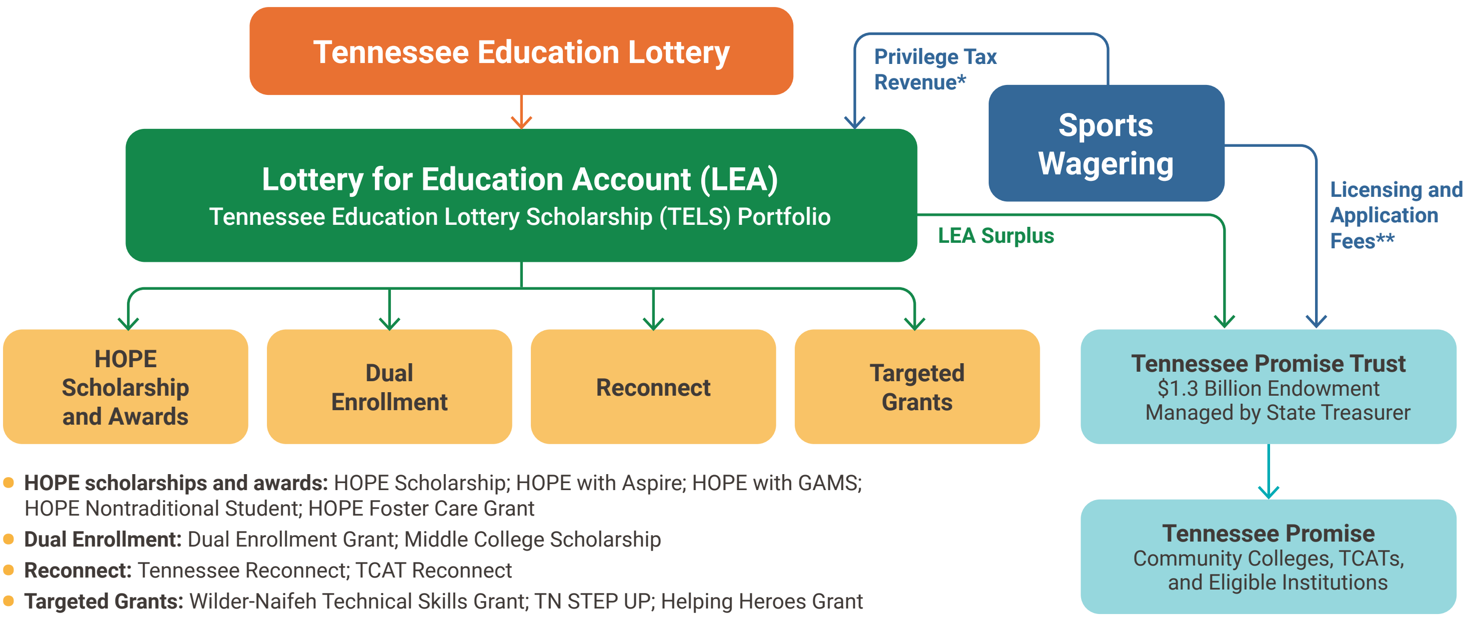
Tennessee's Postsecondary Scholarship System at a Crossroads:

Understanding the Funding Gap

RESEARCH REPORT

Tennessee has built a nationally recognized postsecondary scholarship system that has distributed $4.7 billion (adjusted for inflation) to students statewide in the past 10 years alone.[1] The Tennessee Education Lottery Scholarship (TELS) portfolio includes 13 active programs, with all but one—Tennessee Promise—directly funded by lottery revenue.[2]

The Tennessee Education Lottery Scholarship portfolio relies on net lottery proceeds for funding.



- **HOPE scholarships and awards:** HOPE Scholarship; HOPE with Aspire; HOPE with GAMS; HOPE Nontraditional Student; HOPE Foster Care Grant
- **Dual Enrollment:** Dual Enrollment Grant; Middle College Scholarship
- **Reconnect:** Tennessee Reconnect; TCAT Reconnect
- **Targeted Grants:** Wilder-Naifeh Technical Skills Grant; TN STEP UP; Helping Heroes Grant

Source: THEC, Tennessee Education Lottery Scholarship Program Summary Memo (RDA SW 38), 2026.
Privilege tax revenue from sports wagering directed to LEA when net lottery proceeds are insufficient to cover Tennessee Education Lottery Scholarship shortfalls.
***Licensing and application fees collected by the Sports Wagering Council in excess of operating and administrative expenses.*

While spending on Tennessee's scholarship programs has increased, the lottery revenue funding the programs is shrinking—net lottery proceeds have fallen 21.9% in real terms since FY2022.[3] As demand for the programs continues to rise, Tennessee's scholarship spending is projected to outpace net lottery proceeds.[4] Tennessee policymakers will soon need to make decisions about how to close the widening gap.

"Net lottery proceeds" refer to the money left over from ticket sales after the lottery pays prizes and covers its own operating costs.

KEY TAKEAWAYS

- ✓ Tennessee's scholarship system runs on two funding models—most programs draw directly from lottery proceeds each year, while Tennessee Promise is more insulated by a $1.3 billion endowment.
- ✓ Net lottery proceeds have declined 21.9% in real terms since FY2022, even as scholarship spending and enrollment have both grown.
- ✓ Workforce Pell provides new federal money for short-term programs that may offer a narrow opportunity to ease lottery-fund pressure.
- ✓ Other states facing similar challenges have tried policies targeting revenue and structural reforms.

Lottery proceeds drive most of Tennessee's postsecondary scholarship funding.

In Tennessee, net lottery proceeds flow into the Lottery for Education Account (LEA), funding the Tennessee Education Lottery Scholarship (TELS) portfolio. The TELS portfolio, administered by the Tennessee Student Assistance Corporation (TSAC), consists of 13 active programs serving students pursuing two- and four-year degrees, as well as certificates and credentials for in-demand jobs.[5]

All but one of the scholarship programs are "direct draw" in that they are funded entirely by annual lottery proceeds. Tennessee Promise has a different funding model: its money sits in a roughly $1.3 billion trust made up of two accounts, a $361.4 million *principal account* that cannot be spent, and a *special reserve account* that pays the scholarships and grows or shrinks primarily with investment earnings from the principal account and any lottery surplus left over after TELS needs are met.[6]

The Tennessee Education Lottery Scholarship (TELS) portfolio funds 13 scholarship programs reaching 169,412 students at a cost of $505 million in FY2025.

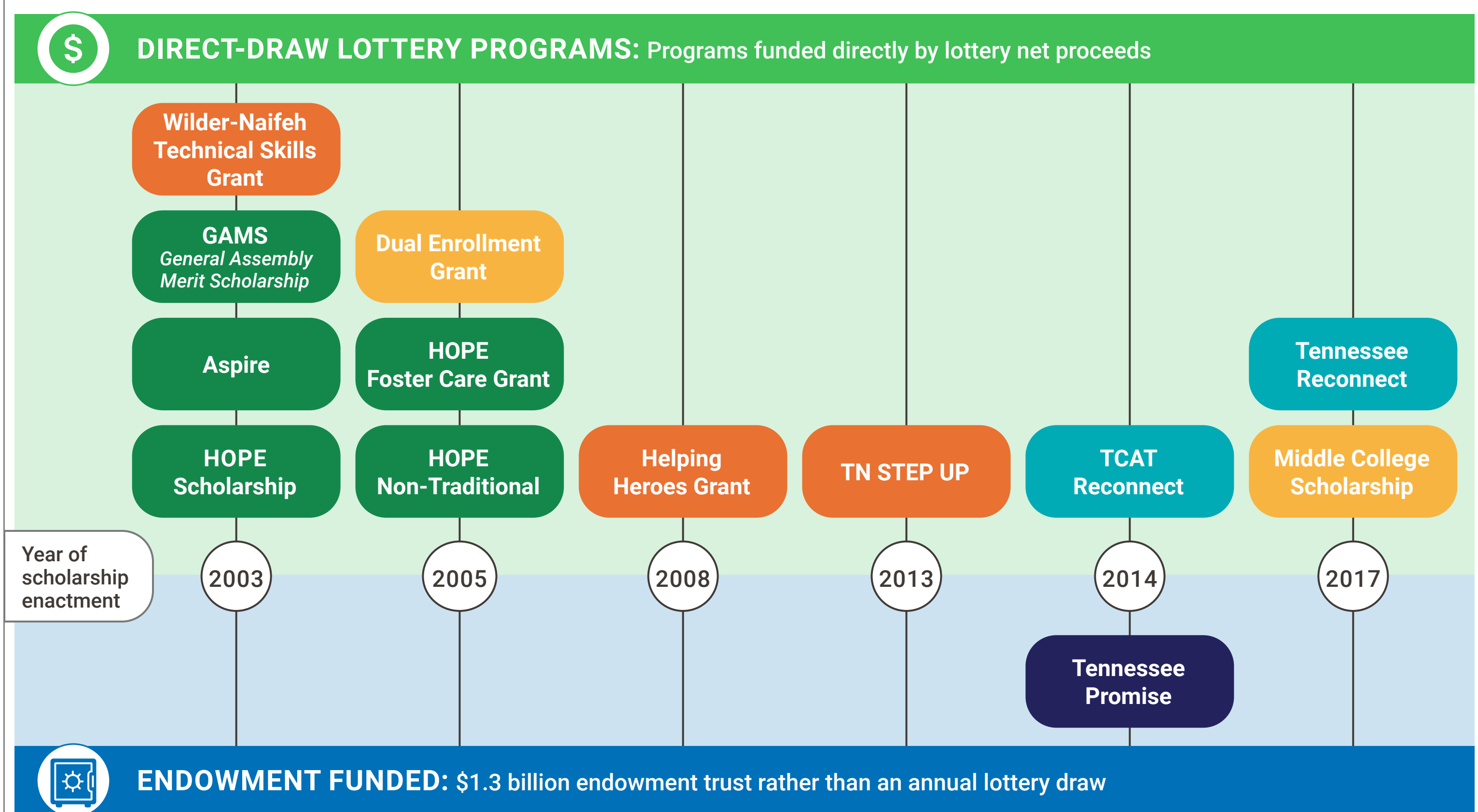
HOPE Scholarships & Awards: Merit-based aid for Tennessee students, with supplements for need, independent status, and foster youth.

Dual Enrollment: Helps high schoolers earn college credit before graduation.

Reconnect: Adult and independent learners returning to community colleges and TCATs—available for all Tennessee residents.

Targeted Grants: TCAT students, students with intellectual disabilities, and veterans.

Tennessee Promise: High school graduates enrolling immediately at a community college, TCAT, or eligible four-year institution.



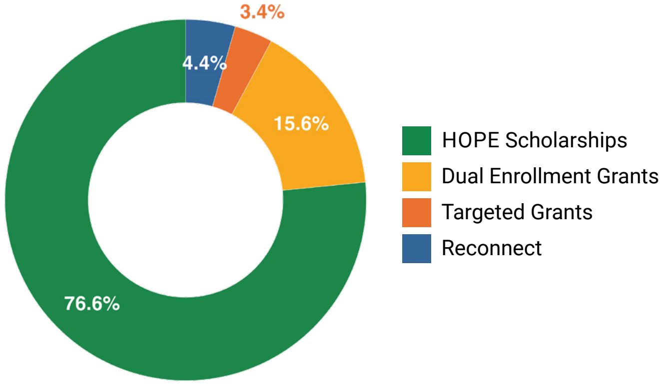
Sources: THEC, 2025 Tennessee Education Lottery Scholarship Report (RDA SW 38), Table 2, 2026b; Appendix A, Overview of the HOPE Scholarship in Tennessee (Iverson, Comptroller of the Treasury/OREA, Sept. 2023).

Tennessee also has additional needs-based grant programs that operate outside of the lottery framework. State general fund appropriations fund the Tennessee Student Assistance Award (TSAA)—currently $125.3 million—as well as a handful of other, smaller state aid programs.[7] Unlike the LEA-funded programs, these programs are structurally insulated from lottery revenue fluctuations.

Lottery revenues are distributed among the 12 direct-draw programs with the largest portion going to HOPE.

The HOPE merit-based scholarship and its supplements account for more than three-quarters of all lottery scholarship spending. In FY2025, the HOPE family of scholarships accounted for 76.6%—$369 million of the $481.8 million—of direct-draw TELS expenditures and served 47.6% (75,264 students) of direct-draw program enrollment.[8]

HOPE scholarships account for the largest share of TELS-funded programs.



Source: THEC, 2025 Tennessee Education Lottery Scholarship Report (RDA SW 38).
Note: Percentages exclude lottery proceeds transferred to the TN Promise account.

The second-largest program by expenditure is the Dual Enrollment Grant (DEG) for high school students. In FY2025, the DEG served 58,078 high school students at a cost of $70.7 million. DEG spending has grown 189% over the last five years, driven largely by expanded eligibility for dual enrollment at Tennessee Colleges of Applied Technology (TCATs). The related Middle College Scholarship, which covers full-time enrollment in an associate-degree program for high school juniors, served 1,239 students at a cost of $4.3 million the same year.[9,10]

The remaining direct-draw programs are far smaller than HOPE or DEG. Tennessee Reconnect and TCAT Reconnect serve adult returners balancing work and family obligations—8,919 students in FY2025 at a combined cost of $21.4 million (4.4% of TELS direct-draw expenditures). Wilder-Naifeh, TN STEP UP, and the Helping Heroes Grant served 12,621 students at a combined cost of $16.5 million (3.4% of TELS direct-draw expenditures).[11]

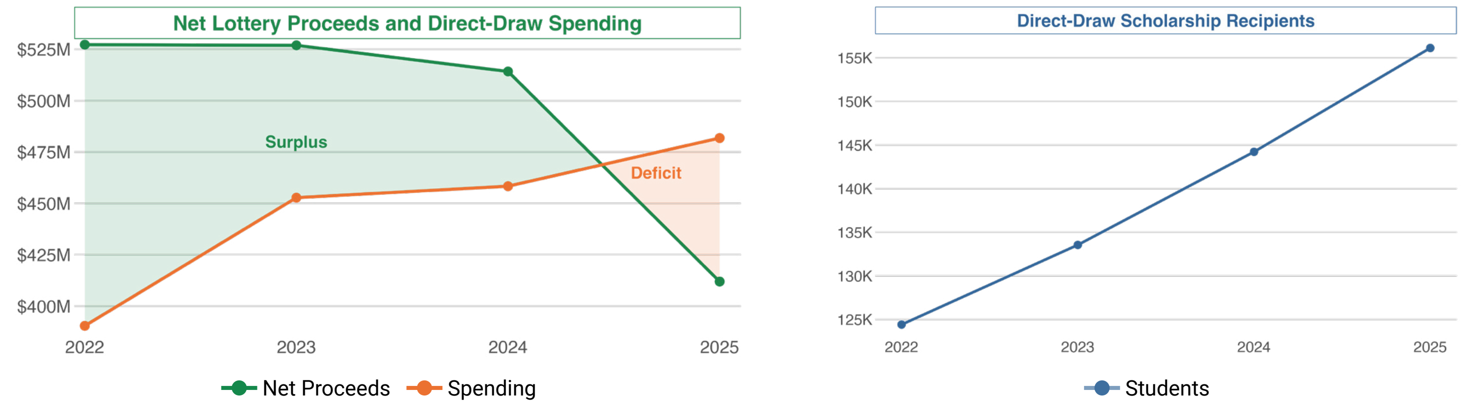
A lottery shortfall and structural changes to how funds are distributed put these programs at risk.

Tennessee's scholarship programs—both the direct-draw TELS and Promise—will be impacted by an anticipated shortfall in lottery revenues and a recent policy change redirecting a previous additional funding source.

Net lottery proceeds have recently decreased, while the number of students drawing on TELS programs has increased.

When adjusted for inflation, from FY2022 to FY2025, TELS net lottery proceeds decreased by 21.9% ($115.3 million)—in the most recent fiscal year alone, proceeds were down 19.9% ($102.2 million).[12] At the same time, spending on TELS direct-draw programs (which excludes Tennessee Promise) increased by 23.4% and the number of student recipients increased by 25.5%.[13,14] In FY2025, for the first time, TELS spending exceeded lottery proceeds.

FY2025 was the first year lottery proceeds fell short of TELS spending—even as scholarship recipients steadily increased.



Source: THEC, TELS Board Report – 2024-2025 AC Year; Tennessee State Funding Board, Meeting Packet (Nov. 3, 2025, "Historical Results" table).

Sports wagering revenue previously supplemented lottery proceeds, but the allocation recently changed.

Until July 1, 2026, 80% of the proceeds from the state's 1.85% sports wagering privilege tax was allotted to the Lottery Education Account.[15] This sports wagering revenue was sufficient to cover the FY2025 deficit and also provided a $3 million net surplus.[16]

However, as part of the 2026 Tennessee Education Freedom Scholarship Act, sports wagering proceeds are now directed to the construction and maintenance of public school (K-12) buildings.[17] If net lottery proceeds fall short of TELS expenditures in the future, the construction and maintenance fund's allocation is reduced dollar-for-dollar to cover the gap.[18] Previously, after TELS needs were met, any remaining funds were allocated to Promise.

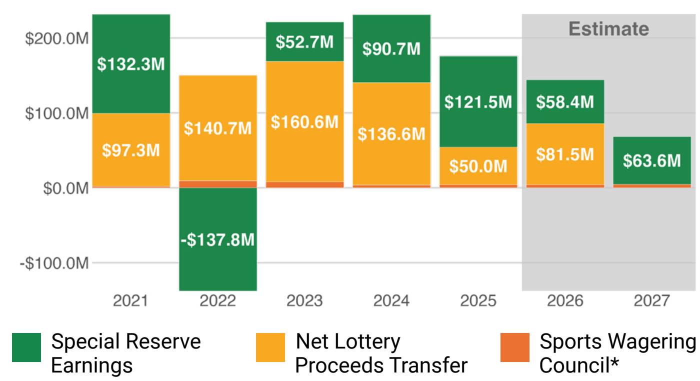
Funding for Tennessee Promise is also set to slow.

Tennessee Promise's special reserve account—which pays for the Promise scholarships—receives any lottery proceeds that remain after funding TELS scholarships. Even though Promise is not directly funded by lottery proceeds, a decline in lottery revenues can mean declining surpluses left over to allocate to the reserve account.

As of FY2026, transfers from the Lottery for Education Account were capped regardless of the size of any future surplus—Promise cannot receive more than $10 million a year. In the four previous years (FY2022-FY2025), surplus transfers ranged between roughly $124 million and $151 million.[19]

According to estimates from the governor's budget for FY2027, Tennessee Promise's special reserve fund will continue to have a surplus for the next two fiscal years—meaning that estimated revenues would sufficiently cover upcoming spending. However, expenditures are estimated to increase by 17.2% from FY2025 to FY2027, while total revenues would decline by 61.2%—this decline reflects net lottery proceed transfers into the special reserve account ending in FY2027, as the lottery account no longer generates a surplus to transfer.[20]

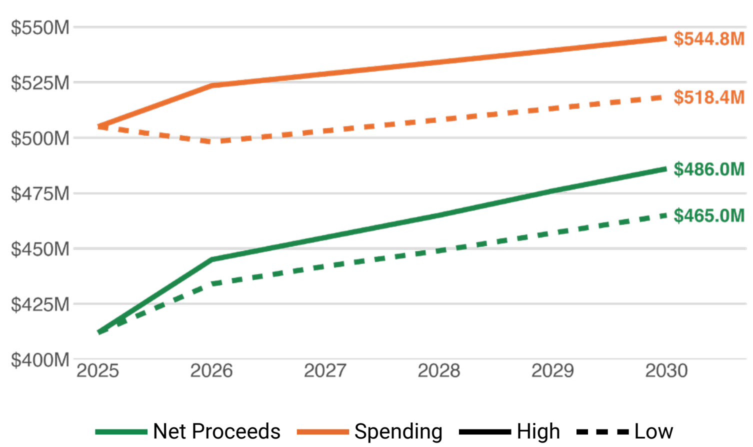
Lottery proceed transfers have been a key funding source for the Tennessee Promise Endowment Fund.



Source: Source: State of Tennessee, FY2022-23–FY2026-27 Governor's Budget.
**Licensing and application fees collected by the Sports Wagering Council in excess of operating and administrative expenses.*

Lottery proceeds are projected to grow, but not fast enough to meet scholarship spending needs.

Scholarship spending is projected to outpace net lottery proceeds through FY2030.



Source: Tennessee Education Lottery Corporation; Tennessee Higher Education Commission, as presented to the Tennessee State Funding Board (Nov. 3, 2025). Figure excludes Tennessee Promise spending.

Between FY2025 and FY2030, the Tennessee Education Lottery Corporation (TELC) and the Tennessee Higher Education Commission (THEC) project that net lottery proceeds will grow faster (between 12.9% and 18.0%) than TELS spending on direct-draw programs (between 7.7% and 13.2%). Even so, spending is forecast to exceed proceeds every year through FY2030, producing a cumulative shortfall.[21]

Because Tennessee Promise is a last-dollar scholarship—meaning it covers whatever tuition and mandatory fees remain after other scholarships have been applied—reductions in TELS funding could increase the number of students receiving Promise funding.

Workforce Pell may offer a narrow opportunity to ease lottery-fund pressure.

A new federal program created by the Working Families Tax Cuts Act, Workforce Pell, extends federal Pell eligibility for the first time to certain short-term TCAT-style programs.[22] The number of TCAT programs eligible for this financial support is not yet known, leaving the grant's impact on Tennessee's lottery revenue shortfall unclear.

Workforce Pell eligibility is federally defined—Tennessee still has to build the pipeline.

Program Length
150-599 clock hours, or
4-15 semester hours; or
6-23 quarter hours

Duration
8-14 weeks

Credentials
Stackable and **Portable** or **the sole recognized credential for the field**

Post Completion Rate
70%

Job Placement Rate
70%

Source: Tennessee State Workforce Development Board. (2026, June 23). Workforce Pell Grant Framework.
Note: This figure summarizes the criteria most relevant to Tennessee's short-format programs. Full eligibility requirements, including institutional eligibility and program cost/earnings tests, are detailed in the SWDB Workforce Pell Grant Framework.

Tennessee Skills Coalition

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Institutions apply directly to Tennessee's State Workforce Development Board (SWDB)—which acts on the governor's behalf. Each program is required to show that employers actually want to hire its graduates and that it fits an in-demand, high-wage field. The SWDB certifies eligible programs at its quarterly meetings.[23]

Other states facing similar challenges are addressing them with revenue and structural alternatives.

Lotteries have long appealed to policymakers nationwide as a way to expand funding for public priorities such as financial aid without raising taxes. In FY2025, five states—Florida, Georgia, Kentucky, South Carolina, and Tennessee—relied on non-tax sources, including lottery revenue, for over 15% of total higher education funding.[24,25]

States facing similar lottery pressures have tried various alternative options that can be categorized in one of two ways: **revenue-side options** that could supplement the lottery with additional dollars but may not fully close the projected gap alone, or **structural options** that review which programs make sense and potentially change how award amounts or the scholarship portfolio are set.

Revenue-side options add new dollars

Lottery modernization. Other state lotteries differ from Tennessee's on two fronts: they allow retailers to accept debit cards—legislation proposing this in Tennessee was introduced but not discussed in 2018—and they offer digital instant games ("e-Instants").

✓ **South Carolina's** debit card sales launched in July 2025. Debit-accepting retailers saw sales 7.5% higher than cash-only retailers through the first half of FY2026—an estimated $11.6 million in added transfer value to the Education Lottery Account, though this overlapped with an unusually large run of jackpots.[26]

✓ **North Carolina's** Digital Instants launched in November 2023 and posted $2.6 billion in sales in FY2025—nearly 40% of the state's lottery sales. But allocations to the state's Education Lottery Fund still dipped slightly, from $1.07 billion to $1.05 billion, even as total sales grew from $5.4 billion to $6.6 billion.[27]

A general fund appropriation alongside the lottery. Tennessee already supports the Tennessee Student Assistance Award (TSAA) grant with general fund appropriations separate from the lottery. Some states supplement their lottery-funded scholarship programs with general fund allocations.

✓ **South Carolina's** top-tier Palmetto Fellows award is primarily funded by lottery funds—contributing $67.3 million in FY2024—and also receives a fixed $12 million-per-year general fund allocation. If funding falls short of the need, state law automatically appropriates whatever additional general fund amount is necessary to provide scholarships to all students meeting the requirements.[28]

✓ **West Virginia's** PROMISE Scholarship Fund combines lottery and video lottery revenue with a separate general revenue appropriation channel to reach a statutory funding target—set at $47.5 million annually since FY2011.[29]

Formal review of financial-aid program alignment. Some states have directed legislative studies of how their scholarship and grant programs interact—though these reviews have focused on eligibility alignment and access barriers rather than consolidation for budget savings.

✓ **Louisiana's** 2024 Senate Resolution 138 directed its Board of Regents to study eligibility alignment across five state financial-aid programs. The resulting 2025 report recommended aligning eligibility rules and adjusting how aid is sequenced against other funding, but its recommendations largely called for increased appropriations rather than program consolidation.[30]

Structural options change how existing dollars are allocated

Fixed, or formula-based scholarships. Rather than guaranteeing full tuition coverage, some states have set award amounts on a fixed or formula basis—via legislative appropriation—so scholarship costs no longer rise automatically with tuition.

✓ **New Mexico's** 2018 Senate Bill 140 replaced its full-tuition guarantee with a flat award amount that varies by institution type—such as two-year versus four-year institutions—rather than tracking each school's actual tuition.[31]

Tennessee will soon have to address balancing current funding pressures with increasing eligibility and enrollment in its nationally recognized postsecondary scholarship programs. Policymakers don't need to choose between funding today's students and building tomorrow's stability—but they will need to decide what balance the state can afford.

References

1. All figures are inflation adjusted using the CPI-U Index to reflect FY2025 dollars.
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15. Tennessee Higher Education Commission. (2026a, February 20). *Tennessee Education Lottery Scholarship Program Summary* (RDA SW 38), p. 2.
16. Tennessee Higher Education Commission. (2026b, February 20). *2025 Tennessee Education Lottery Scholarship Report* (RDA SW 38), p. 5.
17. Tennessee State Funding Board. (2025, November 3). *SFB Minutes*, p. 3.
18. The LEA has a shortfall reserve subaccount of $100,000,000 that, if used in a fiscal year, must be replenished the following fiscal year. There is an additional $10,000,000 in the general shortfall reserve subaccount that does not need to be reinstated if used. According to the new legislation, sports wagering funds would be used prior to leveraging the reserve subaccount funds. TN Code § 4-51-111(b)(3)(C).
19. Tennessee General Assembly, Fiscal Review Committee. (2026, February 21). *Fiscal note: HB 2106/SB 2159*.
20. Governor's Office, State of Tennessee. (2026). *The budget document: Fiscal year 2026–2027* (Vol. 1), p. A-41, Tennessee Promise Last Dollar Scholarship Multi-Year Projection.
21. Tennessee State Funding Board. (2025, November 3). *State Funding Board meeting packet*, pp. 174-175.
22. Workforce Pell was created by provisions in the Working Families Tax Cuts Act of 2025. Some federal sources refer to the same law as the One Big Beautiful Bill Act (OBBBA).
23. Tennessee State Workforce Development Board. (2026, June 23). *State Workforce Development Board policy: Workforce Pell Grant Framework* (Sections 1 & 8). Tennessee Department of Labor and Workforce Development. Effective July 1, 2026.
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25. Brown, P. (2023). *SHEF: FY 2022 Issue Brief: Analyzing Lottery Proceeds as an Aspect of State Support for Higher Education.* State Higher Education Executive Officers Association.
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Tennessee Skills Coalition is a statewide coalition working to address policy barriers that limit Tennesseans' access to jobs that require skills training beyond high school.

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