenue below projected levels.<sup>11</sup> Following the lottery allocating a peak amount to higher education of \$165 million in FY 2013, for each of the next four fiscal years, Arkansas' lottery transferred reduced amounts to higher education, and the amount the state allocated to student financial aid also declined across each of those subsequent four years.

The amount of money Florida's legislature allocated to student financial aid (which Florida's lottery helps fund) increased by more than 120% even though the total amount that their lottery transferred to beneficiaries, including higher education, grew by 44.7% from 2001 to 2020. Knowing that lottery-supported financial aid programs have expanded despite reductions in lottery proceeds or that these programs have outpaced lottery transfers in terms of percentage

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11. Wickline, M. R., (2011, December 7). Lottery on track to net \$5 million less: 12-month forecast for scholarships draws sharp words from legislator. *Arkansas Democrat Gazette*. [www.arkansasonline.com/news/2011/dec/07/lottery-track-net-5-million-less-20111207](http://www.arkansasonline.com/news/2011/dec/07/lottery-track-net-5-million-less-20111207)

growth can help SHEEO agencies and policymakers see the ways in which additional funding streams might be sustaining increases in state-support for various line items. In states where lottery transfers are expanding at a lower rate than the line items policymakers earmarked these funds to support, SHEEO agencies and policymakers should consider evaluating excess lottery proceeds' volatility in regard to higher education funding.

Since policymakers in three states within this analysis designated lottery proceeds to support multiple areas of higher education, SHEEO agencies who are seeking to study lottery revenues should remember the importance of matching lottery profits to corresponding aspects of higher education. For example, prior to Oregon's 2017 biennium budget, all lottery proceeds to higher education went toward supporting collegiate athletic programs, with attention to non-revenue producing sports and scholarships. Following the voters' approval of Measure 99 in 2016, Oregon's 2017 biennium budget earmarked lottery funds to higher education to begin supporting the state's Outdoor School which seeks to teach leadership skills to 5th and 6th grade students through STEM curriculum, which is housed at Oregon State University. With this change, the total amount of lottery proceeds that higher education received increased by six-fold in two budget cycles. Identifying instances when a new revenue recipient has driven change in the total amount of lottery proceeds allocated to higher education could further assist SHEEO agencies and policymakers' work to gauge lottery support as it relates to specific needs within higher education's budget.

## IMPLICATIONS

State lotteries providing financial support for higher education at varying levels and across different budgetary areas holds implications for SHEEO agencies. The historical context of policymakers leveraging lottery adoption as a tool for creating funding for public projects without raising taxes allows higher education leaders to anticipate that as states face budgetary constraints, policymakers will inevitably view state-sanctioned gambling as a potential solution. Should these adoption debates arise, SHEEO agencies will want to evaluate the extent to which and aspects of their system that could benefit from lottery proceeds against the risk of volatility in gambling-based proceeds and the possibility of crowding out other forms of revenue. SHEEO agencies can understand the relationship between gambling-based revenues (whether lotteries or another medium) and higher education by investigating how revenue totals, the percentage transferred to beneficiaries, and line items that receive gambling-based proceeds correspond to funding outcomes.

SHEEO agencies should not study lottery proceeds in isolation. State agencies should evaluate how lottery funding trends relate to other forms of state support, as well as examine which institutions and student populations benefit from lottery transfers. This approach allows higher education leaders to gauge a lottery's capacity to financially contribute to specific areas. Moreover, state higher education systems that receive a lower percentage of lottery proceeds might consider the possibility of allocating funds to areas that would benefit from one-time supplements. For states that distribute a higher percentage of transfers to higher education, SHEEO agencies and policymakers can use these insights to assess their programs' dependency on lottery funds should lottery ticket sales slow. These steps will help state higher education leaders and policymakers avoid viewing lottery earmarks as a uniform policy, advocate for funding parameters that can positively impact overlooked areas, and gain insights on a revenue stream that the SHEF report and dataset do not directly measure.

# STATE HIGHER EDUCATION EXECUTIVE OFFICERS ASSOCIATION

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3035 CENTER GREEN DRIVE, SUITE 100, BOULDER, COLORADO, 80301 • 303.541.1600  
1233 20TH STREET NW, SUITE 360, WASHINGTON, D.C., 20036 • 202.558.2236

**SHEEO.org • SHEF.SHEEO.org**

