

The Executive Budget

Fiscal Year 2009-10



January 9, 2009

Submitted by
Mark Sanford
Governor
State of South Carolina

to the
118th General Assembly of South Carolina,
First Session



State of South Carolina

Office of the Governor

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January 9, 2009

To the Citizens of South Carolina and the Members of the South Carolina General Assembly:

In the pages that follow is this administration's FY 2009-10 Executive Budget, and it is my earnest hope that it serves as a starting point in this year's difficult deliberations over the budget.

Our goal in this executive budget and each of the last five remains consistent - to present to the General Assembly a balanced state budget that, without raising taxes, provides essential services to the citizens of South Carolina in the priority areas of education, health care and social services, economic development, public safety and natural resources. However, reaching this goal was difficult given the serious financial challenges facing our state.

Regrettably, the FY 2009-10 Executive Budget we present makes cuts that we would not have *chosen* to make, but are now *forced* to make because the majority in the Legislature chose not to use this administration's recommendations, as set forth in five previous executive budgets, that would have kept our fiscal house on more solid footing to better manage the current national economic decline. These budgets provided a blueprint to build a stronger financial foundation by limiting spending growth, reorganizing our inefficient and unaccountable structure and using results-based budgeting practices. When economic times were good, calls for fiscal restraint were roundly ignored. In the hope that crisis creates opportunity, we renew our call once again to adopt a course of sustainable spending rather than go through these tough and damaging cuts as revenue rises and falls.

What is happening with our state's finances has certainly been amplified by events in the global economy. But to be clear, the situation we find ourselves in was predictable, preventable, and, in many ways, guaranteed based on the run-up in state spending we've seen over the past several years. Prior to the various mid-year reductions, South Carolina's state government had grown by 43 percent since 2004, ***leading*** the Southeast in year-to-year government growth. Our state also continues to have outstanding liabilities of almost \$20 billion. In FY 2006-07 and FY 2007-08 combined, the General Assembly spent an ***additional \$1.3 billion in surplus revenues***, which our proposed population plus inflation spending cap, if adopted by the Legislature, would have prevented nearly all of the mid-year cuts to date and would have done far less damage to our government than the current cuts. While the opportunity to act will no longer prevent massive spending cuts, we do believe that such spending limits could prevent this problem in future years. As a result, it is critical that the General Assembly finally adopt legislation limiting spending.

The following pages lay out this administration's spending and policy initiatives. From a spending perspective, the FY 2009-10 Executive Budget prioritizes \$5.8 billion in spending by breaking down each activity in government, ranking them to adequately fund our most critical and effective services, and identifying cost savings measures. Our budgeting approach is based on the performance and results of each agency activity rather than on subjective, agency-driven or political considerations. With this budget we again seek to limit annualizations which continue to harm the financial stability of our state. Simply put, using one-time revenue to pay for recurring services is not a sound way to operate the state. The FY 2008-09 Appropriations Act contained about \$270 million in annualizations, starting us effectively that much further in the hole. Over the last two years, we have proposed limiting annualizations to no more than one percent of the total budget and we repeat that call again this year.

From a policy perspective, we continue to push for a reformed tax code so that we are more competitive with regard to economic development, a reformed education system that provides more choices to parents and puts more dollars into the classroom, a restructured state government that is more efficient and accountable to the taxpayer, a reformed retirement system that helps repay \$20 billion in outstanding liabilities, and improvements to the quality of life for all South Carolinians.

We believe that a flatter, simpler, and lower income tax rate is vital if we are going to attract jobs and investment to the state. In particular, we believe it is time to simplify our overall tax code. To this end, we are recommending two things. One, use the current economic development incentives that relate to corporate income tax to eliminate that tax on all businesses – becoming only the fifth state in the United States to do so. The plan would phase down the corporate income tax over ten years and would ultimately be used to retain current and attract prospective businesses to South Carolina. Two, give South Carolina taxpayers the option of paying a 3.65 percent flat income tax. In turn, we are proposing to offset the decrease in income tax revenue with a cigarette tax increase to 37 cents, implementing a \$3 per ton tipping fee, and eliminating our state's three sales tax holidays. Amid the current economic challenges, this reduced corporate rate, optional rate and simplified code will allow income tax dollars to be invested more efficiently through the private sector, rather than flow through Columbia.

We are also again calling for the General Assembly to enact comprehensive restructuring legislation that would increase accountability to the taxpayers and reduce duplicative government. Fractured government with limited accountability does not serve the taxpayers' interests. According to *Governing* magazine's Fact Book, South Carolina government operates with a ratio of 234 state employees per 10,000 residents – 35 percent higher than the U.S. average of 174 state employees per 10,000 in population. The costs associated with this unusually high ratio of state employees take dollars away from direct benefits for the citizens served by South Carolina government and demand more in the way of funding from taxpayers. Duplication, waste and unaccountability are unacceptable given the limited resources we have to fund basic, critical services.

Maintaining funding for teachers and the classroom remains a high priority in our executive budget, even with significantly less resources. Accordingly, we propose giving local school districts flexibility to put education dollars in the classroom by restoring the recent cut to the base student cost. Fewer state resources does not mean that quality should suffer; but rather it presents an opportunity to ensure that every student has access to high-quality instruction. In addition, we believe that parents and children should have a path out of failing or low performing schools in South Carolina and again urge the General Assembly to enact greater choices for them. In 2007, 42 percent of

South Carolina public schools were deemed “Unsatisfactory” by the Education Oversight Committee’s School Report Card. Until we can ensure that every student has access to a high-quality education, parents should have the freedom to enroll their children in a school that gets the results they need right now.

Providing basic health care services to our state’s most needy citizens also remains a high priority for our administration. Accordingly, we propose to fully fund the maintenance of effort for the Medicaid program, recognizing that demand grows when the economy weakens. Last year, the General Assembly chose to do a couple of things that hampered the Department of Health and Human Services’ (DHHS) ability to provide Medicaid services to these citizens. First, over our objections, they raided the agency’s reserves of over \$100 million to pay for other operations, rather than use it to address the expected growth in the program. Next, the Rescissions Appropriations Act passed in October also carved out several exceptions leaving DHHS to more stringently cut direct service programs when the Budget and Control Board imposed across-the-board cuts in December. As such, we ask that the General Assembly fund the Medicaid maintenance of effort in FY 2009-10.

Finally, this executive budget pays down the \$45 million deficit that the Department of Corrections will incur, due to a lack of sufficient funding by the General Assembly. For too long, the Department of Corrections has been asked to safely incarcerate inmates with less funding per inmate than nearly any other jurisdiction in the nation. We call upon the General Assembly to fully fund the Department of Corrections in FY 2009-10.

The above recommendations highlight only some of the changes we believe will afford long-term benefits to the people of this state. Imposing a limit on spending and acting on a plan to repay outstanding state debt is essential if South Carolina is to return to a course of fiscal stability. We present this budget, the result of hundreds of man hours by citizens from around the state, and urge you to join us in setting state government on a path toward greater affordability and accountability.

I would like to express my thanks to all who gave time, talents, and focus to this effort, and I look forward to working with the General Assembly on ways we can make such initiatives work for the taxpayers of South Carolina.

Mark Sanford

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Executive Summary

Executive Summary

Regrettably, the FY 2009-10 Executive Budget we present makes cuts that we would not have *chosen* to make, but are now *forced* to make because the majority in the Legislature chose not to follow many of the recommendations set forth in our five previous executive budgets that would have kept our fiscal house on more solid footing to better manage the current national economic decline. These budgets provided a blueprint to build a stronger financial foundation by limiting spending growth, reorganizing our inefficient and unaccountable structure and using results-based budgeting practices. When economic times were good, calls for fiscal restraint were roundly ignored. In the hope that crisis creates opportunity, we renew our call once again to adopt a course of sustainable spending rather than go through these tough and damaging cuts as revenue grows and falls.

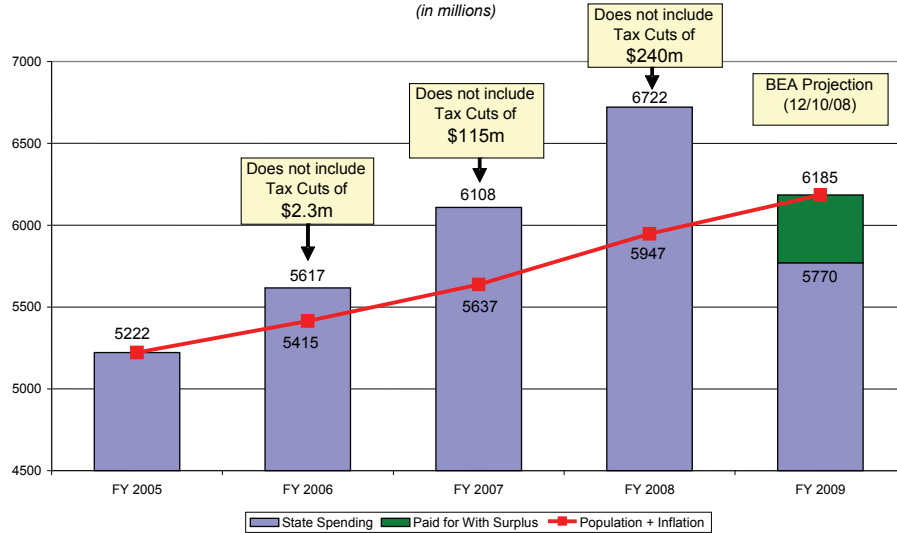
Objectives

While the objectives of this executive budget strike a similar tone to the five previous, the current economic situation at both a national and state level makes this year's budget that much more important for the way we deal with less revenue coming into government and more demand for many government services. Our first goal is to present to the General Assembly a balanced state budget that does not raise taxes and at the same time funds essential services for South Carolinians in the priority areas of education, health care and social services, economic development, public safety, and natural resources. This budget also provides us a chance to highlight several policy items we intend to push this coming year.

South Carolina families, along with our state and nation as a whole, face economic times more challenging than any in recent memory. The collapse of the credit, housing, and stock markets, and, in turn, the belt-tightening in government budgets at the state and local level diminishes the capacity to which government is able to serve citizens. Accordingly, we have had to reprioritize spending by making painful cuts, but we also have a unique opportunity to fundamentally change the way we, as a state, budget taxpayer money.

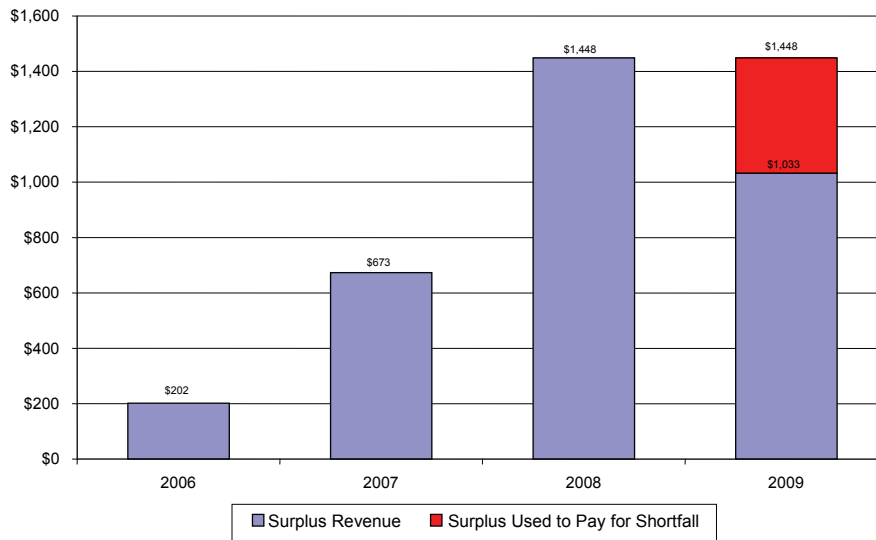
Take, for instance, our administration's repeated calls for spending caps – in essence, limiting budget writers to growing government by at most population plus inflation, or some other recognized measure, each year. The argument for spending caps is both theoretical in that there is always a bias for politicians to increase spending no matter if it's a year of feast or famine, and practical, since having this cap in place during the past five years would have mitigated the severe cuts to government of the past few months. In the end, the chief aim is to set a more sustainable spending pattern over the entire course of a business cycle to avoid damaging cuts in the down years.

State Government Growth - Just Recurring Dollars
FY 2005 – FY 2009
(in millions)



It is important to point out that in the years leading up to the current year, there were *excess funds over the population plus inflation cap*.

Surplus Revenue Under Population + Inflation Spending Cap
(in millions)



Our point is that these monies should have gone into a long-term rainy day fund or toward paying down the state's unfunded liabilities of over \$20 billion, or sent directly back to the taxpayers – the best economic stimulus of them all. Unfortunately, our argument for fiscal prudence was met with

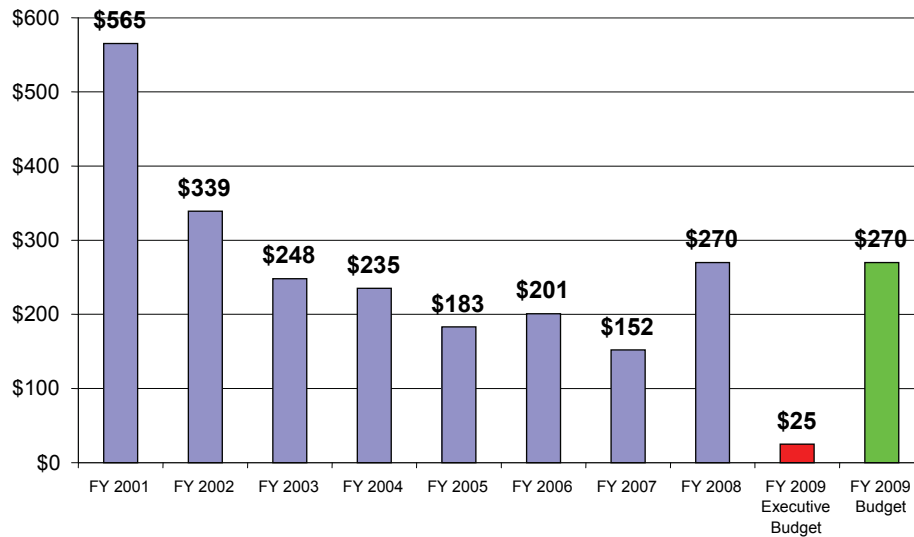
silence or, even worse, ridicule from some powerful players in the budgeting process. The legislative budget writers' failure to respond to our calls for fiscal discipline has created an unstable financial condition for our state that demands change in the way we approach budgeting the taxpayers' money. Accordingly, we believe that we need to capitalize on the current economic challenges and finally institute some common-sense budgeting principles that will go a long way toward making state government spending more sustainable in the future and make South Carolina more competitive in the global marketplace.

Administration Goals

To improve South Carolina's competitive advantage globally and ensure that government spending does not grow at an unsustainable level, the administration has laid out seven major budget goals for the FY 2009-10 Executive Budget. Adhering to these goals, we have prioritized and funded the state's critical needs, while keeping the taxpayers' best interest in mind and retaining the fiscal discipline demanded by organizations such as national bond rating companies. Our seven goals for the FY 2009-10 Executive Budget are as follows:

1. **Limit the annual growth of general fund spending by not exceeding population growth plus the rate of inflation.** Echoing the thoughts above, this administration believes in the fundamental idea that government should not grow faster than the taxpayer's ability to sustain it over time. We believe a spending cap would have better controlled government spending that grew by 40 percent over the previous four years, a rate many times faster than the growth of the underlying economy. As evidenced by the painful spending cuts we are making now, it should be very clear that we cannot grow government faster than people's ability to pay for it without it catching up with you at some point. To that end, we are calling for legislation to limit spending increases to the growth in population plus inflation. Similar measures have passed the House numerous times, and one sponsored by Senator Glenn McConnell was narrowly defeated in the Senate just this past year.
2. **Limit annualizations to one percent of revenue.** To put our state's fiscal house in order, we must stop the practice of annualizations – using one-time money to fund recurring needs. Annualizations represent borrowing from Peter to pay Paul and, ultimately, only serve to delay tough decisions by putting off budget pain for another year. This problem is evident as annualizations nearly doubled in the preceding two years, making the hole we have to climb out of this year even deeper. With the passage of the FY 2008-09 Appropriations Act, we were concerned that the General Assembly had pushed the state's annualization total for the year back to a seven-year high of around \$270 million – ultimately meaning South Carolina is starting the next fiscal year in a very deep hole that has grown deeper with the declining national economy. This proposal is modeled on the Florida Constitution that limits annualizations to three percent of revenue, requiring a three-fifths vote of both Houses to exceed that limit.

South Carolina Annualizations Since FY 2000-01



We believe there needs to be a limit on annualization spending, which is why we continue to ask that annualizations not exceed one percent of total estimated revenue for a fiscal year. This executive budget falls below this level at only \$32.8 million, 0.52% percent of the total revenue.

3. **Provide tax cuts for individuals and businesses to spur investment and job creation.** There has never been a more important time to discuss where we want to go as a state with respect to growing our economy. We believe staying competitive amid today's challenges means two things. One, a lowered and flattened income tax would represent a significant step toward making our state more attractive and improving our competitive position when it comes to growing our economy. Two, we have to get away from our current piecemeal approach to economic development that selectively provides tax incentives to some businesses but not to others. We believe a better approach would be to simply lower the overall tax rate for corporations, so that we are not only giving companies a good deal when they decide to locate here but also a reason to stay and expand. This is particularly important to avoid the unintended consequence that comes with much of today's incentives system, wherein we have one set of incentives for businesses coming into our state, and much less in the way of help for small and mid-size businesses already here in our state to invest and grow.

To this end, we are recommending a three-part proposal to spur job creation and capital investment. The plan is as follows:

- First, enact an optional income tax cut of nearly 50 percent, cutting the state's top marginal rate from the current 7 percent to a flat 3.65 percent. We also believe in fully indexing the income tax brackets. The cut would be offset by a 30 cents per-pack increase to the state's cigarette tax, a new

\$3 per-ton tipping fee for landfill dumping, and elimination of the state's three sales tax holidays.

- Second, implement a 10-year phase out of the corporate income tax from the current 5 percent to 0. The cut would be offset by transitioning from most corporate tax exemptions and some business incentives over that same 10-year time period.
- Third, form a committee to evaluate the inequities in the current property tax structure that adversely impact businesses.

4. **Appropriate funds based on a rational assessment, from the citizen's perspective, of the relative importance of the activities of government.** To prioritize and then provide for the core needs of the state, we again are utilizing the Budgeting for Results process that we established during FY 2005-06. In preparing our executive budget, we held a series of budget discussions, open to the public and the press, with directors of state agencies throughout South Carolina to discuss better and more efficient ways to achieve our state's budgetary goals.

In addition to public budget hearings, we worked with our "results teams" made up of state employees and volunteers from the private sector to compile a list of more than 1,600 activities performed in our state. Using the Budgeting for Results process, we then worked with the results teams to rank all of these activities as they relate to the core outcomes we think government should provide. Instead of "funding" agencies, we "purchased" the activities and outcomes we believed would deliver the greatest results for our citizens.

This year preparing the executive budget presented a difficult challenge due to the dramatic and unprecedented drop in revenue. Many cost savings were found and many tough choices were made to ensure that our state's essential services were adequately funded.

Through these actions, our proposed budget recommends over **\$266.6 million in specific general fund savings** to the taxpayers through operational efficiencies realized by state agencies and by not purchasing lower priority activities.

We are also recommending purchasing higher priority activities in the areas of education, health care and social services, economic development, public safety, natural resources, and, finally, constitutional and statewide needs described as follows.

a) **K-12 Education – \$2.23 Billion General Funds/\$3.57 Billion Total Funds –**

To provide for the state's K-12 needs during FY 2009-10, we propose giving local school districts the flexibility they need to put education dollars in the classroom by restoring funding for the base student cost to \$2,339. This funding also holds teacher salaries harmless; however, we once again propose that teachers be rewarded based on results in the classroom or their willingness to teach core subjects in critical needs areas and not simply on their longevity. In this budget, K-12 represents 38.7 percent of general fund spending. A key function of the K-12 educational system is to prepare students for college, work

and life. Unfortunately, the quality of education that many of our students receive is far from what will prepare them for life in today's ever-changing global economy. To better prepare our students, we have established five goals that can be achieved through the activities we purchase in our budget: increase the high school completion rate; increase participation and achievement in rigorous courses; raise the national performance ranking of South Carolina's students on the SAT, ACT and NAEP; eliminate the achievement gap; and improve the efficiency with which education dollars are spent.

To achieve these goals, we propose supporting the following activities:

- **Restoring funding to the base student cost: \$2,339.**
- **Concur with the proposal of State Education Superintendent Jim Rex and the EOC to preserve average teacher salaries at \$47,376, while rewarding performance and willingness to teach core subjects in critical needs areas.**
- **Funding Education and Economic Development Act obligations to provide our students with the tools they need to choose a career path that will prepare them for today's competitive world: \$29.3 million.**
- **Rewarding students who graduate earlier than the traditional four-year high school program with a scholarship: \$1.2 million**
- **Funding Student Health and Fitness Act obligations: \$31 million. We will also support FitnessGram assessment which will continue to help fight childhood obesity.**
- **Providing South Carolina's "Below Average" and "Unsatisfactory" schools the flexibility to pursue innovative programs that will help them overcome the obstacles that have limited their success.**
- **Offering school choice to students in chronically underperforming schools. The Education Oversight Committee recommends, and we concur, that our students in 151 underperforming schools should be able to attend another school of their choice. This model requires no additional funding, as the EOC proposes that state per-pupil funding follows the child to the school they choose to attend. This also supports our goal of driving dollars directly to where they are needed most: the classroom.**
- **Expanding public school choice options for students by providing funding for the South Carolina Public Charter School District: \$860,000.**
- **Funding for 4K Child Development Education Pilot Program: \$21 million.**
- **Funding school bus operations: \$94.6 million.**
- **Funding to lease school buses: \$8.4 million.**

- b) **Higher Education and Cultural Resources – \$614.7 Million General Funds / \$4.04 Billion Total Funds** – Our primary goal for higher education is to provide a quality education at an affordable price. Achieving these goals will be challenging given the fragmented system of 33 public colleges and universities that operate independently with little coordination and oversight. Adding to these challenges is the current economic downturn coupled with a recent national rating of “F” in college affordability by the National Center for Public Policy and Higher Education. Having a postsecondary program serves little purpose if our students cannot afford to participate.

We believe accessibility and affordability of our higher education system should be at the forefront of our executive budget, which is why we are increasing funding for our needs-based scholarships and maintaining the total funding to the state’s other scholarship programs:

- **Needs-based scholarships** for total funding of \$17.8 million.
- **LIFE Scholarships** for total funding of \$148.7 million.
- **Palmetto Fellows Scholarships** for total funding of \$37.4.

- c) **Health Care and Protections of Children and Adults – \$1.5 Billion General Funds / \$9.2 Billion Total Funds** – South Carolina is currently ranked 42nd in the nation in the overall health status of its citizens. One of our primary goals is to meet the maintenance of effort (Medicaid) for core health benefits to our most vulnerable citizens. We also need to continue preventing and treating substance abuse. Since the prevalence of smoking ranks our state 37th in the nation with 23 percent – a slight increase from 36th a year ago at 22.5 percent – we need to continue our focus on chronic disease prevention. With that in mind, we remain concerned that South Carolina ranks 6th in adult obesity, 18th in heart disease, and 1st in the stroke death rate. Moreover, in 2007, 16 percent of our population lacked health insurance. With such serious health concerns, during FY 2009-10, we propose health care spending as a percentage of the total budget at 25.9 percent. Specifically, to provide support for the state’s health care and protections of children and adults during FY 2009-10, we propose:

- **Maintaining maintenance of effort (Medicaid) for core health care benefits for the poor, elderly, and persons with disabilities through the Department of Health and Human Services: \$137.3 million.**
- **Preventing and treating substance abuse by funding chemical dependency community-based prevention and treatment services: \$8 million.**
- **Continuing our focus on chronic disease prevention at the Department of Health and Environmental Control: \$2.21 million for chronic disease prevention.**
- **Continuing development of the Child Support Enforcement System and the Family Court Case Management System: \$17.5 million.**

d) **Economic Development – \$43 Million General Funds / \$1.58 Billion Total Funds** – As South Carolina faces persistent competition from all over the world,

we continue to succeed in attracting new business and encouraging existing businesses to grow and be competitive in an ever-changing marketplace. We believe that with the right soil conditions, South Carolina can flourish in attracting capital and creating new jobs. Much of this groundwork has already been done by this administration and our Department of Commerce. As a case in point, more than 132,000 South Carolinians are working now than when we took office in 2003. Nevertheless, with a rapidly changing world, there is always room for improvement. Specifically, to assist with the state’s economic development during FY 2009-10, we propose:

- **Eliminating our corporate income tax which, coupled with our flat tax and indexation of tax brackets proposal, would move us from 25th to 6th in terms of overall best Business Climate in the country, according to The Tax Foundation.**
- **Implementing an optional income tax of 3.65 percent and fully indexing our tax bracket to inflation for total tax relief of \$133 million.**
- **Funding \$5.1 million in interest owed on the \$161 million federal loan for unemployment compensation benefits requested for the Employment Security Commission.**
- **Funding Local Workforce Investment: \$79.6 million.**
- **Exploring with the Department of Transportation all opportunities regarding the creation of public-private partnerships for the building, operation, and maintenance of our highways.**
- **Repealing the special incentives granted to retailers like Cabela’s and Bass Pro Shop.**

e) **Public Safety – \$593 Million General Funds / \$1.06 Billion Total Funds** –

Our administration has made “quality of life” in South Carolina a priority. South Carolina provides a unique look and feel that most other states and countries cannot provide. At a fundamental level, however, no factor is more important when discussing quality of life than the ability of citizens to live free from crime and unnecessarily harsh results of natural or man-made disasters. South Carolina is fortunate to have committed troopers, officers, and employees working in its public safety agencies. Despite these efforts, South Carolina continues to face many challenges in the area of public safety, demonstrated by crime, natural or man-made disasters, and accidents at rates higher than most of its Southeastern neighbors.

Specifically, to assist with the state’s public safety needs during FY 2009-10, we propose supporting the following activities:

- Paying down the deficit at the Department of Corrections created by a lack of adequate funding by the General Assembly: \$45 million.
- Maintaining the current level of funding at the Department of Public Safety, allowing Highway Patrol officers to provide greater highway traffic enforcement and to further reduce the response times to collisions: \$68.8 million.
- Maintaining funding for the state's seven high-security, eight medium-security, eleven minimum-security, and three female institutions: \$342.7 million.
- Maintaining funding for community supervision of 49,797 adult jurisdictional offenders: \$18.6 million.

- f) **Natural Resources – \$70.25 Million General Funds / \$322 Million Total Funds** – South Carolina is blessed with beautiful expanses of timberland and shoreline teeming with wildlife. With this blessing comes the considerable responsibility of preserving our natural resources. We must be careful to ensure that short-term gain does not overcome our state's long-term goals. Although we recognize that our current budgetary circumstances will limit our conservation efforts over the next year, we plan to use our best efforts to safeguard South Carolina's natural beauty.

To provide for the state's natural resource needs during FY 2009-10, we recommend funding for the following activities:

- Preserving historic sites and natural resources by redirecting a portion of film incentive funds to the Conservation Bank: \$4.9 million.
- Monitoring and preserving South Carolina's marine infrastructure: \$801,470.
- Protecting and managing water resources: \$1.2 million.

- g) **Improve Central State Government Support – \$528 Million General Funds/\$788 Million Total Funds** – Government should be accountable to those who pay for it – the taxpayers. This administration continues to push for policies that will provide an efficient and effective government that maximizes value to the taxpayers. In this section of the budget, we will look at ways to improve the structures and policies of central state government and other governmental services in an effort to propose ways that might make them operate more efficiently and effectively. To this end, we propose that the General Assembly adopt the Government Efficiency and Accountability Review (GEAR) Committee recommendations that will reduce cost, increase accountability, improve services, reduce duplication, and allow South Carolina to become more competitive in a world economy. To date, only 16 out of the 61 of the GEAR Committee's recommendations have been adopted, which means that the General Assembly has ample opportunity to obtain cost savings without

cutting essential governmental services by adopting the remainder of the recommendations. Given the dramatic downturn in the economy and the state's fiscal condition, it is time the General Assembly gives proper consideration to all of these recommendations. The following are some of our past recommendations that we continue to include in this budget:

- **Moving to nightly custodial services – savings of \$1 million.**
- **Moving participants from non-preferred drugs to clinically equivalent generic or preferred drugs – savings of \$16.4 million.**
- **Establishing a network management approach along with a \$1000 per participant maximum for chiropractic care – savings of \$4.7 million.**
- **Creating a Central State Travel Division within the Comptroller General's Office to manage and monitor agency travel – savings of \$831,218.**

In addition, we use this section to explore new ideas for reducing costs in central state government. Some of the new recommendations to reduce waste and increase efficiency in central state government include:

- **Eliminating costly, inefficient DSIT DB2 services at DHEC – savings of \$1 million.**
 - **Implementing efficient cell phone, pager, and satellite phone policies – savings of \$800,000.**
 - **Reducing insurance premiums paid to the Insurance Reserve Fund – savings of \$3.8 million.**
 - **Eliminating vendor preferences in the procurement code – savings of \$130,000.**
5. **Decrease the size of state government by consolidating agencies, boards, and commissions and strengthening the cabinet form of government.** Government in South Carolina costs 140 percent the national average, and given the budget challenges our state faces today and in the future, we can simply no longer afford our inefficient, unaccountable government structure.

The administration has been committed to continuing the legacy of Governor Carroll Campbell by further restructuring state government to increase accountability and reduce duplication and waste. Our state government today is still largely fractured and duplicative, wasting dollars that would otherwise go to the citizens of our state. Many agencies are run by boards and commissions comprised of well-intended people who give their time, typically for little or no pay. While we are grateful for all citizens willing to give their time to serve the people of this state, these people also have families and careers that keep them away from the daily operations of state government. We believe that the cabinet form of government, rather than boards and commissions, will significantly increase government efficiency and effectiveness because those charged

with managing cabinet agencies report directly to the governor – who is directly accountable to all voters in the state.

The need for more accountability has hardly been more evident than in the past couple of years with two different reports highlighting millions of tax dollars being wasted – one on the Department of Transportation (DOT) from the Legislative Audit Council and the other on the Budget and Control Board from the GEAR Committee. Fortunately, the efforts of this administration and others led to DOT becoming a part of our cabinet. The Budget and Control Board, however, remains a part of our government system and is still the only one of its kind in the entire country.

Last year, a Department of Administration bill passed the House unanimously before stalling in the Senate. Representatives Jim Harrison and Garry Smith prefiled legislation reintroducing this measure in the House this year, and Senators Larry Martin, Chip Campsen, and Vincent Sheheen did so in the Senate. We believe passage of this legislation should be the first order of business for both the House and Senate this year.

We would also ask all in the General Assembly to join with the sponsors named above, and other members, to advance the restructuring proposals in our executive budget including streamlining healthcare agencies.

These restructuring proposals, when taken in total, will allow us to eliminate or merge duplicative state offices, departments, agencies, boards, or commissions. In doing this, the state will realize **restructuring savings of over \$21 million during FY 2009-10.**

6. **Honor the promises and obligations of prior years.** Our retirement system's last reported unfunded liability as of the end of June 2007 was over \$10 billion. However, this number is only a part of the picture as it does not include \$8.6 billion of unfunded Other Post Employment Benefits (OPEB) costs for retirees' health care. The combined \$18.6 billion in unfunded liabilities is a key reason that this administration was against the proposal last year to double the guaranteed cost-of-living increase for retirees, which added billions more in costs to the system.

Unfortunately, the \$18.6 billion number has gotten substantially worse over the past 18 months. Although we were unsuccessful in our efforts to prevent the Budget and Control Board from adopting Treasurer Chellis' plan to assume a higher 8 percent rate of return for our state's investment portfolio, our investment performance has (like that of most investments) been quite weak since those numbers were reported.

While our state's portfolio outperformed the market overall, the Investment Commission still reported losing 15.1 percent plus fees over the twelve month period ending last September and 10.9 percent in the first quarter of FY 2008-09 alone. Thus, in one quarter alone, the Retirement System has lost over \$2 billion of its holdings.

The bottom line is that our \$18.6 billion in unfunded liabilities has increased by billions of dollars over the past 18 months. While updated numbers will not be reported for a while – partially due to “smoothing” techniques, which will still mask the true depth of

the problem – the frightening reality is that our combined retirement accounts likely have less than half of the assets needed to pay our total anticipated long-term costs. These numbers will become even worse if we continue to underperform the unlikely 8 percent return benchmark that the Treasurer led the Budget and Control Board to adopt as our assumed rate of return last summer.

South Carolina's retirement system is underfunded, much like several other public pension systems across the United States. In his annual letter to shareholders, America's most famed investor Warren Buffett wrote last year that public pension "funding is woefully inadequate" and that "problems will only become apparent long after" public officials who made the promises have left office. He goes on to write that "promises involving...generous cost-of-living adjustments are easy for these officials to make....those promises will be anything but easy to keep." To increase the solvency of our system, we must make long overdue changes now to lessen the potential of severe future pain for both taxpayers and retirees.

The GEAR Report made the following common-sense recommendations for non-vested employees to shore up finances of the retirement systems:

- Base retirement income on the salary from the last five years of employment rather than the last three years.
- Discontinue the practice of applying unused vacation pay to the number before calculating retirement pay.
- Eliminate the TERI program for new state employees.
- Discontinue the practice of applying unused sick leave to the length of service.
- Move back to a requirement of thirty years of service for full retirement (as is the standard in most states) as opposed to the reduced twenty-eight year requirement adopted by the legislature earlier this decade.

We support all of these proposals as ways to help stop the financial bleeding, but we must go further in order to begin addressing our tens of billions in debt and keep our state's high credit rating. One way to do so is to ask retirees to start paying a larger percentage of their health care costs. Agencies (and thus taxpayers) have traditionally paid the same cost-share for health care for retirees as current state employees. Currently, taxpayers are paying approximately 71 percent of the health care costs for retirees and their families. Over the past ten years, taxpayers have picked up between 67-82 percent of that cost with retirees paying the other 20-30 percent of the health care tab.

In FY 2009, retiree's total health cost is projected to be near \$360 million, which means that taxpayers will be paying over \$250 million this year for retiree's health care. This charge is paid through a surcharge on agencies' payrolls. That charge is increasing rapidly - from less than 2 percent of an agency's payroll in 1999 to 3.5 percent in the current budget year – an over 80 percent increase in the past decade.

Dropping the employers' surcharge for retiree health care costs back down to around 2.65 percent will free up about 0.85 percent of this payroll surcharge to use toward paying down unfunded liabilities for retirees. This change would free up about \$62 million in recurring funds that could be allocated to reducing the total unfunded liability of retirees' health care by approximately \$2 billion.

This change would require retirees to start paying approximately 46 percent of their insurance cost that is not already covered by Medicare. By comparison, taxpayers in the state of Florida only pay a maximum of \$150 a month of health care costs per vested retiree based on a formula of \$5 per year of service. In South Carolina, taxpayers are paying over double that amount with an average of \$348 a month for a retiree's health care. The disparity is even larger when comparing employees who worked for less than 30 years with their respective states.

A report issued in 2000 by the South Carolina Chamber of Commerce showed that our state's retirement system was more generous than 90 percent of the major government pension systems in the country. Since that time, the Legislature has even increased those benefits by guaranteeing a 2 percent annual cost of living increase for retirees. Unfortunately South Carolina is still a relatively poor state ranking in the bottom 20 percent in terms of income. While it is a noble goal to pursue, how can relatively low-income South Carolina taxpayers afford to pay benefits to public retirees who rank in the top 10 percent in the country? And will the tens of billions required to do so come from substantially higher taxes or from cutting funding to other worthwhile government programs?

On their website, the President of the South Carolina State Employees Association writes the following about how their benefits have been obtained (emphasis added):

demonstrations of our numerical strength have yielded retirement benefits second to none, a TERI program, 28 year retirement, pay raises and cost-of-living increases. None of these benefits came automatically. It is through the efforts of a united front of state employees and retirees, advocating for ourselves and others, who are not members, that all of these benefits accrued to us.

The reality is that benefits accruing to government retirees have to come from somewhere – in this case, current taxpayers. However, the tens of billions in unfunded future benefits – political promises that have been made but not funded – will either have to come from our children and grandchildren or the entire system will collapse under the weight of its debt. Most taxpayers in South Carolina cannot afford retirement benefits “second to none” for themselves much less hundreds of thousands of public retirees.

We must act now if we are to keep these promises to future generations of retirees and the implied promise of a better future for all of our children. Given the significant unfunded liabilities partially brought about in large part by the increases in overall retiree benefits granted over the past decade, it is both reasonable and necessary to ask that

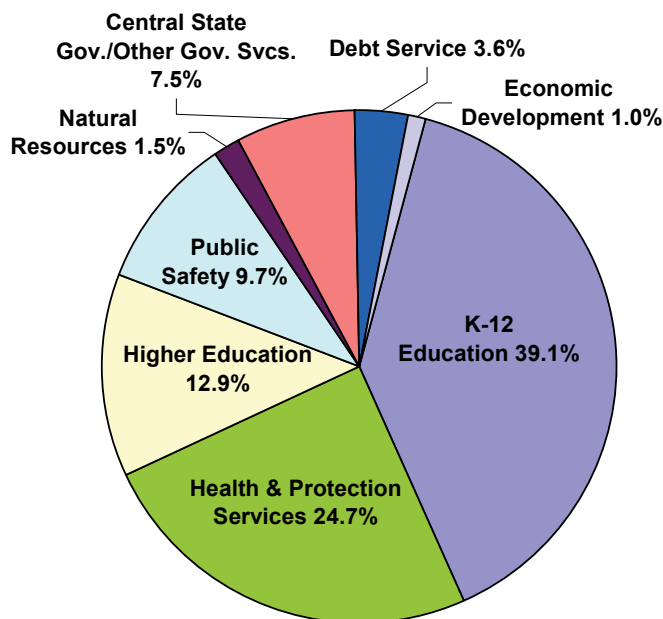
retirees shoulder a larger percentage of their insurance costs – especially since the change is being made to help save their long-term benefits.

A continued failure to start funding our long-term liabilities and shore up the solvency of our retirement systems will threaten the financial well-being of every South Carolinian - especially state retirees. But these proposals are also made in an effort to decrease a legacy of huge debt with which we are on the verge of burdening our children and grandchildren.

7. **Fund property tax relief** – Since 1995, the state has returned billions in property tax relief to the people of South Carolina. Two sessions ago, the General Assembly passed legislation which offers even more property tax relief by shifting K-12 Education funding responsibility from owner-occupied homeowners to the general populace in the form of a sales tax increase. While we feel that it is important to highlight the tax shift nature of this bill, we nevertheless agreed with and signed this landmark property tax bill since we feel that the burden of being a homeowner within the state has become too great for some of our fellow citizens. **In this budget, we set aside \$81.5 million for FY 2009-10 in payments back to local governments for property tax relief** – in addition to the funding mechanism to continue complete elimination of the school operating portion of property taxes.

Summary Comparison of General Fund Expenditures

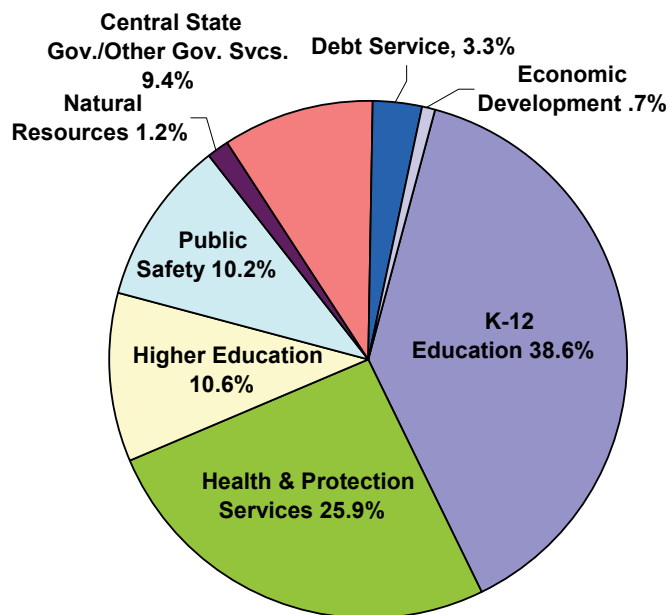
Current Budget – FY 2008-09 General Fund Expenditures



Category	Dollars in Millions
- K-12 Education	2,225.0
- Health & Protection Services	1,404.9
- Higher Ed. & Cultural Resources	731.9
- Central State Government / Other Governmental Services	425.4
- Public Safety	551.4
- Debt Service	203.8
- Natural Resources	87.4
- Economic Development	56.9
TOTAL	5,686.6

Note: Numbers include Rescission Bill and December 2008 7% across the board cuts

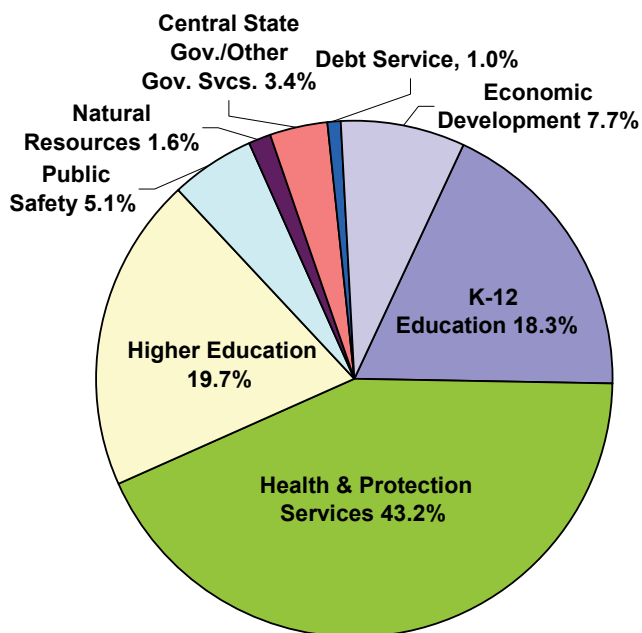
Governor's Purchase Plan – FY 2009-10 General Fund Expenditures



Category	Dollars in Millions
- K-12 Education	2,237.8
- Health & Protection Services	1,498.0
- Higher Ed. & Cultural Resources	614.7
- Central State Government / Other Governmental Services	528.1
- Public Safety	593.5
- Debt Service	190.5
- Natural Resources	70.2
- Economic Development	43.0
TOTAL	5,775.8

Summary Comparison of Total Fund Expenditures

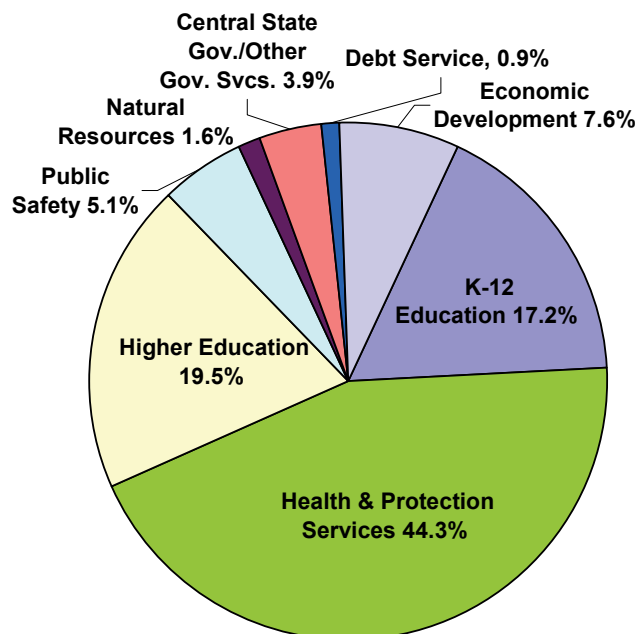
Current Budget – FY 2008-09 Total Fund Expenditures



Category	Dollars in Millions
- Health & Protection Services	8,591.8
- Higher Ed. & Cultural Resources	3,912.5
- K-12 Education	3,642.2
- Economic Development	1,530.9
- Public Safety	1,011.6
- Central State Government /Other Governmental Services	679.9
- Natural Resources	320.1
- Debt Service	203.7
TOTAL	19,892.7

Note: Numbers include Rescission Bill and December 2008 7% across the board cuts

Governor's Purchase Plan – FY 2009-10 Total Fund Expenditures



Category	Dollars in Millions
- Health & Protection Services	9,202.1
- K-12 Education	3,568.0
- Higher Ed. & Cultural Resources	4,043.2
- Economic Development	1,581.5
- Public Safety	1,059.4
- Central State Government /Other Governmental Services	787.6
- Natural Resources	322.0
- Debt Service	190.5
TOTAL	20,754.3

\$20.75 Billion

Includes all funding such as the General Fund, Other & Federal Funds, Capital Reserve Fund, Surplus, Contingency Reserve Fund, EIA, Lottery, other Revenue Adjustments

Higher Priorities

Lower Priorities

What our plan buys:

\$9.2 billion	Health care and protection for nearly a million children and adults
\$3.6 billion	K-12 education for almost 700,000 students
\$4.04 billion	Higher education for over 222,000 students & funding for cultural resources
\$1.58 billion	Economic development
\$1.06 billion	Public safety
\$787 million	Central state government/other governmental services
\$542 million	Property tax relief fund
\$273.2 million	Constitutional/statutory funding requirements
\$322 million	Protection of our natural resources
\$190.5 million	Debt service for General Obligation Bonds
\$62 million	Funding for OPEB liability
\$45 million	Funding for deficit at Department of Corrections

\$20.75 billion TOTAL

\$266.6 Million General Funds

Examples of what our plan does not buy:

\$48.2 million	Activities that have been determined by the Budget Results Teams to either have spending inefficiencies or that are low priorities for the goal area
\$31.5 million	A fragmented system at the state's higher education institutions
\$21.4 million	Duplicative administrative costs that can be saved by restructuring
\$17.2 million	Full salaries of TERI employees leaving state government
\$10.2 million	Excess Agency Travel
\$1.0 million	Daily custodial services
\$983,133	Free DPS traffic control at special events
\$668,100	Full Legislative Session
\$360,000	Excess vehicle maintenance facilities in the Columbia area

\$266.6 million TOTAL

Additional Information

More details of agency activities can be found at the Office of State Budget's website at <http://www.budget.sc.gov/OSB-agency-activity.phtm>. Further specific highlights of the Governor's Purchasing Plan for each goal area can be found later in this document starting with Improving K-12 Student Performance on page 104. The Governor's complete Purchasing Plan by goal area can be found in Appendix B-3; the complete Purchasing Plan by agency can be found in Appendix B-4; and the complete Savings Proposals can be found in Appendix C.

The Budgeting for Results Process

The Budgeting for Results Process

Results matter...or at least they should. Especially when it comes to tax dollars and public expenditures. Increasingly, taxpayers are demanding results and performance in return for their hard earned dollars.

– Geoffrey F. Segal, Reason Foundation (2004)

Most managers have no idea what their products and services really cost. At best, conventional cost accounting is marginally relevant to decisions about operations and management. At worst, it distorts reality and causes dysfunctional decisions.

– Kehoe, et al., *Activity-Based Management in Government* (1995)

This is our fifth executive budget using an “activity-based” approach that emphasizes outcomes or results. This approach requires agencies to break state government programs and processes down into literally hundreds of separate and distinct activities. We then establish key goals for the state to accomplish in major functional areas of government, such as education, public safety, and economic development. Next, we carefully select sound and verifiable indicators of success from reliable sources to measure both short- and long-term progress. Finally, we identify strategies that are considered “best practices” or scientific evidence and documentation to bring about real, proven, significant, and lasting results.

Hence, this intensive activity-based budget method provides decision makers – our administration, legislators, public officials, and administrators – with valuable and important information and data. These detailed cost data are significant because they give decision makers the opportunity to make optimal choices about how to allocate limited resources. Moreover, activity-based data permit decision makers to streamline, reengineer, and innovate state agency operations and processes to produce the maximum results at the best cost.

Further, without activity-based data, it is difficult or nearly impossible to answer such questions as:

- Is this state governmental service or activity of good value? Is it both cost-efficient and cost-effective?
- Are the costs associated with this activity competitive? In other words, can this activity be provided more cheaply by competing service providers (public or private)?
- More importantly, is this activity even desirable to or needed by the public?

Additionally, at this juncture, it is equally important to comment that many experts in public finance believe that the cardinal aim of activity-based budgeting is accountability. Performance information and data used in budgeting holds public officials, especially program managers, accountable for

service quality, cost-efficiency, and program effectiveness. The focus of activity-based budgeting is, once again, on results, not simply inputs. For this reason, governors, legislators, service or program recipients, and the public generally can determine accountability with a degree of certainty through the use of activity-based methods, whereas this is not possible utilizing traditional or line-item approaches. This ability to assess performance and hold public managers and administrators accountable serves as a powerful incentive to improve quality.

As pointed out in previous budgets, our executive budget is a vast departure from the traditional state budgeting practices of the past – which, unfortunately, continue to be used today by the state’s Legislature. As such, budget or financial analysis utilized in the legislative spending process is unavoidably limited or incomplete.

By the standards of today’s financial practices, traditional governmental budget processes are by and large considered to be archaic, marginal and void of careful analysis and decision making as they relate to the preceding year’s “appropriation’s base.” Their focus is on “new monies” alone, that is, on those funds that result from revenue growth during the previous year.

This incremental approach allows obviously for only a narrow, minor discretionary review of state spending. Thus, public policy is made in incremental or successive steps, resting on decisions made in prior years. Unfortunately, incrementalism does little more than *control* spending and *preserve* the status quo of the bureaucracy. Worse still, past spending decisions simply are unexamined. These “automatic” determinations – without consideration of the twin critical aims of (1) establishing cost savings and (2) effectively formulating and discerning productive results – prove to be counterproductive and often simply wasteful.

Traditional Budgeting vs. Budgeting for Results

Incremental or Traditional Budgeting	Results-Based Budgeting
Focus is on the allocation of “new monies” only (5-10 percent of budget total)	Focus is on nearly all monies or the entire budget amount (excepting certain obligations such as debt service, reserve fund requirements, etc.)
Concentration is on inputs (what you buy), e.g., “objects of expenditure”	Concentration is on outputs (what results are expected)
Narrow or marginal decision making	Comprehensive or enterprise-wide decision making
Subjective based	Objective based
Preserving the status quo	Determining new, creative approaches to problems and needs
Agency or bureaucracy driven	Outcome driven
Promotes restraints, restrictions and red tape	Encourages flexibility and ingenuity
Control orientation	Planning and management orientation
Emphasizes compliance and preserving legality	Emphasizes performance and innovation
Stresses audit trails and conformity	Stresses program evaluation and improvement
Involves agency heads, elected officials and advocacy groups	Involves everyone wanting to participate, especially those wearing a “citizen’s hat”
Encourages and perpetuates single-agency programs	Encourages intra- and inter-agency cooperation among programs and activities

Our administration utilizes what experts have described as a pioneering budget process that examines the entire budget – virtually every activity performed by government and its associated funding. Again, this is done ultimately in the context of a set of pre-established goals or results that are determined by our administration to be of major significance to the citizenry. Called “Budgeting for Results” (BFR), it is a process that includes input or direct participation from ordinary citizens and subject-matter experts, designated as Result Teams, that develop purchase strategies to achieve the preset goals. Using these so-called “purchase strategies,” the Result Teams then prioritize all state governmental activities, looking for possible cost savings, consolidations, and process improvements. The Result Teams then relay this information – indicators, strategies, priorities, and innovations – to the administration. This extensive information then becomes a blueprint for our budget.

Definition of Terms
Goal Areas – Seven broad result or priority areas that the administration believes South Carolinians want most from their state government.
Indicators – Key measures or indices that provide the best evidence to the citizen that a statewide goal area is being achieved.
Strategies – Proven or promising approaches, influences, or factors for achieving goals or results.
Activities – Individual or discrete actions taken by state government to accomplish goals and objectives. For the citizen, “What is the state doing, for whom, and does this accomplish something that is both valuable and needed?” “Precisely, why are we doing it?” “And at what cost?”

We believe that our budgeting approach is detailed, transparent, and rational. Overall, its focus is aimed toward bringing about positive consequences, again, both for the short- and long-term. In effect, the purpose of BFR and our executive budget for FY 2009-10 is:

To build and present a coherent, comprehensive spending plan for South Carolina based on clearly articulated statewide goals, effective strategies, and creative and insightful thinking. To focus on the “keeps,” not the cuts. To underscore “results” to ensure that citizens – not agencies, special interest groups, or lobbyists – get their full money’s worth from state government.

We adopted the BFR process because of its logical approach to public budgeting and fiscal decision making. BFR was originally based on Washington State’s budget process model which was established in the fall of 2002. It is a process, in a modified form, which has been adopted by several states like Iowa and Michigan and local governments like Los Angeles and Dallas.

As we remarked last year, the BFR process examines the entirety of government and nearly all statewide funding. Our priorities are clear. This budget demonstrates how we will live within our means and invest in what matters by honing in on core goals and directing the whole of state government and its funding structure toward meeting those goals. It is our roadmap to a results-producing government that serves South Carolina's needs.

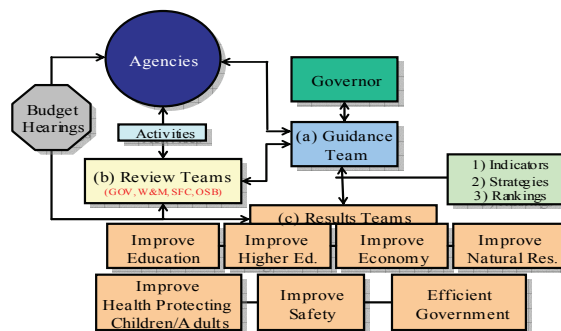
The Budgeting for Results Organizational Structure

A popular government without popular information or the means of acquiring it is but a prologue to a farce or a tragedy or perhaps both.

– James Madison, *The Writings of James Madison 103* (1910)

The principal structural components of BFR are units or “teams.” These organizational units consist of (1) a Guidance Team, (2) a Review Team, and (3) seven Results Teams.

Budgeting for Results Structure



1. **The Guidance Team (GT)** predominantly planned, supported, and monitored the BFR process. The GT consisted of our staff and staff of the Office of State Budget (OSB). The GT also actively worked to energize the BFR process and met to coordinate and maintain the efforts of the seven Results Teams.
2. **The Review Team (TRT)** was designed to review and assess each agency's detailed activities before the activities were submitted to the Results Teams. The TRT further ensured that the activities were properly defined or explained and formatted. Also, they placed activities into the appropriate, logical goal areas. Staffing consisted of personnel from the OSB and the Governor's Office. It should be acknowledged that each of these staff members possessed extensive knowledge of the agency budgets within the various goal areas.

3. **The Results Teams (RT)** were integral to the entire BFR process – in terms of sheer work and productivity. They were made up of groups of typically five to seven persons who possessed some expertise in relevant subject matter but were asked to think like citizens, setting aside any agency or advocacy bias. Their chief roles and responsibilities were to identify those indicators that would best show progress toward their respective goal areas. Based on these indicators, the RTs also established key purchase strategies on how to best achieve each goal area. Most important, the RTs were responsible for ranking and prioritizing agency or governmental activities that best met some aspect of their particular goal area.

The Budgeting for Results Process

The BFR process consists basically of six steps: (1) setting major goal or result areas; (2) reviewing and finalizing agency activity inventories; (3) developing or fine-tuning chief indicators of progress and key strategies for achieving results; (4) holding public budget hearings for select result or goal areas; (5) sorting and prioritizing agency or governmental activities and identifying savings; and (6) distributing resources among goal areas, i.e., the finalization of the purchase plans by result areas.

While each step in the BFR process is important and consequential, the singular importance of indicators cannot be underestimated. Indicators are, of course, the “yardsticks” or measures by which progress toward goal areas can be assessed. This is integral to any performance-based budgeting system, especially activity-based budgets. Significant also in the context of the BFR process is that strategies or approaches for achieving goals or results are intertwined with and dependent upon the indicator of progress in that they are the guideposts for prioritizing agency activities. Hence, the right indicator combined with the right strategy will yield a composite of prioritized governmental activities that are goal-oriented and expected to achieve concrete results.

Step #1 – Setting major goal or result areas. The first step was to set major goal or result areas that need to be achieved in the state. Based on previous years' experience with BFR, we ultimately concluded that seven statewide goals would represent where the citizens of South Carolina wanted to focus in terms of results and progress made. Incidentally, these seven goal areas roughly coincide with the focus areas of the subcommittees of the House Ways and Means Committee and the Senate Finance Committee.

The following seven wide-ranging goals or results areas were identified:

1. Improve the conditions for our economic growth
2. Improve the health and protections of our children and adults
3. Improve the safety of our people and property
4. Improve the quality of our natural resources
5. Improve our K-12 student performance
6. Improve our higher education system and cultural resources
7. Improve central state government support and other governmental services

Step #2 – Developing agency activity inventories. The next step was to develop an all-inclusive inventory of the activities that state government performs. For each activity, three main elements were required – a description of the activity, its expected outcome, and its cost.

To acquire this activity information and data, working in conjunction with OSB, we requested, as in previous years, that each agency break down its budget into discrete and definitive activities. Each agency was instructed to provide a description of each activity it provides directly or indirectly to citizens of South Carolina. An activity was defined as something an organization does to accomplish its goals and objectives and that consumes resources and produces a product, service, or outcome. Most importantly, an activity should describe in a citizen-oriented way the following: what is done; for whom; why; at what cost; and what is to be expected or accomplished.

State agencies submitted agency activities to OSB, which entered them into an existing database. Most activities presented reflected previous years' submittals, excepting enhancements and new activities. Next, the TRT examined the activities to evaluate the quality of the activity descriptions and outcome measures. Those activities requiring more work or improvement were sent back to agencies for appropriate corrections or improvements. Once this was completed, OSB sorted the activities to correspond to the seven goal areas, or verified that assortments from previous arrangements were correct. For example, those activities – regardless of agency or department – that appeared to fall within the goal area of K-12 improvement were placed there; those activities that related to the improvement of health were directed there, and so forth.

Thus, the final product of this second step was the formation of a comprehensive inventory of activities, numbering more than 1,600 separate and distinct activities that comprised the entirety of what state government does, for whom, why, at what cost, and for what effects or outcomes.

Step #3 – Developing chief indicators of progress and key strategies for achieving results.

Again, seven RTs were put together consisting of experts and knowledgeable citizen participants versed in the subject matter of each goal area. Each RT was headed by a team leader from the Governor's Office. OSB provided financial subject matter and research expertise for each RT.

Step 3 required each RT to identify chief *indicators* of progress based on verifiable and well-documented statistical sources (the U.S. Census Bureau, the U.S. Labor Department, USC's South Carolina Indicators Project, etc.). These were, according to experts and specialists in the subject matter, the best and most comprehensive indicators for a goal area.

After the identification of indicators, each RT then collectively identified *strategies* that it felt – based on scientific data and information and literature – demonstrated empirically broad and comprehensive achievement within a state goal area.

These indicators and, more importantly, their link to strategies would be later utilized by the RTs as the basis or mechanism to review, analyze, and ultimately prioritize and rank activities which would advance the state toward the preset statewide goals.

This year, each RT re-evaluated the efforts of last year's teams in identifying indicators for each major goal. The indicators are key to the BFR effort and allow the state – particularly our administration, the General Assembly, state agencies, and the public at large – the opportunity to gauge the progress of accomplishing statewide policy goals, more specifically the seven goals designated in this FY 2009-10 Executive Budget. In addition, these indicators will allow our administration, the General Assembly, and the public to determine if the strategies we have

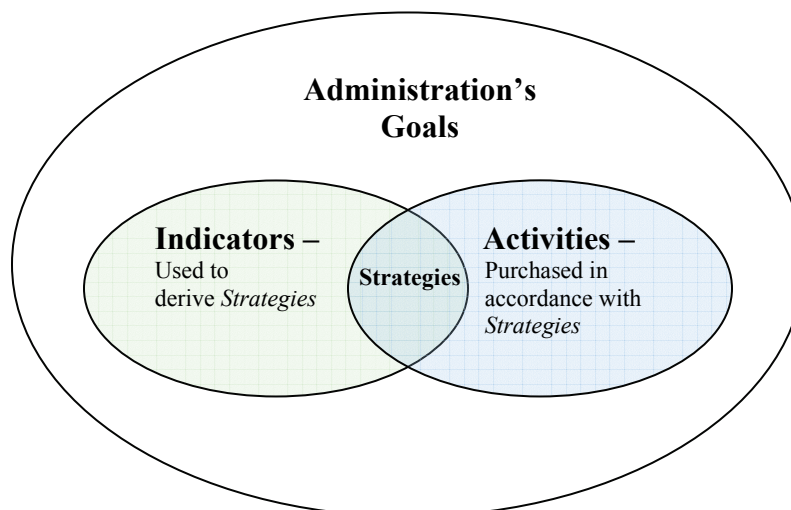
identified in achieving the statewide goals are effective, especially for both short-term and, more importantly, *long-term* evaluative purposes.

Additionally, it should be emphasized once again that BFR is a budgeting approach that places emphasis on logic, order, and proven cause-and-effect relationships. Utilizing the highest degree of objectivity and data analysis, this approach involves not only the setting of broad goals, but also dividing these further into specific objectives and then identifying indicators, measurements, and strategies by which verifiable progress can be reasonably assessed over time.

Further, in Step 3, the BFR approach creates a strategic framework for RT's analysis and decision making. This framework comprises the following:

- Requires the consideration of the results citizens expect from government;
- Articulates those strategies that are most effective in achieving those results;
- Puts front and center those indicators which will best measure progress;
- And as relates to Step 4 (below), initiates an estimation or anticipation of prioritized spending to select or prioritize (buy) the activities that are most critical to implementing strategies and achieving (measuring) success;
- Helps keep the focus on contribution to priority results – lets RT's escape agency "silos" and consider instead statewide strategies;
- Makes performance information more relevant to budget choices;
- Helps frame the question, "Are we sure we are buying things at the best possible price?"; and
- Helps us describe the activities and results the *entire* budget will buy.

Diagram of Interrelationships of Goals, Indicators, Activities and Strategies



Step #4 – Holding public budget hearings for each result area. This step allowed the opportunity for the governor, the governor’s policy staff, appropriate RT members, and other interested parties – including the general public – to meet with agency heads and personnel to discuss governmental activities particular to a goal area. This year there were seven meetings held for each of the major budget groups. The hearings typically lasted two to three hours and can be accurately depicted as interactive, providing a forum for conversation rather than formal presentations by agencies. Generally, the discussions centered on how agency governmental activities were contributing to the results or goals set by our administration. Agencies were questioned about their most beneficial, highest priority activities, as well as those that were marginal or less productive.

Step #5 – Sorting and prioritizing agency or governmental activities and identifying savings. This step involved the RTs prioritizing or ranking – “purchasing” – governmental activities. The product or deliverable here was the development of a preliminary purchase plan of prioritized activities – an initial budget for each goal area.

Early on, the OSB had sorted activities by the designated goal areas (Step 2 – the developing of agency activity inventories). During the interim steps above, OSB had sorted activities by strategies which were developed by the RTs in Step 3 (i.e., the developing of chief indicators of progress and key strategies for achieving results). At this point, each RT was charged with reviewing the activities, not yet seen by the RTs, and deciding which *linked most closely* to their respective goal area, indicators, and strategies. Eventually, these activities were ranked by each team member (assigning an equivalent numerical value) based upon which goal area strategy it fell under. Obviously, those activities that appeared unrelated or less important to the goal area or, especially, the major purchase strategies were abolished, placed on a wish list, or sent to a more appropriate goal area or RT.

With this process completed, each RT, in effect, had ranked or prioritized its portion of the 1,600 activities to complete a goal-specific preliminary purchase plan, which was – by all accounts among RT participants – perceived as both thorough and complete. The RTs also reviewed all costs associated with the activities regardless of the funding source (e.g., state General Fund, federal and “other” monies). Most importantly, perhaps, this step was an opportunity for RT members to challenge their previous assumptions and rationales for prioritization and to look for creative and innovative ways to do things differently and, hopefully, better. Central questions at this stage were, “Are these activities the most efficient and effective ways to achieve the designated goal area(s)?” “Does this budget plainly make sense? Can it *be easily understood* so that it produces the results South Carolinians want and at the right price?” Equally important, other questions that required answers, to the extent possible, included:

- Can these activities (those ranked, at a minimum, as “important”) realistically be measured in terms of performance or outcomes, and how?
- For those activities *not* purchased, what are likely to be the consequences?
- Can those activities that obviously appear to be duplicative, in and across agency structures, be eliminated or merged? If so, where can the cost savings be targeted in terms of other activities?
- What activities appear to be antiquated, no longer relevant to today’s citizenry? Can or should they be salvaged, or should they simply be abolished freeing up funds for more important, underfunded activities?

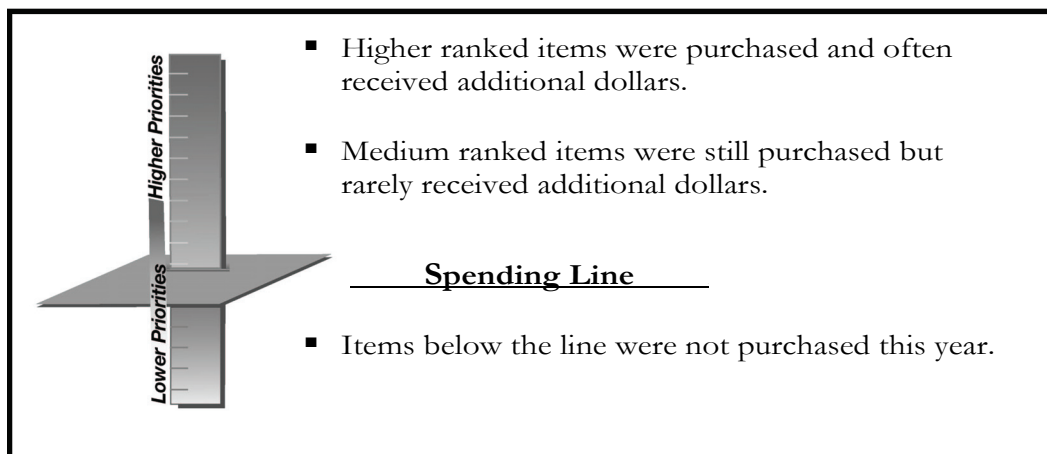
- What activities appear to be excessively funded, especially those ranked on the lower end of the prioritization list?
- In the final analysis, is this purchase plan for education, health, etc., the best possible budget – given the circumstances – for purposes of advancing the quality of life for all South Carolinians? Generally speaking, what more needs to be done in the future to make South Carolina great?

Step #6 – Distributing resources among goal areas, i.e., finalizing the purchase plans by result areas. The heart of Step 6 was the methodical and careful review by our administration of the preliminary purchase plans submitted by the RTs and the finalization of a completed purchase plan reflecting our philosophy and policies. Ultimately, this final purchase plan took the form and substance of this FY 2009-10 Executive Budget.

It is noteworthy that the review of the RTs' rankings or preliminary purchase plans and our administration's finalization of priorities was not, by any means, an easy task. As was the case for the FY 2008-09 Executive Budget, many governmental activities were of nearly equal importance relative to purchase strategies and statewide goals. Further, we clearly stated that even though one activity was ranked below another activity, it was not correct to assume that the activity is of lesser value or importance than those prioritized above it. We did point out, however, that activities ranked in the upper 15 to 20 percent of a goal area were clearly of the greatest significance and that those at or near the bottom of the rung were, based on our estimation and analysis, perhaps not as valuable or central to selected strategies within identified goal areas.

Further, during Step 6 available funds and FTEs were spread, based on historical spending patterns and our preferences, across the seven goal areas. This was done, of course, only after constitutional and statutorily mandated expenditures were met (e.g., debt service, aid to subdivisions, and property tax relief). After spreading funds among the goal areas, we began using the information and data from the RT preliminary purchase plans, along with other research and materials to "purchase" activities of the highest priority until the funds allocated to the specific goal areas were exhausted. The result was that those governmental activities that were of the greatest importance, or moderately so, to respective goal areas were funded. Those activities that fell below the "spending line" were not funded.

The "Spending Line"



Finally, some concluding observations about Step 6. Based on zero-based budgeting precepts and accepted activity-based procedures, we evaluated new activities on an equal basis as existing activities. The evaluation of a governmental activity was based on indicators and purchase strategies as related to the achievement of statewide goals. In other words, purchasing was done on the basis of anticipated outcomes rather than historical precedent.

As in prior years, during this process there were some activities that fell below the purchase line that gave us pause. However, given the priority ranking, the question that we had to ask ourselves was what activity above the purchasing line we would not purchase so that we could switch it with an activity below the line. This process, while difficult and tedious at times, helped us prioritize our spending in a world of limited resources and, equally important, it was based on our spending cap. The resulting budget recommendations represent this new focus on maximizing results for the citizens of South Carolina.

A Change in Budgeting Models and Mind-Set

The man who is striving to solve a problem defined by existing knowledge and technique is not just looking. He knows what he wants to achieve, and he designs his instruments and directs his thoughts accordingly.

Rather than being an interpreter, the scientist who embraces a new paradigm is like the man wearing inverted lenses.

– Thomas Kuhn, *The Structure of Scientific Revolutions* (1962)

The BFR process has proven to be successful and well-received by progressive-thinking legislators, the media, and the public. We believe that the process is innovative and pragmatic as a public budgeting mechanism.

This year's BFR effort was for us, as we stated last year, "a shift in paradigms." The outdated, traditional budgeting approaches of concentrating on apportioning new monies only, the concentrating on inputs alone, and the continuing bureaucracy-driven emphasis simply on self-preservation is no longer tenable during times when revenues are in a steep decline.

In a sense, BFR was born out of increasing recognition and comprehension of South Carolina's socio-economic makeup, status, and performance. More exactly, it resulted principally out of the understanding of our administration that conventional budgeting structures and processes were not keeping pace with the times.

In conclusion, we feel assured that the BFR process for FY 2009-10 was another excellent step forward in setting goals and priorities critical to South Carolina. In light of this, and the willingness among some members of the General Assembly to find ways to improve and enhance budgetary processes and decision making, we propose that a similar proviso be introduced as initiated by Rep.

Dan Cooper four years ago and adopted by the House. As we did last year, we ask the General Assembly to adopt the following proviso in the FY 2009-10 appropriation bill:

NEW PROVISIO (GP: Joint Committee on Activity-Based Budgeting). *There is established the Joint Committee on Activity-Based Budgeting composed of nine members. The nine members shall be appointed as follows: three Senators appointed by the Chairman of the Senate Finance Committee; three members of the House of Representatives appointed by the Chairman of the House Ways and Means Committee; and three members appointed by the Governor. The Governor shall appoint the committee chairman. The terms of members shall be coterminous with the term of their appointing authority. Members of the Senate and House of Representatives shall serve ex officio. The committee shall study activity-based budgeting processes and how they may apply to the budget and appropriations processes for the State. Because the intent is to reduce duplication of government services, maximize cost-efficiencies, and still continue to provide excellent customer services, all costs of implementing a new budgeting system must be considered, including technological and human resource applications. Further, the committee will consider those budget processes that incorporate zero-based principles, particularly those which examine the entirety of government and state funding. Such budget processes must additionally emphasize, to the extent possible, the establishment of clearly delineated statewide goals; activity outcomes and results; spending strategies and priorities; and the measurement of performance.*

The committee may propose, by majority vote, a budget process not inconsistent to matters relating to the discharge of its duties. This proposal shall be reported to the Senate Finance Committee and the House Ways and Means Committee by no later than January 1, 2010.

Professional and clerical services for the committee must be made available from the staffs of the General Assembly, the Budget and Control Board, and other state agencies and institutions as needed. The members of the committee are not entitled to receive the per diem, mileage, and subsistence allowed by law for members of boards, committees, and commissions when engaged in the exercise of their duties as members of the committee. All other costs and expenses of the committee must be paid in equal proportion by the Senate, the House of Representatives, and the Office of the Governor, but only after the expenditures have been approved in advance by the President Pro Tempore of the Senate, the Speaker of the House, and the Governor.

Revenue

Revenue

Economy Continues to Recede

This year marks a stark turning point for the economy on a national and state level, with many states facing significant budget shortfalls. More than 40 states are dealing with more than \$30 billion in shortfalls in their current budgets, while 25 are looking at deficits of \$60 billion for FY 2009-10. Most states, including South Carolina, will continue to be impacted by the weakening national economy, which means FY 2009-10 could prove to be more challenging than FY 2008-09.

At the end of 2008, South Carolina's general fund reductions for FY 2008-09 totaled almost \$1 billion. Unfortunately, more reductions are expected in 2009 due to further deceleration of the economy and a lack of spending restraint in previous years when times were good.

There are a couple of items, among many, that can be highlighted as the cause of the economic situation. First, the financial troubles caused by sub-prime lending practices have led to a host of risky investments by major financial institutions. A number of these institutions have become insolvent or have had to write-down billions of dollars in lending losses already – and now have turned to the federal government to help bail them out.

In addition, a weak housing market has made credit problems worse simply because of the securitization of the mortgages. The success of these securities depends on house prices not falling. They are falling, however, and are expected to continue falling at an even faster pace. The decline in housing construction and home values, with attendant losses in personal wealth, will have an immediate negative impact on consumer spending, and there are no indications that this trend will be reversed any time soon.

The weakened economy is something we have said has been coming for quite some time. In fact, we said that the Board of Economic Advisors (BEA) and, by extension, the General Assembly's revenue projections last year were far too optimistic. In addition to two previous letters to the State Chief Economist warning of the economic downturn, we wrote a February 9, 2008, letter encouraging BEA Chairman John Rainey to lower the revenue estimate and stated, "...the starting point is to cut out around \$100 million... and I think the further north you go from there, the more prudent you should become." Interestingly enough, two months later the BEA was forced to cut their estimates by roughly \$90 million.

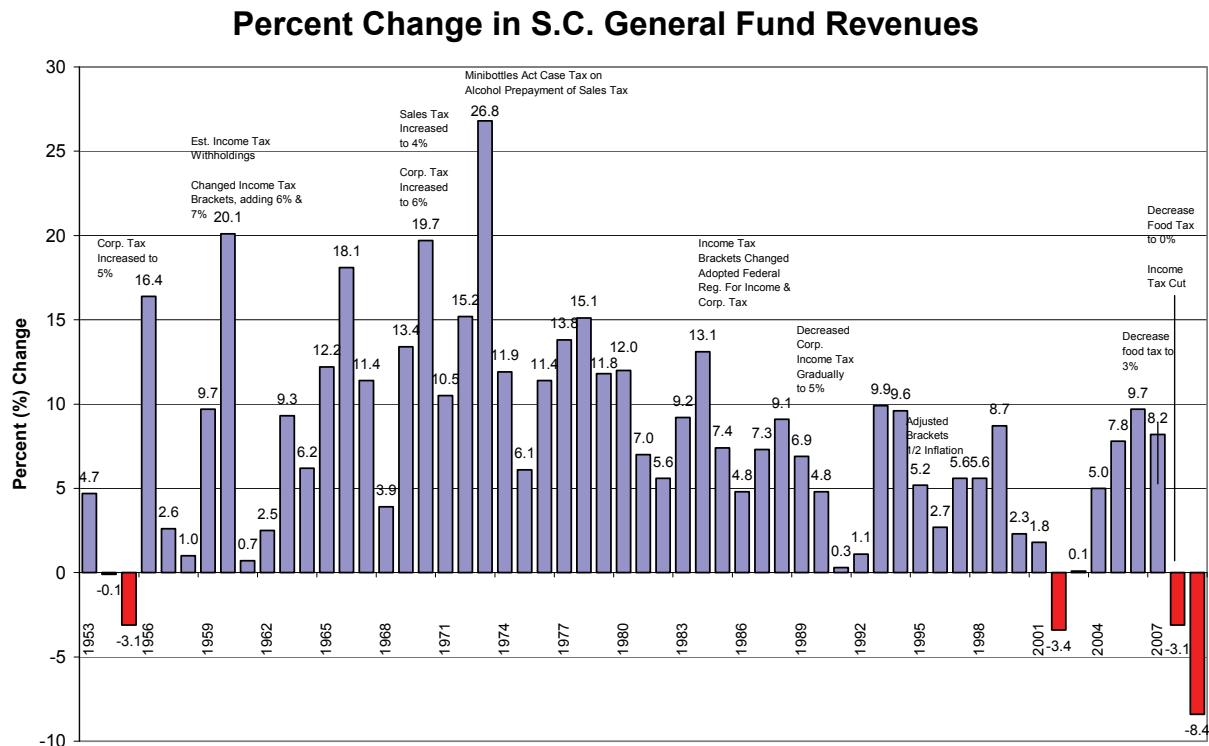
Go back to the last economic downturn and you will see that the February estimates for revenue projections from FY 2000-01 to FY 2002-03 were a total of \$1.185 billion higher than actual revenues. Not surprisingly, this administration entered office with a \$1 billion shortfall that included an unconstitutional deficit and raided trust and reserve funds. More prudent forecasting is vital to eliminating these sorts of financial holes.

Given the over \$1 billion dollar shortfall in the current fiscal year, our state's economists must make more realistic and reasonable forecasts of the economy as they consider future revenue projections. Both the MAP Commission and the GEAR Committee recommended changes to the way the state

makes revenue estimates. The GEAR Committee recommended that the BEA use a national economic forecasting service when formulating revenue estimates. We agree and, once again, urge the General Assembly to look at the private sector for other means of accurately forecasting revenues. It seems prudent to find a way to project revenues that will take the political influences out of the process in order to make forecasting more accurate and realistic.

Currently, the BEA is forecasting that revenue will decline in 2009 by over eight percent, which is the largest revenue decrease in the past 50 years for South Carolina.

For FY 2009-10, the BEA estimated general fund revenue to be the same as this current year at \$6.325 billion – revenue numbers similar to four years ago. Accordingly, we must prioritize the state’s needs and determine how we can fulfill them in light of strapped resources and avoid previous spending habits.



Source: Board of Economic Advisors

Increases to General Fund Revenue

In our past budgets, we took an in-depth look at the benefit of the Job Development Fees that continue to be dedicated for the Redevelopment Authorities (RDA) of Charleston, Myrtle Beach, and the Savannah River Site. These monies have been dedicated since 1994 for the purpose of redeveloping military bases that have closed. Each year the state is forced to remit to the RDAs a portion of their individual income tax withholding even though these entities have fulfilled their original mission. To this end, we believe it is time the taxpayers stop supplementing a project that has been completed. Specifically, we recommend suspending these RDAs for FY 2009-10, which will lead to **an increase of \$4.6 million in general fund revenue next year.**

During the late 1990's, the four largest cigarette manufacturers reached an agreement with 46 states, known as the Tobacco Master Settlement Agreement (MSA), to settle state suits to recover costs associated with treating smoking-related illnesses. South Carolina began securitizing its MSA payments in FY 2000-01. It is estimated that the tobacco settlement will generate **\$10 million in revenue** for FY 2009-10.

The GEAR report found several cost savings at the Budget and Control Board that would generate nonrecurring revenue for the new fiscal year. We have identified two that can easily generate millions to help pay for some nonrecurring budget priorities. First, because of our recommendation for a statewide contract for temporary staffing services, the building that the Tempo program operates out of could be sold for approximately **\$2 million** in one-time revenue. Second, the Budget and Control Board should operate as a "break-even" agency rather than a profit center of state government, which is why we believe carry-forward dollars at the Board should be used for other, more vital services. Given the fact that the Board finished last year with over \$1 billion in cash, we do not feel that this recommendation is unreasonable. The two above recommendations from the GEAR report will generate a total of **\$42,000,000** in nonrecurring revenue.

The remaining revenue generators can be identified in the "Nonrecurring Revenue" section of the following chart.

FY 2009-10 Executive Budget

Recurring Revenue	
FY 2009-10 BEA Estimate Gross General Fund Revenue (Dec. 10, 2008)	6,324,559,868
Less: Tax Relief Trust Fund	(542,519,869)
Plus: Tax Relief Trust Fund Carryforward	1,451,372
Net General Fund Revenue Estimate FY 2008-09	5,783,491,371
Revenue Adjustments:	
Transfer of Excess Cash from B&C Board	40,000,000
Transfer Cash – DHEC Waste Funds	4,500,000
Transfer of Cash from DMV (10-Year License)	773,000
Transfer of Cash from DMV (Close 6 Field Offices)	500,800
Diversion of South Carolina Launch Funds	6,000,000
Taxes and Fees Redirected from RDA's to General Funds	4,600,000
Adjusted General Fund Revenue Estimate	5,856,190,171
Less: FY 2008-09 Base Appropriations (After vetoes-Mid-Yr Rescission Bill)	6,247,807,776
Less: FY 2008-09 Across-the-Board Reductions (B&CB 12/11/08 Actions)	(383,475,665)
"New" Recurring Revenue	(8,141,940)
Cost Savings:	
Agency "Savings"	218,844,273
Below-the-Line "Savings"	47,724,773
EFA Scholarship Change in Source of Funding to Lottery (net gain)	4,165,000
Subtotal, Cost Savings	266,569,046
TOTAL "NEW" FUNDS	537,303,092
Incremental Statewide Items:	
General Reserve Fund <i>(1% of FY2007-08 actual revenues) (paid with nonrecurring dollars)</i>	63,923,944
Capital Reserve Fund	(5,322,170)
Local Government Fund	(49,947,911)
Debt Service	(28,601,864)
Homestead Exemption Fund – BEA Est. Shortfall (Dec. 10, 2008)	81,548,694
Total Statewide Items	(61,600,693)
"New" Funds Less Statewide Items	475,702,399
Nonrecurring Revenue Sources	
B&C Board – Sale of Property (Elimination of Tempo Program)	2,000,000
Transfer of Cash from DMV Carry-Forward Funds	4,000,000
Transfer of Cash from DMV (Notices/Correspondence)	325,000
Total Nonrecurring Sources	16,325,000
Other Funds	
Tobacco Deallocation	10,000,000

Education Lottery Revenues

It has been argued that the commencement of the North Carolina lottery has and will continue to cause South Carolina lottery sales to decrease. The BEA predicts that this amount will be about the same as last year's lottery appropriation at \$255 million.

With lottery revenue in competition with other states, it is more important than ever that we make every effort to run our lottery as efficiently as possible to maximize dollars going to educate our children. For this reason, we again propose reducing the current retail commission of seven percent

to a commission of six percent – which is in line with the national average. In addition, we are recommending that the lottery advertising threshold be reduced to a more reasonable limit of 1/2 of one percent of the previous years' gross sales. These two recommendations will generate more lottery revenue to benefit our education system.

LOTTERY REVENUES	FY 2008-09	FY 2009-10
BEA Revenue Estimate	244,000,000	244,000,000
BEA Interest Estimate	3,400,000	2,600,000
Unclaimed Prizes	8,400,000	8,400,000
Surplus Cash	4,922,729	
Limit Retailer Commissions to 6 Percent of Sales		9,597,974
Limit Advertising Budget		4,165,000
Education Lottery Revenue	260,722,729	268,762,974

Run a Fiscally Disciplined
Government

Run a Fiscally Disciplined Government

A wise and frugal government, which shall leave men free to regulate their own pursuits of industry and improvement, and shall not take from the mouth of labor and bread it has earned – this is the sum of good government.

– Thomas Jefferson

The overarching goal of this executive budget is to eliminate spending that we believe is inconsistent with the priorities of South Carolinians in these challenging economic times – all the while respecting the fundamental belief that excessive increases in state government spending are not sustainable in the long run.

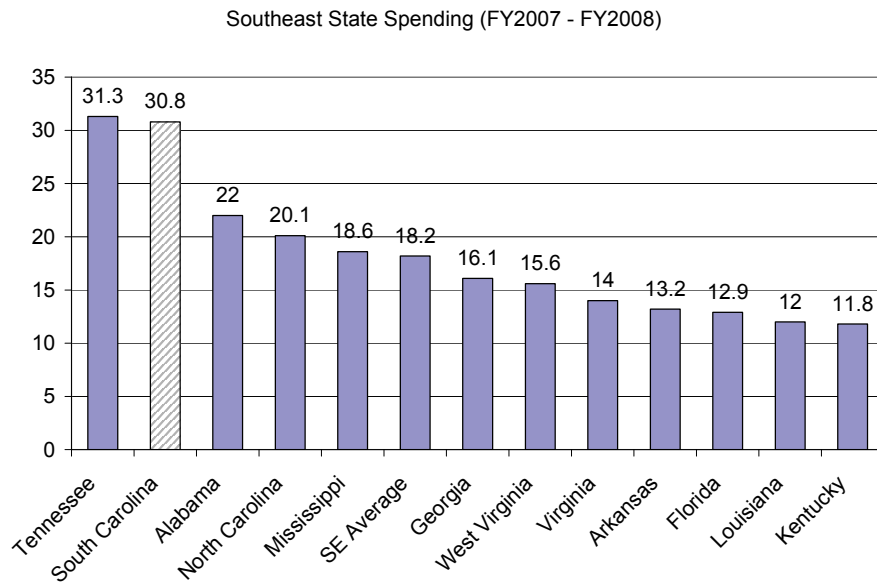
We have said for six years now that there should be a wholesale change to budgeting that requires legislators in Columbia to take a longer term approach and stop growing government faster than the underlying economy. Budgets of previous years simply spent all of the money coming to Columbia with what seemed very little consideration of a future economic downturn. This notion of good times and bad times dates all the way back to the Biblical story of the seven fat cows and the seven skinny cows. During times of prosperity, we failed to restrain spending and, as a result, we are forced to cut programs to the bone when times get tough.

Times are now tough. Our current budget problems were predictable, preventable and guaranteed based on the run-up in state spending over the past four years and ignoring our call for spending limits. State spending has increased by 40 percent over the past four years alone, and the simple reality that gravity always works and trees don't grow to the sky has been ignored. What goes up must come down, and our state is now learning that lesson at the expense of taxpayers, those who work in government and those served by government.

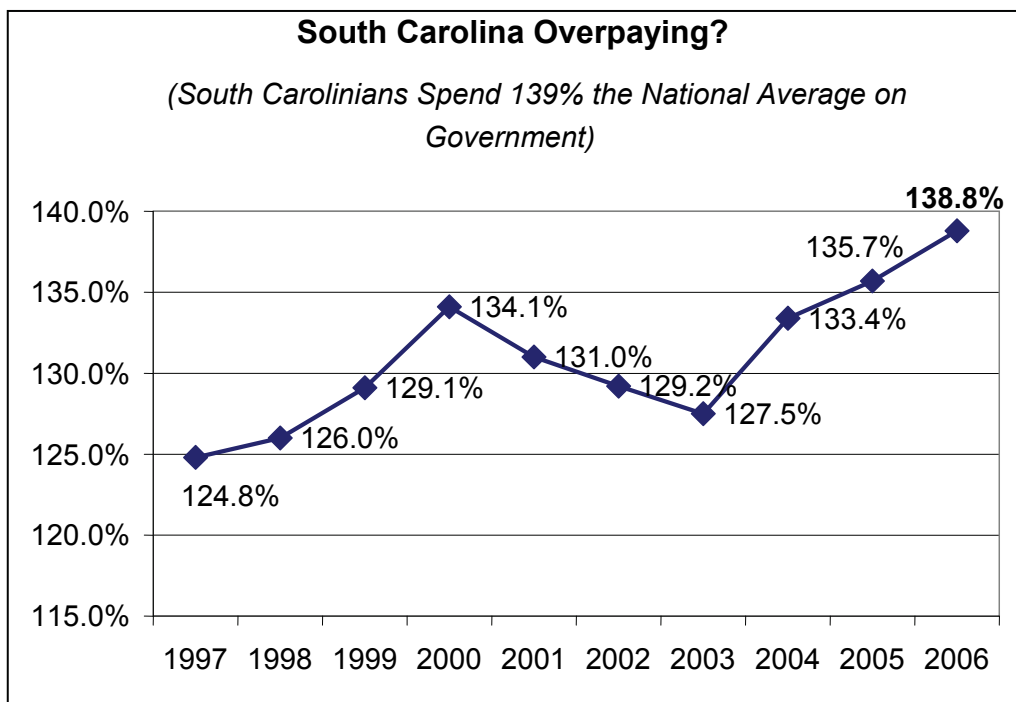
Even as the economy was clearly on the decline last year, the General Assembly appropriated money with the full expectation that anticipated revenues would be sufficient to cover all state government expenditures. Unfortunately, today state agencies are paying dearly for past bad budgeting practices as the good times are over. In fact, tax revenues are falling short and are set to decrease for only the third time in 50 years. That is why a fundamental belief of this administration is that excessive government spending cannot be sustained in the long run.

Outspending the Competition

It is important for us to remain competitive in this ever-changing global marketplace, and to do this, we must be held accountable for every tax dollar spent. Prior to the current fiscal year, South Carolina grew the size of government the second fastest in the Southeast from FY 2007 to FY 2008. In fact, government spending increased by over 30 percent during this time period, according to the National Association of State Budget Officers.



At a national level, the story is not much better. Government in South Carolina costs almost 140 percent the United States average. This figure is cause for concern as we strive to compete against other states and attempt to invest valuable tax dollars back into the private sector.



All Services Not Created Equal

In October of last year, the General Assembly, to its credit, reconvened in special session to take up targeted cuts instead of simply taking the politically expedient route of allowing the Budget and Control Board to order across-the-board cuts. We were very pleased to see the House and Senate adopt a targeted plan that recognized all services are not created equal and made cuts accordingly. On the other hand, we were disappointed that the majority of the Budget and Control Board voted against this practice with, instead, a seven percent across-the-board cut last December. It is our hope and expectation that using a targeted method will be the rule rather than the exception in addressing future budget shortfalls.

We believe we have yet to see the worst of the financial storm our state and country will experience. This administration has been warning for years about the dangers of unsustainable spending, an inefficient and unaccountable structure, and poor budgeting practices leading up to these tough times. Our state found itself in the red last year, and we do not believe this is the last of the budget shortfalls for FY 2008-09. The outlook for the next fiscal year appears to be the same. This means that we must continue to evaluate our core governmental functions and programs and prioritize them based on their importance. All functions and programs are not created equally, and that is why this administration has consistently opposed across-the-board budget cuts. This type of budgeting makes it difficult to eliminate the least vital government functions and programs and to fully protect those that are most essential.

Bottom line, given the continued deceleration in the national economy, we urge the General Assembly to make reduction decisions using responsible targeted cuts.

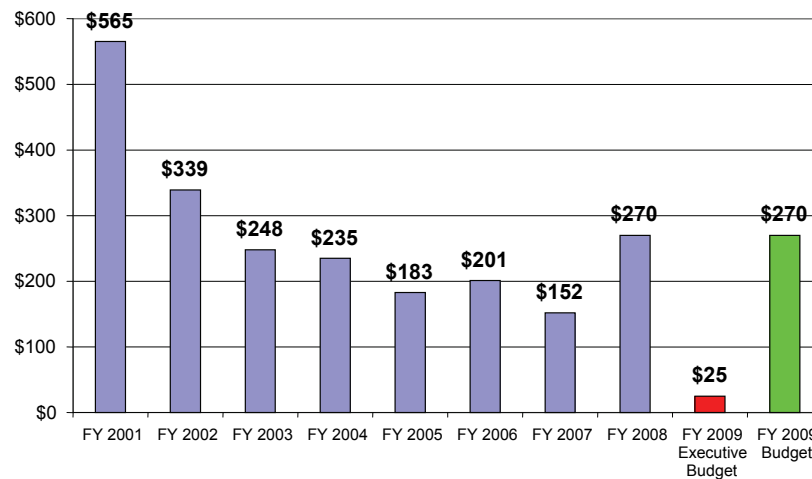
Annualizations on the Rise

To put our state's fiscal house in order, we must stop the practice of annualizations – using one-time money to fund recurring needs. Annualizations represent borrowing from Peter to pay Paul and ultimately only serve to delay tough decisions by putting off budget pain for another year. The problem with doing so is evident as annualizations nearly doubled in the preceding two years, making the hole we have to climb out of this year even deeper. With the passage of the FY 2008-09 Appropriations Act, we are concerned that the state's annualization total for the year is back to a seven year high of around \$270 million – ultimately meaning we are starting the next fiscal year in a very deep hole that has grown deeper with the declining national economy.

Even more distressing, a large portion of last year's annualizations were a result of budget raids on the Department of Health and Human Services Medicaid reserves in the amount of \$100 million. We believed raiding the reserve funds was especially inappropriate because it came right on the heels of a massive expansion of over \$21 million in the Medicaid SCHIP program in the last appropriations act. Using Medicaid reserve funds to fulfill other recurring obligations was especially shortsighted given the weakening economy – as unemployment rises, the Medicaid-eligible population grows and the state's costs increase.

We believe there needs to be a limit on annualization spending, which is why we continue to ask that annualizations not exceed one percent of total estimated revenue for a fiscal year. This executive budget falls below this level at only **\$32.8 million**.

South Carolina Annualizations Since FY 2000-01



Unfunded Liabilities

Public pension....funding is woefully inadequate. Because the fuse on this time bomb is long, politicians flinch from inflicting tax pain, given that problems will only become apparent long after these officials have departed. Promises involving....generous cost-of-living adjustments are easy for these officials to make....those promises will be anything but easy to keep.

- **Warren Buffett (2007 letter to shareholders, writing about pension managers' projections of 8 percent returns)**

Our retirement system's last reported unfunded liability as of the end of June 2007 was over \$10 billion. However, this number is only a part of the picture as it does not include \$8.6 billion of unfunded Other Post Employment Benefits (OPEB) costs for retirees' health care. The combined \$18.6 billion in unfunded liabilities is a key reason this administration was against the proposal last year to double the guaranteed cost-of-living increase for retirees as it added over billions more in costs to the system.

Put another way, South Carolinians now hold an almost \$20 billion "I.O.U." for unpaid political promises for retiree salaries and health care. This invisible mortgage totals \$10,000 per taxpayer, and will only increase if we choose to pass it on to our children and grandchildren.

Specifically, H. 4876 changed the way mandatory and *ad hoc* Cost of Living Adjustments (COLA) are approved for state retirees. This new law potentially adds another \$2.6 billion to the \$20 billion unpaid-for political promise, while artificially boosting expected returns, to bizarrely justify more spending. Specifically, the eight percent investment return assumption is out of line with other states facing similar retirement issues. Factoring in inflation, our rate of return would move to five percent – higher than the national average and that of neighboring states. In fact, according to the

actuary group, Milliman, South Carolina's optimistic expectations are 11 percent higher than the national median for public funds, 33 percent higher than Georgia's retirement system, and 43 percent higher than North Carolina's.

Unfortunately, the \$18.6 billion number has gotten substantially worse over the past 18 months simply because our investment performance has (like that of most investments) been weak. For example, the Investment Commission reported losing 2.6 percent plus fees over the 12-month period ending last June. Our state has not yet reported its performance over the last six months of 2008, but considering the S&P 500 has dropped over 29 percent during this period, it can be expected that our portfolio has similar returns.

The bottom line is that our \$18.6 billion in unfunded liabilities has increased by billions of dollars over the past 18 months. While updated numbers will not be reported for a while, the frightening reality is that our combined retirement accounts likely will have less than half of the assets needed to pay our total anticipated long-term costs. These numbers will be even worse if we continue to under perform the 8 percent assumed rate of return adopted last summer.

In order to increase the solvency of our system, we must make long overdue changes now to lessen the potential of severe future pain for both taxpayers and retirees. The GEAR Report made the following common-sense recommendations for non-vested employees in order to shore up finances of the retirement systems:

- Base retirement income on the salary from the last five years of employment rather than the last three years.
- Discontinue the practice of applying unused vacation pay to the number before calculating retirement pay.
- Eliminate the TERI program.
- Discontinue the practice of applying unused sick leave to the length of service.
- Move back to a requirement of thirty years of service for full retirement (as is the standard in most states) as opposed to the reduced twenty-eight year requirement adopted by the legislature earlier this decade.

We support all of these proposals as ways to help staunch the financial bleeding, but we must go further in order to begin addressing our tens of billions in debt and keep our state's high credit rating. One way to do so is to ask retirees to start paying a larger percentage of their health care costs. Agencies (and thus taxpayers) have traditionally paid the same cost-share for health care for retirees as state employees. Currently, taxpayers are paying approximately 71 percent of the health care costs for retirees and their families. Over the past ten years, taxpayers have picked up between 67-82 percent of that cost with retirees paying the other 20-30 percent of the health care tab.

In FY 2009, retirees' total health cost is projected to be near \$360 million, which means that taxpayers will be paying over \$250 million this year for retirees' health care. This charge is paid through a surcharge on agencies' payrolls. That charge is increasing rapidly - from less than 2 percent of an agency's payroll in 1999 to 3.5 percent in the current budget year - an over 80 percent increase in the past decade.

Dropping the employers' surcharge for retiree health care costs back down to around 2.65 percent will free up about 0.85 percent of this payroll surcharge to use toward paying down unfunded liabilities for retirees. This change would free up about \$62 million in recurring funds that could be allocated to reducing the total unfunded liability of retirees' health care system by approximately \$2 billion.

This change would require retirees to start paying approximately 46 percent of their insurance cost that is not already covered by Medicare. By comparison, taxpayers in the state of Florida only pay a maximum of \$150 a month of health care costs per vested retiree based on a formula of \$5 per year of service. In South Carolina, taxpayers are paying over double that amount with an average of \$348 a month for a retiree's health care. The disparity is even larger when comparing employee's who worked for less than 30 years with their respective states. A report issued in 2000 by the South Carolina Chamber of Commerce showed that our state's retirement system was more generous than 90 percent of the major government pension systems in the country. Since that time, the legislature has even increased those benefits by guaranteeing a 2 percent annual cost of living increase for retirees.

On their website, the President of the South Carolina State Employees Association writes the following about how their benefits have been obtained (emphasis added):

demonstrations of our numerical strength have yielded retirement benefits second to none, a TERI program, 28 year retirement, pay raises and cost-of-living increases. None of these benefits came automatically. It is through the efforts of a united front of state employees and retirees, advocating for ourselves and others, who are not members, that all of these benefits accrued to us.

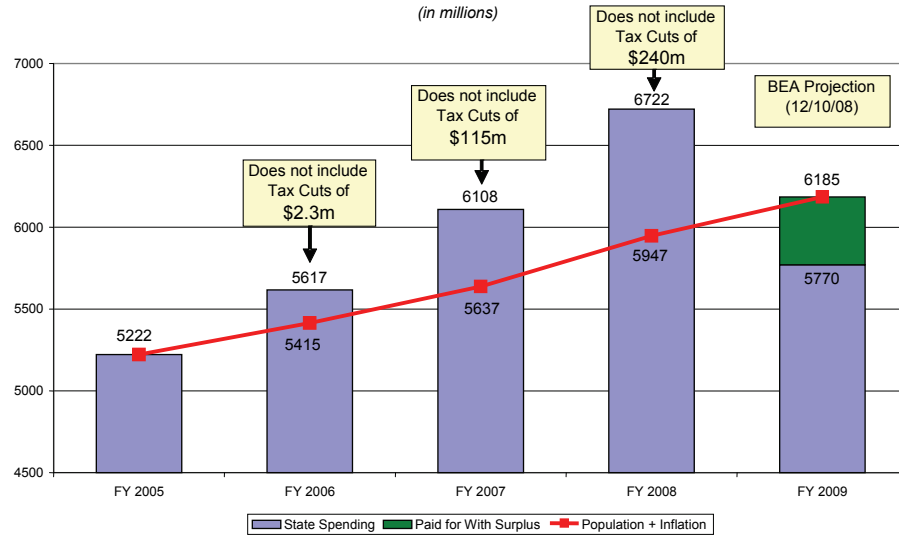
The reality is that benefits accruing to government retirees have to come from somewhere – in this case, current taxpayers. However, the tens of billions in unfunded future benefits – political promises that have been made but not funded – will either have to come from our children and grandchildren or the entire system will collapse under the weight of its debt. Most taxpayers in South Carolina cannot afford retirement benefits “second to none” for themselves, much less for hundreds of thousands of public retirees.

We continue to believe greater steps need to be taken so that the state's financial burdens are not handed to the next generation of taxpayers, and we urge the General Assembly to consider our concerns in the next legislative session with the above recommended reforms.

Population Plus Inflation

In past years, we have laid out our case for holding the growth in government to a rate that is equal to the growth in population plus the growth in inflation. Adhering to this spending limit was especially important considering the large amounts of new revenue coming in during past budget cycles. As the chart below illustrates, the population plus inflation threshold has been exceeded in the three budgets where it was needed the most.

State Government Growth - Just Recurring Dollars
FY2005 - FY2009
(in millions)



Regrettably, the failure to adhere to a spending limit has made a bad budget situation even worse due to the unprecedented economic downturn. We believe that when economic times are good, budget writers must resist the temptation to spend excessive tax dollars on new programs that cannot be sustained when challenging financial times are upon us.

We will again push for permanent legislation that caps spending in the upcoming session. Our proposal is simple: we must keep spending in line with population plus inflation. Specifically, the population plus inflation limit must apply to all recurring and nonrecurring appropriations during a fiscal year – excluding federal and other funds; EIA revenue; Education Lottery revenue; Capital Reserve Fund yearly funding requirements; General Reserve Fund yearly funding requirements; Local Government Fund yearly funding requirements; Capital Reserve Fund appropriations; Department of Transportation revenue; and general fund revenue used for the tax relief trust fund, to replenish any trust or reserve accounts, or to prepay debt. We believe that any excess revenue over the cap should be used in one of the following ways: (1) to be deposited into an additional reserve fund to pay down existing debt, or (2) to be returned to taxpayers across the state.

Spending Transparency

We might hope to see the finances of the Union as clear and intelligible as a merchant's books, so that every member of Congress and every man of any mind in the Union should be able to comprehend them, to investigate abuses, and consequently to control them.

– Thomas Jefferson

This administration believes that South Carolinians are entitled to easy access to full and complete information regarding how their hard-earned tax dollars are being spent by state government. Increasing transparency of state government spending leads to more accountability to taxpayers of South Carolina.

In this vein, we announced this past session the completion of a new state Spending Transparency website aimed at providing citizens with a greater degree of information about how their tax dollars are used. The site was created pursuant to a Spending Transparency Executive Order issued in 2007 and developed in concert with Comptroller General Richard Eckstrom's office. The site, which is found at <https://ssl.sc.gov/SpendingTransparency>, contains reports collected by the Comptroller General's Office on all agencies' funds expended and their sources.

These websites give voters the ability to hold government accountable for the decisions it makes. The new site provides another tool for our citizens to have the maximum amount of information about how their government operates and how their tax dollars are being spent.

Modernize Government

Modernize Government

South Carolina [government] still runs on its 1895 constitution. Guess what? It doesn't work.

– Josh Goodman, *Governing Magazine* (August 2008)

An Archaic Government – A Historical Perspective

In 2008, South Carolina's government structure still largely resembles the government first established by a 113-year-old state Constitution during a period of racial turmoil and with the primary goal of diluting executive power. In this rapidly transforming world that is defined by innovation, competition, and globalization, South Carolina will be left behind if we continue to hold on to the vestiges of the past and fail to modernize and restructure state government.

The 1895 state Constitution was adopted as a response to two things: 1) the 1865 state Constitution failed to meet Congress' requirement that all states adopt the 14th Amendment giving blacks equal protection of the laws, which resulted in Congress abolishing South Carolina's General Assembly and 2) to the dismay of state leaders like Ben "Pitchfork" Tillman, the 1868 state Constitution afforded too many rights to blacks. In 1890, Tillman was elected governor, and in his inaugural address he best summed up the purpose and intent of the 1895 Constitution stating, "The whites ... have absolute control of the State government, and we intend any and all hazards to retain it."¹ This was accomplished by denying equal rights for blacks, requiring literacy tests and poll taxes to vote, separating schools, prohibiting interracial marriages, and spreading power among several areas of government due to fear of a governor, especially a black governor, having too much power.

At a time when most other states and the federal government were moving toward executive centrality, the 1895 Constitution adopted the "long ballot," which required the governor to share executive power among nine constitutionally elected officers. Ironically, this constitution also afforded the governor a "chief executive" role, and yet the long ballot and other measures adopted by the General Assembly prevented him from carrying out his duty to ***actually be a chief executive*** and manage the administrative and executive functions of state government. For example, even though many other states were in the midst of budget reforms to give the chief executive more control over government spending, in 1919 the General Assembly created a three-member Budget Commission, today known as the Budget and Control Board, made up of the governor and the chairmen of House Ways and Means and Senate Finance Committees to ensure legislative dominance over spending policy.² Remarkably, this mindset continues almost a century later.

In addition to creating the archaically-structured Budget and Control Board, the General Assembly also diluted executive power by creating numerous state agencies without direct accountability to the Chief Executive. Up until 1993, state government amassed ***145 agencies*** and not one was directly

¹ Walter Edgar, *South Carolina: A History*, p.11, University of South Carolina (1998).

² Luther F. Carter and Richard Young, *The South Carolina Governor*, p.13, University of South Carolina (2003).

under the control of the governor. Most were governed by a board or commission appointed by the governor, Legislature, or both.

This menagerie of governance forms has resulted in fragmentation, confusion, redundancy, and a lack of accountability in state government that continues today. Fourteen major restructuring studies conducted over the course of 87 years came to the same conclusion and recommended that the General Assembly consolidate state government and centralize executive authority.

Amazingly, just fifteen years ago a movement to restructure and modernize state government began. Now fourteen agencies are part of the governor's cabinet, and the governor can finally submit his own executive budget proposal, which, until 1993, was prepared and submitted by the Budget and Control Board.

While we have made some progress toward moving South Carolina out of the 19th century, we have a long way to go to modernize state government and join the rest of the nation in the 21st century.

An Inefficient Government – The Numbers

This administration has said for six years now that government should be reorganized to run like a business focused on both its customers and its costs, not its own interests. Becoming more efficient, effective and accountable to the taxpayer ultimately results in less waste, better services, and surpluses being returned to the taxpayer.

Unfortunately, despite this administration's persistent calls for restructuring and spending restraint, government continues to grow, spending continues to increase, and accountability has not improved. This lack of efficiency and accountability is most apparent when looking at the following statistics:

- For every 10,000 South Carolinians, there are 234 state employees, which is 35 percent more than the U.S. average.
- In South Carolina the cost of government is almost 140 percent the national average.
- In South Carolina we pay more than 17.2 percent of our personal income for government, while the national average is less than 13.1 percent.
- The average wages for state residents grew 6.3 percent in FY 2007-08, while state government spending grew 15.7 percent. For every new dollar earned by the average South Carolinian, government spent an additional \$2.49.

Due to these excesses, our state is now struggling to deal with a \$1.001 billion budget shortfall that could have been mitigated if the state had already begun the process of restructuring six years ago. Fortunately, the General Assembly has an opportunity to restructure state government to address these budget shortfalls in the new legislative session. Government restructuring will not only help salve the current budget crisis but will also help avoid further near-term shortfalls and stabilize government growth in the long term. This executive budget provides a roadmap for deriving much-needed savings while making government more efficient and accountable.

A Proven Solution – Evidence that Restructuring Works

For six years we have presented our restructuring proposals to the General Assembly, and for six years we have heard the same question from legislators – show me how restructuring will make government more efficient and effective. Our administration has responded by pointing to the numerous studies performed over the course of 87 years and the undeniable efficiencies achieved by agencies that are part of an accountable, cabinet structure.

Restructuring Studies

Dating back to as early as 1920 and as late as 2007, 14 major restructuring studies have consistently found that South Carolina state government is too large, fragmented, unwieldy, and unaccountable.

The first in-depth report came in 1991 out of the South Carolina Commission on Government Restructuring formed by Governor Campbell and co-chaired by Lt. Governor Nick Theodore and House Speaker David Wilkins. This study determined that a prescription for better government is an overall state structure that:

- Establishes clear lines of authority, responsibility, and accountability;
- Concentrates Executive Branch authority, responsibility, and accountability;
- Creates a manageable span of control;
- Integrates functions into a smaller number of departments;
- Enhances the responsiveness of state government to the needs of South Carolina's citizens; and
- Seeks continuous improvement of the quality of policies and procedures.

The study also concluded that:

The cabinet form of government ... will lead to a unity in direction and purpose of state government through a clearly defined hierarchical structure, headed by the state's highest elected official. An elected chief executive, responsible for administration and with the power to make the bureaucracy work, is in the best position to achieve administrative effectiveness and political accountability.

Using this prescription, the 1991 Commission proposed to consolidate 145 state agencies, boards and commissions into fifteen cabinet departments. In 1993, the General Assembly adopted about half of the Commission's proposal. Three reports since that time reaffirmed the need to finish implementing the 1991 proposal to fully modernize state government – the 2003 Task Force on Government Restructuring and Campaign Finance Report, the 2003 MAP Commission Report, and the 2007 GEAR Commission Report.

The 2003 Governor's Commission on Management, Accountability, and Performance (MAP) also found areas in our state government that are duplicative, inefficient, or just plain wasteful and determined that further government restructuring would result in a first-year's savings of \$225

million, followed by savings of \$300 million in future years. The math is simple. The total savings, after four years of implementation, would be \$1.43 billion.³

In 2007, the Government Efficiency and Accountability Review (GEAR) Committee focused its study on the Budget and Control Board and found ways to reduce costs, increase accountability, improve services, consolidate functions, return functions to the private sector, and help our state become more competitive in a global economy. The committee offered 61 recommendations which, if implemented, would save the taxpayers almost \$500 million over the next few years – a significant amount that could have helped relieve our current budget shortfall problems.

Study after study has concluded that our current government structure is cumbersome, fragmented, inefficient and unaccountable. Each of these studies has shown that meaningful government restructuring is the prescription for these ailments. To the General Assembly's credit, part of the prescription was implemented and has proven the cabinet form of government works. It is time for the General Assembly to take the next step to fully implement the restructuring plans set forth in 1991 and proposed in this executive budget.

Proven Examples

While numerous studies have shown that a streamlined, cabinet form of government is better, our administration has proven it actually works. From the Department of Corrections' nationally-recognized efficiencies in food and medical costs to the State Parks Service becoming one of the top ten most self-sufficient systems in the nation, our administration has produced dozens of examples of how accountability leads to more efficient and effective government. The Department of Motor Vehicles has provided the most dramatic example of how a simplified cabinet agency can save money and, at the same time, provide better services. Since 2003, DMV has drastically slashed wait times, provided customers with online alternatives to visiting physical offices, and all the while returned over \$40 million in savings to the General Fund from FY 2005 to FY 2007. As recently as the passage of the FY 2008-09 Rescission Appropriations Act, DMV offered another \$10 million in surpluses to the General Fund which was used to shore up budget shortfalls.

Here are some other examples of how an accountable, cabinet structure produces results:

- The Department of Parks, Recreation and Tourism reorganized the agency by aligning the human capital and financial resources to assure maximum funds were allocated to the higher priority program areas. As a result, PRT has reduced the personal services budget by over \$1 million and the operating budget by more than \$4 million over the past five years. The agency also currently operates with 107 less FTE's than in FY 2002, allowing it to reinvest those savings in advertising – with a return of \$23 for each dollar invested.
- The Department of Corrections built a grist mill and expanded poultry operation for eggs, saving taxpayers \$750,000 annually. The agency also

³ If those savings were returned to the taxpayers, each person would receive \$329.77, each taxpayer would receive \$725.25, and each family would receive \$1,269.23.

cut 70 teachers and administrative staff and replaced them with TV lessons beamed in by satellite, saving more than \$4 million.

- Under our administration, the Department of Commerce reduced its staff and budget by 25 percent and still exceeded its capital investment goal by \$1.1 billion and its jobs goal by 30 percent.
- The Department of Social Services has achieved a total savings of \$4,726,000, a 5.2 percent savings from their FY 2003-04 General Fund Appropriation of \$90 million, which includes the following: reduction in force (\$2.5 million); mandatory furlough (\$1.8 million); consolidation of office space (\$225,000); reduction in the number of state vehicles (\$122,000); elimination of same-day meal reimbursement (\$45,000); reduction in the number of cell phones (\$34,000).
- The Department of Transportation, the most recent addition to the governor's cabinet, has already achieved significant cost savings. In 2007, DOT realized one-time cost savings totaling \$17.8 million and annual cost savings of \$9.7 million by implementing new initiatives including decreasing agency travel and fuel consumption, aggressively negotiating legal claims against the agency, and ending contracts for two lobbyists which had cost \$20,000 per month.
- The Department of Motor Vehicles, which joined the cabinet in 2003, continues to prove that a government agency can provide quality services at low cost and meet expectations that consumers demand of private-sector businesses. DMV has transformed itself into a self-sustaining agency, returning over \$50 million in surpluses since 2005 to the General Fund. It has also dramatically improved services by integrating technology allowing drivers to renew and make changes to their drivers' licenses online, pay fees with credit cards, and receive a new license in the mail in just a couple of days.

These are just a few examples that prove a cabinet structure leads to better government. Such a structure facilitates leadership, direction, supervision, and evaluation from a responsible chief executive who is directly accountable to the citizens he serves. We believe, and our cabinet agencies' performance shows, that an elected chief executive, bound by the Constitution and accountable to voters to perform successfully, is in the best position to achieve effectiveness and political accountability.

A Government Ready for Change

...[T]he chances seem good that, before too long, South Carolina government will step out of its 19th century clothing and move toward the structure that prevails virtually everywhere else in America.

– Josh Goodman, *Governing Magazine* (August 2008)

This year South Carolina is struggling through a severe budget shortfall and economic downturn with no signs of ending in the near future. While the weakened national economy has deepened our budget shortfall, it is undeniable that spending restraint, better budgeting practices, and a more efficient and accountable government structure could have softened the economic blow. Unfortunately, our state is learning that lesson at the expense of taxpayers, those who work in government and those served by government.

While this moment is challenging, it is also an opportunity to permanently streamline and simplify government and make the chief executive directly responsible for government's performance, or lack thereof, to the taxpayers and the citizens it serves. President Ronald Reagan captured this moment appropriately in his nomination acceptance speech in 1980, quoting President Franklin D. Roosevelt when he said:

And the time is now to redeem promises once made to the American people by another candidate, in another time and another place. He said, "For three long years I have been going up and down this country preaching that government – federal, state, and local – costs too much. I shall not stop that preaching. As an immediate program of action, we must abolish useless offices. We must eliminate unnecessary functions of government...we must consolidate subdivisions of government and, like the private citizen, give up luxuries which we can no longer afford."

It is time for the General Assembly to rise above parochial and political interests and make the necessary changes, including the Restructuring Plan outlined in this budget, which will have a lasting impact for the taxpayers, the next economic downturn, and improved government services.

We have been very pleased to see the House of Representatives pass several parts of our restructuring plans over the years, and in 2008, the House unanimously passed measures to consolidate health care agency functions and overhaul the Budget and Control Board into an accountable, efficient Department of Administration. The House has also adopted constitutional amendments to ask voters to unify the Executive Branch by reducing the number of constitutional officers. The time has long passed for the Senate to follow suit.

This January we ask the General Assembly to quickly adopt the House-passed Department of Administration bill and reconsider our complete Restructuring Plan for the reasons we have explained in this section.

Our Restructuring Plan

Our plan includes three major goals and specific agency reorganization recommendations to accomplish these goals which are explained below.

1. Create Executive Accountability of Central Administrative Functions

As with private corporations, accountability is essential for governments to function properly. Yet South Carolina is the only state in the country that empowers a quasi-legislative/executive board, the Budget and Control Board, to oversee the state's administrative support functions. To establish accountability and better manage support services to state agencies, we propose the placement of crucial Budget and Control Board-managed administrative functions within a cabinet-level Department of Administration.

As discussed earlier, the Board was created out of an archaic system grounded in legislative dominance and fear of a modern centralized government. In 1919, during a nationwide movement to centralize budgetary policy making in the executive branch, the South Carolina General Assembly instead "compromised" by creating a Budget Commission made up of the Governor and the Chairmen of the House Ways and Means and Senate Finance Committees. For the next three decades, despite the legislative imbalance, the Budget Commission expanded its power to include administrative and executive functions, and by the 1940s, the Commission was exercising fiscal authority that governors in other states exercised unilaterally.⁴

Today, the Budget and Control Board, now a five-member board, is an enormous institution which employs more than 1,100 people and provides nearly every state agency with a variety of services and support, ranging from procurement and mail delivery, to human resources and data/telecommunications services, to retirement and building maintenance. Nearly a century later, the five-headed structure of the board is dominated by legislative influence that undermines the constitutionally-based principles of separation of powers and checks and balances of the legislative and executive branches.

This cumbersome structure also results in a lack of accountability and contributes to many services of the Board costing too much. The chief executive of any well-run company or well-run state must have a direct line of authority to have the accountability necessary for success. As previously mentioned, to highlight the inefficiencies that exist under the current Budget and Control Board framework, we established the Government Efficiency and Accountability Review Committee in 2007. In addition to finding \$500 million in potential savings, the committee also found that the Budget and Control Board could release at least \$20 million in carry-forward funds to the General Fund, a surplus formed by overcharging state agencies for IT services, which could greatly ease the current budget woes. Further, the GEAR Committee found another \$146 million that could be re-allocated to fund more pressing needs of the state. We again urge the General Assembly to reconsider the GEAR Committee's recommendations.

More importantly, we again urge the General Assembly to create a Department of Administration to manage the state's central administrative functions, including the daily operations of state

⁴ Luther F. Carter and Richard Young, *The South Carolina Governor*, p.13, University of South Carolina (2003).

government. As the state's chief executive officer, the governor should be responsible for the central administration of the executive branch – a responsibility given to every other governor in the nation.

Budget and Control Board Restructuring Plan

Create a Department of Administration with a director appointed by the governor and confirmed by the Senate.

From the Budget and Control Board and the Governor's Office:

1. Office of General Services – Our state owns over 8,000 buildings comprising 60 million square feet of space with no central authority to make management decisions. Tens or even hundreds of thousands of square feet of state-owned office space sits vacant, yet the state leases hundreds of thousands more square feet of office space from the private sector.
2. Office of Human Resources – Not having any one person in charge or responsible can allow for the perpetuation of programs that need to be fixed or ended.
3. Employee Insurance Program.
4. Chief Information Officer – This office has the potential to give state agencies the principal means to improve delivery of IT services and lower the cost of government, but it has yet to accomplish these goals and is not directly responsible or accountable for this failure. It is telling that in six years there have been four CIOs.
5. Energy Office.
6. Division of Procurement Services – Our state's antiquated procurement system, currently overseen by the Budget and Control Board, sometimes serves as a roadblock that unnecessarily slows down time-sensitive projects. For instance, the Department of Parks, Recreation and Tourism recently engaged the procurement system to assist them in outsourcing the state's bait and tackle shops. What should have been a simple procurement matter was delayed, thereby preventing PRT from outsourcing these shops within a reasonable timeframe.
7. Division of Internal Audit and Performance Review.
8. Research and Statistics (excluding Digital Cartography and Precinct Demographics) – Digital Cartography and Precinct Demographics are related to redistricting after the Decennial Census, which is largely a legislative branch function.
9. One-half of the Executive Director's office.
10. One-half of the Internal Operations office.
11. Governor's Office of Executive Policy and Programs (excluding Guardian *ad Litem* Office, Continuum of Care, and the state Ombudsman).

Budget and Control Board responsibilities

By moving central administrative functions to the governor's cabinet as identified above, the Budget and Control Board would then be free to focus on key areas of state fiscal policy, specifically by:

1. Approving state revenue and expenditure projections.
2. Authorizing the issuance of bonds.
3. Addressing budgetary shortfalls.
4. Administering the State Retirement System.
5. Exercising other specific fiscal responsibilities, as enumerated by law.

We also propose that the Department of Administration house the State Inspector General.

Department of Administration – Inspector General

State Inspector General – We propose creating a central office responsible for identifying waste, fraud, and abuse within the executive branch. The Inspector General's Office would be established and appointed for a six-year term in the same manner as the Chief of the State Law Enforcement Division. The Inspector General would be nominated by the governor and confirmed by the Senate, serving a six-year term.

2. Modernize the Executive Branch's Organizational Structure

The South Carolina Constitution, ratified in 1895 when all women and most African Americans were effectively disenfranchised, established a very weak executive branch of government, which shares institutional branch power, along with accountability and responsibility, among the governor and eight statewide constitutional officers. Such a large number of elected executive branch officials frequently results in our government working at cross-purposes and producing inconsistent and conflicting public policy. While feigning voter engagement, the current Executive Branch structure actually results in a bifurcated system with no clear lines of responsibility. South Carolina will be better served by having these officers appointed by the governor.

For an example, look to the Superintendent of Education. One of the primary issues in the gubernatorial campaign every four years is education. Our state's struggles in education are well-documented, so our citizens naturally want clear lines of accountability for the reasons behind those struggles – yet no clear lines exist. The governor has little authority to implement any reforms, no matter how desperately they are needed and no matter how loud the citizens cry for help. Accountability in the area of education is shared among the 170 members of the General Assembly, the Superintendent of Education, the state Board of Education, and the governor. With so many "leaders," there is no accountability. A gubernatorial appointment of the Superintendent of Education will not solve all of our education problems, and we are not suggesting it will. However, a cabinet-level Superintendent will provide one coherent education policy throughout South

Carolina and a direct line of accountability to the governor, who will ultimately be responsible for the rate of progress within our public education system.

Another more current example is our administration's concerns over the recent program created by the Lieutenant Governor's office called Senior Shield that would help senior citizens identify legitimate businesses in the state. While our administration supports the good intentions of this program, we do not believe the state should be spending scarce dollars on an endeavor that is largely duplicative of other consumer protection programs already available in the public and private sectors. Our differing takes on whether to implement this new program would not be an issue if the governor and lieutenant governor ran on the same ticket. This example is also emblematic of the larger problem within state government – the governor is unable to speak with a unified voice to citizens and taxpayers because he must share executive authority with eight statewide constitutional officers.

The House of Representatives, in 2005 and 2008, adopted measures to reduce the number of constitutional officers. We hope this legislative session the Senate will finally follow suit. We propose, once more, the reduction and restructuring of the state's constitutional officers as follows:

Place the Governor and Lieutenant Governor on the same ticket.

In the long-standing tradition of the federal executive branch, where the President and Vice President run on the same ballot, we propose having the Governor and Lieutenant Governor run together as a team (as they do in 24 other states).

Make the following cabinet positions appointed by the Governor, with the advice and consent of the Senate:

1. **Adjutant General** – In an effort to depoliticize the military branch of state government and to provide a greater degree of accountability within the governor's constitutionally-established role as "commander-in-chief," we propose having the Adjutant General appointed by the governor (as in 49 other states).
2. **Commissioner of Agriculture** – As with the Adjutant General, to streamline the executive branch and provide greater accountability, we propose having the Commissioner of Agriculture appointed by the governor (as they do in 30 other states). Additionally, the governor would be accountable for a major economic sector of the state.
3. **State Superintendent of Education** – We propose having the state Superintendent of Education appointed by the governor (as they do in 11 other states) to provide central accountability for the state's public education system.
4. **Secretary of State** – As has been proposed by many people, including former Secretaries of State, we propose having this officer appointed by the governor (as they do in 10 other states).

3. Simplify, Streamline, and Create More Accountability in Government

Fourteen major reorganization studies of South Carolina's government over the last 87 years have reached a similar conclusion: South Carolina's government has far too many agencies, making it disjointed, unwieldy, and unaccountable. We have a hodgepodge of 70 independent agencies, commissions, and departments, which provide hundreds of public programs or services, many of them redundant.

While a cabinet form of government was in some measure created in 1993, consolidating 76 agencies into 13 cabinet offices, more than 80 percent of our state government remains outside the management and oversight of the state's chief executive – the governor. To provide better service and better value to our clients – the taxpayers – we need to consolidate departments with similar missions under the cabinet.

As discussed earlier in this section, a framework for better state government, as gleaned from the major reorganization studies, is based on six principles:

1. Establish clear lines of authority, responsibility, and accountability;
2. Concentrate the authority and accountability at a single point, the governor;
3. Accord responsibility in a reasonable and manageable manner;
4. Integrate governmental functions into a small number of departments;
5. Enhance state government's responsiveness to the needs of the citizens; and
6. Seek continuous improvement in the quality and effectiveness of state government through emphasis on customer service, strategic planning, and other quality management principles.

Guided by these six principles, our proposal seeks to consolidate, simplify, and make our state agencies more accountable – a task which becomes more feasible through a strong cabinet form of government, headed by the governor.

We anticipate adoption of our Restructuring Plan in this area will result in savings of over \$21 million for FY 2009-10.

Education Restructuring Plan

Both the MAP Commission and the South Carolina Commission on Government Restructuring recognized the need to consolidate educational programs with similar missions, policies and programs to provide better opportunities for coordination and prevent competition for scarce resources. Accordingly, we propose a more coordinated education reorganization plan as follows:

State Department of Education

1. Transfer the powers of the State Board of Education to the Superintendent of Education, who would be appointed by the governor subject to Senate confirmation.
2. Move ETV, the Wil Lou Gray Opportunity School, School for the Deaf and Blind, the John de la Howe School, the Governor's School for Science and Mathematics, and the Governor's School for the Arts and Humanities under the administrative direction of the State Department of Education. **Savings: \$1,166,844**

The powers of the current boards at ETV, Wil Lou Gray Opportunity School, School for the Deaf and Blind, the John de la Howe School, the Governor's School for Science and Mathematics, and the Governor's School for the Arts and Humanities would be given to the Superintendent of Education, and the members of the boards would serve as an advisory board.

Health Care Restructuring Plan

Our state health and human service delivery system is fragmented and disjointed, with too many agencies providing redundant and costly services. In January 2003, the Legislative Audit Council (LAC) conducted an in-depth study of our eight health and human service agencies, finding that five of the eight agencies are outside the governor's cabinet. The LAC also found that similar services are provided by multiple agencies, causing the expenditure of extra resources – in a state without extra resources to spend – on service coordination. Predictably, the costs were due to administrative overlap and were primarily found in the areas of finance, personnel, and information technology.

The LAC report also found, as most of the health and human services agencies are outside the cabinet, that there is “no central point of accountability for [the agencies’] performance.” Further, the report indicated that “[a] cabinet system could increase accountability and responsiveness to client concerns by directly linking the performance of agencies with a single statewide elected official who is authorized to implement changes.” The report concluded:

If programs with similar services were consolidated into fewer agencies, under the authority of a single cabinet secretary, obtaining help from state government could be made less complex. The need for different agencies to make referrals to each other could be reduced while planning and budgeting could be done more comprehensively. In most cases, administrative costs could be lower.

In October 2004, the LAC produced a follow-up report, which concluded that while a few minor recommendations had been made, none of the health and human service restructuring recommendations had been implemented. More than four years later, similar services are still provided by multiple agencies, and there is still no single point of accountability for their performance.

Most recently, in November 2008, the LAC released a new audit of the Department of Disabilities and Special Needs (DDSN) which cited numerous incidents of inefficiencies and failures to follow agency protocols. This report reaffirms our previous proposals of making DDSN directly accountable to the governor, who can hold this agency responsible to the families it serves.

We largely agree with the LAC reports, and we have based much of our proposed structure around their findings. Our main concern is the need for services to efficiently and effectively meet the needs and choices of consumers – which our current system clearly fails to do.

We propose the merger of these health and human services agencies into one accountable and affordable delivery system under a cabinet-level director to improve accountability, care, and responsiveness to our citizens.

Department of Health Oversight and Finance

1. Rename the Department of Health and Human Services the Department of Health Oversight and Finance.
2. This agency will continue to be the lead agency for Medicaid oversight and finance of Medicaid expenditures.

Department of Health Services (Health Services)

1. Division of Public Health (currently the health programs at the Department of Health and Environmental Control). **Proposed Restructuring Savings: \$5,672,714**
2. Division of Mental Health (currently Department of Mental Health). **Savings: \$6,874,703**
 - The powers of the current Mental Health Commission would be given to the director of Health Services, and the members of the commission would serve as an advisory board.
 - Continuum of Care for Emotionally Disturbed Children would be moved from the Governor's Office to the new Division of Mental Health. **Savings: \$152,315**
3. Division of Disabilities and Special Needs (currently Department of Disabilities and Special Needs) **Savings: \$2,259,107**
 - The powers of the current Disabilities and Special Needs Commission would be given to the director of Health Services, and the commission would serve as an advisory board.
4. Division of Addiction Services (currently Department of Alcohol and Other Drug Abuse Services). **Savings: \$501,920**

Department of Rehabilitative Services

1. Merge the Vocational Rehabilitation Department and the Commission for the Blind. **Savings: \$654,826**
2. The administrative responsibilities of the Vocational Rehabilitation Department and the Commission for the Blind would be given to one director appointed by the governor with the advice and consent of the Senate.
3. The board members of the Vocational Rehabilitation Department and the Commission for the Blind would serve on advisory boards.

Department of Transportation Reform Plan

A priority for this administration in 2007 was to provide more accountability within the Department of Transportation (DOT). We were pleased to see the General Assembly adopt some of our recommendations by giving the governor the authority to appoint the Secretary and by creating standards by which road projects are prioritized. Initial indications show that a cabinet-level director is starting to produce results. DOT has saved at least \$25 million in taxpayer money by implementing new initiatives to reduce costs, including decreasing agency travel and fuel consumption and cutting off spending for a Washington lobbyist.

While these results are encouraging, we understand that true reform may take more than one attempt. The DOT Commission remains intact as a quasi-accountable entity and still has the ability to override the ranking criteria. To ensure true accountability and to provide a clear line of responsibility, we encourage the General Assembly to remove the remaining quasi-accountable system by eliminating the Commission.

The following proposed system will allow the Department of Transportation to be more accountable, more cost effective, and most importantly, will provide for improved transportation services for our citizens.

State Department of Transportation

Transfer the powers of the Commissioners of the state Department of Transportation to the Secretary of the Department of Transportation.

Environment and Natural Resources Restructuring Plan

South Carolina's environmental and natural resource programs are distributed among several state agencies. In our view, there should be a closer connection between the management of our natural resources and our environmental regulation. Furthermore, we believe to better protect our environmental resources and our citizens from health hazards, the Department of Health and Environmental Control (DHEC) should be split and managed in two separate entities under a more accountable cabinet structure.

The inefficiencies of our current system are exhibited by the bifurcated approach to water quality, which is managed by both the Department of Natural Resources (DNR) and DHEC. By combining the water conservation activities from DNR with the water regulatory activities from DHEC, we will be able to provide a cost-effective and comprehensive management approach to this crucial state resource. Additionally, the need for more accountability at DHEC is easily apparent due to numerous incidents where the agency has failed to balance business interests and their duty to prevent health hazards and adequately regulate environmental pollution. Without a direct line of accountability to the governor, DHEC will continue to be shielded from responsibility for its mistakes.

We believe that consolidating agencies with similar missions of protecting the environment and natural resources into a single agency under the governor – as we have proposed for the last several years – will increase accountability, reduce duplication, provide cost savings, and bring us in line with our neighboring states. For example, the North Carolina Department of Environment and Natural Resources and the Georgia Department of Natural Resources both provide environmental regulation and enforcement of wildlife laws.

We propose the creation of the Department of Environment and Natural Resources under a cabinet-level director, appointed by the governor and confirmed by the Senate. In light of recent events indicating DHEC's inability to adequately protect our citizens from health and environmental hazards, we also propose in the near term to bring DHEC into the cabinet, with a director appointed by the governor and confirmed by the Senate.

Department of Environment and Natural Resources (DENR)

1. Division of Environmental Protection (currently the Environmental Quality Control Division and the Ocean and Coastal Resource Management Division of the Department of Health and Environmental Control).
 - Maintain an environmental regulatory board.
2. Division of Natural Resources (currently the Department of Natural Resources). **Savings: \$1,095,026**
 - The powers of the current Department of Natural Resources Board would be given to the DENR director, and the members of the Board would serve as an advisory board.
3. Division of Forestry (currently the South Carolina Forestry Commission). **Savings: \$541,941**
 - The powers of the current Forestry Commission would be given to the DENR director, and the members of the Commission would serve as an advisory board.

Corrections and Probation Services Restructuring Plan

South Carolina is one of only ten states that separates the functions of the Department of Corrections from those of the Department of Probation, Parole, and Pardon Services (PPP). The agency will be led by a cabinet-level director, appointed by the governor with the advice and consent of the Senate.

A unified Department of Corrections and Probation will ensure that offenders are managed and measured by one agency from admission to final release, whether that release is directly from prison or from another degree of state supervision. Further, a unified corrections system will ensure consistent decisions about behavior and risk assessment for clients. We believe a unified system will have several other benefits, including:

1. Better coordination and exchange of information, resources, and personnel.
2. Savings from eliminating administrative duplication and allowing for better use of scarce programming resources in areas such as drug and alcohol treatment programs and re-entry programs.
3. A single point of contact for victims of crime to learn about the status of offenders from entry to sentence completion.

Our administration will continue to work with the General Assembly to develop a new alternative sentencing option for non-violent offenders. Yet, under the current structure, options such as restitution centers and electronic monitoring systems overlap the missions of these two agencies. By joining the entities, one agency will manage these related functions, and we will improve coordination, better manage limited resources, realize significant financial savings, and improve protection for law-abiding citizens.

Further, we propose combining the Parole Board at PPP with the Parole Board at the Department of Juvenile Justice (DJJ). Both Parole Boards control similar budgets, even though the DJJ Parole Board hears far fewer cases each year. As both boards have similar missions, their merger presents an opportunity to gain efficiencies and cost savings.

Department of Corrections and Probation
<ol style="list-style-type: none">1. Division of Corrections.2. Division of Probation, Parole and Pardon Services. Savings: \$622,126<ul style="list-style-type: none">– The PPP Parole Board would be combined with the DJJ Parole Board to perform probation, parole, and pardon functions. Savings: \$425,000

Economic Development Reform Plan

South Carolina's business leadership recognizes an unprecedented rapid transformation of the national and international economies. This transformation, the "emerging new economy," is defined by globalization with an ever-increasing reliance on knowledge-based technologies and is highlighted by intense competition, creativity, inventiveness, and innovation.

Our administration clearly acknowledges this economic phenomenon, and we sincerely hope the leadership in the General Assembly will join us. We have a mutual interest – the economic development of South Carolina – and we believe firmly that traditional approaches to economic development are out of sync with this emerging economy. No longer will a piecemeal, localized approach at economic development, led by 170 mini-Secretaries of Commerce suffice to bring

South Carolina into 21st century economic realities. Through cooperation, reflection, research, study, and planning, a modern comprehensive strategy can stabilize and energize South Carolina's economic engines. Further, we believe that the government should improve the economic "soil conditions" and allow the business sector to do what it does best. We propose four key objectives:

1. Bring together the relevant stakeholders – industry, academia, and government – to collaborate in developing a shared economic strategy for South Carolina.
2. Assess the competitive position of South Carolina and of the selected industry clusters in the state.
3. Identify key challenges, opportunities, and new strategic directions for South Carolina.
4. Promote consensus on an economic strategy and action agenda for South Carolina.

Our administration's primary goal is job creation and economic development. Numerous federal, state, and local resources are poured into programs to help create jobs and promote economic development, but our antiquated practice of ineffectively scattering these resources among multiple state agencies with minimally-distinguishable missions, along with our tendency to allow powerful legislators to spend significant resources on local projects that do nothing to promote economic development, minimizes the effect of these resources.

For an example of more effective use of resources, look to the Workforce Investment Act (WIA), which was created in 1998 to fund job training and employment programs. Moving the WIA program from the Employment Security Commission to the Department of Commerce a few years ago has ensured that over \$70 million in WIA funds will be used to help build the high-skilled workforce South Carolina needs in order to attract new industry.

To maximize the effect of our economic development dollars and to ensure a consistent, cohesive, and strong economic mission, we propose housing our economic development programs within a single agency. Further, the administrative savings would allow the greater resources to be focused on the core missions of job creation and economic development. Our proposed consolidation offers us a great tool in strengthening the focus of our resources in the most effective areas.

Department of Commerce
<ol style="list-style-type: none">1. Retain the current functions of the Department of Commerce.2. Office of Local Government (currently at the Budget and Control Board).

Literary and Cultural Resources Restructuring Plan

In 1991, the Commission on Government Restructuring recommended merging all four of our cultural and literary agencies under the administration of one agency. Unfortunately, the General Assembly did not include this change in its Restructuring Act of 1993. North Carolina consolidated its arts and cultural agencies in 1971. The North Carolina Department of Cultural Resources was formed by combining the Office of Archives and History with the Office of Arts and Libraries, and it is charged with providing cultural, artistic, and historic resources to the citizens of North Carolina in a unified manner. Our proposal is modeled after North Carolina's effective structure.

We believe the merger of these agencies will streamline management and reduce administrative costs, and accordingly, we submit the following proposal:

Department of Literary and Cultural Resources

1. Create a Department of Literary and Cultural Resources and DLCR Board.
 - The DLCR Board would be responsible for appointing the director of the agency.
 - The DLCR Board should have equal representation from each of the four areas to ensure fair and balanced weight.
2. Division of Archives and History (currently the Department of Archives and History). **Savings: \$198,858.** We also propose moving the Institute for Archeology and Anthropology from USC to this division. **Savings: \$496,812**
3. Division of Arts (currently the Arts Commission). **Savings: \$202,893**
4. State Library. **Savings: \$114,151**
5. State Museum. **Savings: \$114,438**

State Trust Fund Authority

South Carolina currently maintains a number of internal service funds that manage various risks related to public buildings, torts, medical malpractice, automobile use by public employees, health and disability, and workers' compensation, each of which is operated independently of the others. These funds include the Insurance Reserve Fund, Employee Insurance Programs Fund, State Accident Fund, Patients' Compensation Fund, Medical Malpractice Liability Insurance Joint Underwriting Association, and the Second Injury Fund.

We propose unifying the Insurance Reserve Fund, which manages the state's property and tort liability risks, and the State Accident Fund, which manages the state's workers' compensation risks. The risks managed by these funds are sufficiently related that they should be administered under the authority of one agency and one administrator. The creation of a Trust Fund Authority will eliminate duplicative overhead costs and will allow the coordinated management of these funds, while decreasing the risk of funds being used for non-prescribed uses. Other funds could be added to the State Trust Fund Authority over time. The State Trust Fund Authority administrator would be appointed by the governor with the advice and consent of the Senate.

State Trust Fund Authority

1. State Accident Fund.
2. Insurance Reserve Fund.

Create a Sunset Commission

“Nothing is so permanent as a temporary government program,” said the eminent economist Milton Friedman. Government programs in South Carolina have proven to be no different, even if the activity is something the public no longer needs.

To help mitigate the negative effects of never-ending government programs, we recommend establishing a sunset commission. According to the National Council of State Legislatures, “the sunset process was one of the first government accountability tools, dating back to the mid-1970s. Although individual sunset processes differ from state to state, a key feature of most processes is the inclusion of an automatic termination clause in the authorizing legislation for a particular state agency or program. Colorado was the first state to implement a sunset review process (in 1976), and within five years, more than two thirds of the states followed suit.”

Sunset commission recommendations, if adopted, can lead to significant taxpayer savings. An example: Texas enacted one of our country’s most progressive sunset programs in 1977.⁵ The Texas Sunset Advisory Commission assesses each agency’s structure and function and recommends that the Legislature re-charter the agency under its current operation, alter the agency’s operations, merge the agency with a similar agency, or eliminate the agency altogether and transfer its functions elsewhere. In the FY 2000-01 budget year, the Legislature adopted 207 out of 230 recommendations made by the Texas Sunset Advisory Commission, which resulted in \$17 million in taxpayer savings.⁶ Additionally, Florida’s Office of Program Policy Analysis and Government Accountability uses a similar process to propose an annual business plan to the Florida Legislature based on agency performance and outcome measures. Since the program’s inauguration in 1994, the Florida Legislature has adopted over \$443 million in savings.

The remarkable successes of the sunset commissions in Florida and Texas provide excellent models for our state government.⁷ In those states, the creation of the commissions yielded tremendous benefits to taxpayers, especially through the lower cost of government services. Remarkably, neither state collects an income tax, but both states operate with extraordinarily low per capita expenditures.⁸

South Carolina officials interested in running our government more effectively and more efficiently can learn some lessons from the experiences of Texas and Florida. A South Carolina Sunset

⁵ Under the Texas Sunset Advisory Commission statute, the charter of nearly every state agency expires every 12 years (excluding a possible 1-year grace period), unless renewed by the Legislature. The agency reviews are on a 12-year cycle, with one agency reviewed each year.

⁶ The recommendations adopted afforded savings ranging from \$3 million to less than \$200,000 per recommendation, involving agencies ranging from the Department of Economic Development to the State Board of Plumbing Examiners.

⁷ As previously stated, South Carolina operates with a ratio of 234 state employees per 10,000 residents, while the United States average is 174, an increase of 35 percent. Texas operates with 45 percent fewer state employees, with 157 per 10,000, while Florida’s ratio is barely half of South Carolina’s, at 120 state employees per 10,000.

⁸ According to *Governing Magazine’s 2006 Source Book*, Florida’s and Texas’s per capita expenditures are \$4,334 and \$4,030 per person, respectively. Comparatively, the United States average is \$5,406 per person, while South Carolina spends \$5,058 per person.

Commission could identify and eliminate waste, duplication, and inefficiency in government agencies, while improving the quality and lowering the costs of government services. Twice, the House of Representatives has passed a measure to create a sunset commission under the Legislative Audit Council, but both times the bill, unfortunately, stalled in the Senate. We strongly believe that a regular review of existing laws will provide substantial benefits to the taxpayers of South Carolina.

We recommend a South Carolina Sunset Commission chartered with the responsibility of assessing the need for each agency, looking for potential duplication of public services or programs, and considering innovative changes to improve each agency's operations and activities.

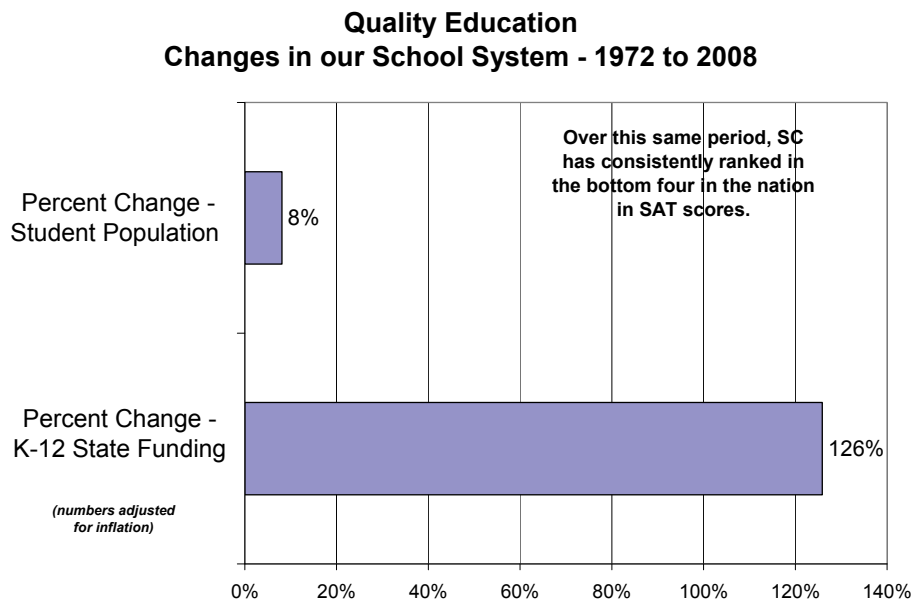
Innovate Education

Innovate Education

The direction in which education starts a man will determine his future life.

– PLATO, *The Republic*

For the last three decades, South Carolina has funneled more and more money into its public education system. While student population has risen by only eight percent over the last 36 years, state funding for K-12 education has increased 126 percent. Over the same period of time, South Carolina has ranked in the bottom four in the nation in SAT scores each year.



Albert Einstein said that insanity is “doing the same thing over and over again and expecting different results.” In South Carolina, we clearly fit this definition of insanity as it pertains to our education system. While many changes have been put in place recently – such as the creation of the Offices of Public School Choice at the state Department of Education – it remains to be seen whether this initiative and others will truly produce the deep change that we need in order to propel our students forward in global competition. We know that incremental increases are not enough, and we must focus our energy on developing a seamless system of education that maximizes the return on our educational investment and is more responsive to the needs of students and parents.

Challenges in Student Performance

Parents send their children to school with the expectation that at the end of each school year their children will be ready for the next grade. Unfortunately, state and national assessment scores show

that a majority of our state's students across grade levels and across subjects are not adequately prepared for the following year. This result is unacceptable in today's highly competitive world, where students must be prepared to meet the challenges of the modern economy.

Falling Short of the 2010 Goal

The Education Accountability Act (EAA) set an ambitious goal that requires South Carolina's student achievement to be ranked in the top half of states nationally in five target areas by 2010. To achieve this goal, we must become one of the five fastest improving systems in the country in our scores on the NAEP, SAT/ACT, on-time graduation rate, closing achievement gaps, and Advanced Placement programs. While student performance has improved in some areas, the current rate of progress is insufficient to reach the goal set by the General Assembly in 1998. Here's a look at where we are now on each of the five target areas outlined in the EAA:

1. National Assessment of Education Progress (NAEP)

Although students have raised scores, reading gains in fourth and eighth grades have been flat and remain several percentage points below the national average. The only EAA goal we are meeting is in our eighth-grade math scores, which place us 21st in the nation. Only 23 percent of our eighth-grade students score proficient on the writing portion of NAEP, well below the national average. Our fourth-grade math scores are ranked 33rd nationally, while our eighth-grade math scores place us 28th. Nationally we are ranked 42nd in fourth-grade reading and 41st in eighth-grade reading, and our ranking among Southeastern states in reading remains near the bottom.

NAEP Reading Results 2007: Ranking of Southeastern States				
State	4th Grade	Rank	8th Grade	Rank
Virginia	227	1	267	1
Kentucky	222	3	262	2
Florida	224	2	260	3
Georgia	219	4	259	4*
North Carolina	218	5	259	4*
Tennessee	216	7*	259	4*
Arkansas	217	6	258	7
South Carolina	214	9	257	8
Louisiana	207	11	253	9
Alabama	216	7*	252	10
Mississippi	208	10	250	11

2. SAT/ACT

For more than three decades, South Carolina has hovered at or near the bottom in regional and national rankings for our SAT and ACT scores – two key indicators of whether a student is adequately prepared for college. We rank at the bottom (11th) among Southeastern states and 48th among all states.

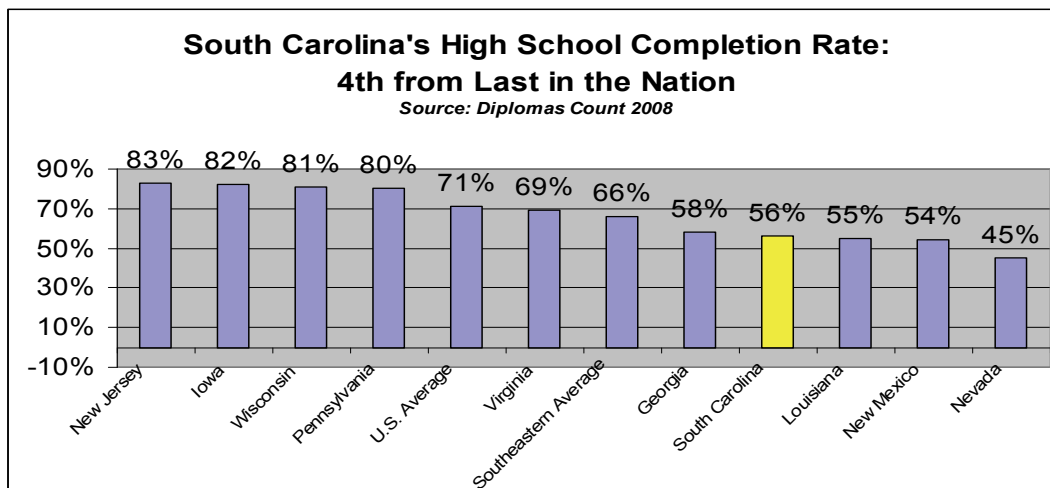
Some argue that South Carolina tests more students in the SAT than other states do, which may result in a lower average score. However, North Carolina and Virginia have a higher percentage of SAT test takers than South Carolina, yet these states still have higher SAT scores. These two states each had 63 percent of high school students participating in the 2008 SAT while South Carolina had 61 percent, yet both states had average scores higher than South Carolina (1,489 in North Carolina and 1,522 in Virginia, compared with South Carolina's score of 1,461. The SAT now includes a writing section, making the highest possible score a 2,400). During the past five years, South Carolina's composite reading and math score has remained virtually constant while the Southeastern average has increased by seven points. We fall 50 points below the national average of 1,511. Our state still falls short of the EAA goal of ranking in the top half of all states on this measure, as we are ranked 48th – falling ahead only of Hawaii, Maine, and the District of Columbia.

3. Advanced Placement (AP)

South Carolina ranks in the top half of all states in AP participation and in the percentage of exams that earn a passing score, meeting the EAA goal. However, there remains a large gap along racial lines in terms of participation – 75 percent of AP participants in 2007 were Caucasian, 12 percent were African American, and less than three percent were Hispanic. Racial data was not available for the remaining 10 percent.

4. Graduation Rate

No matter how it is calculated, high school completion rates in the Palmetto State are abysmal. You could flip a coin to determine whether or not a student in a South Carolina public high school will graduate on time – only about half do, while the other half drop out or take more than four years to finish. The completion rate – which is the percentage of ninth-graders who finish high school on time – has plummeted over the years. According to *Diplomas Count*, a study performed for The Bill and Melinda Gates Foundation, our state loses an average of 158 students per day.

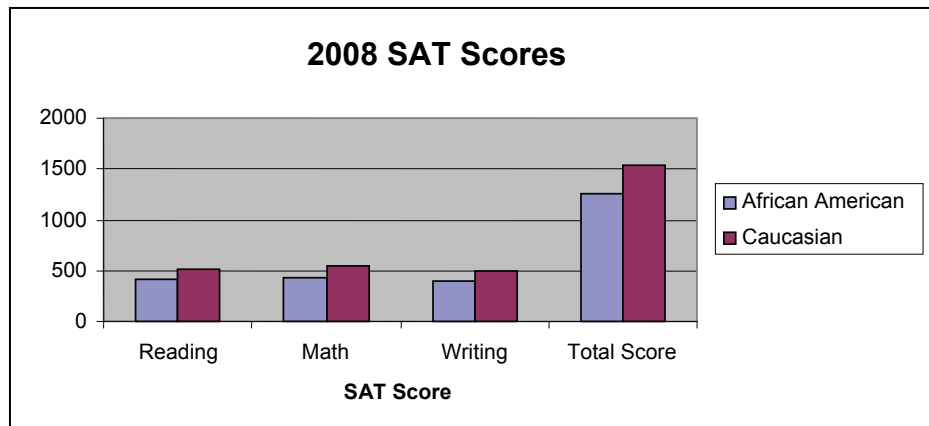
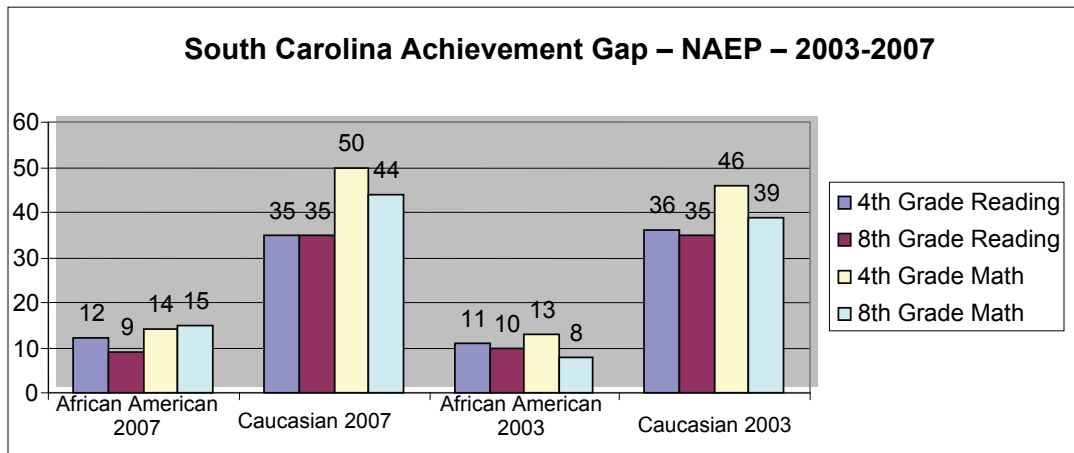


For the 55.6 percent who do make it through the system on time, many still do not go on to attain a college degree. According to the state's College Freshman Report – produced by the Department of Education – 65.5 percent of the 38,000 graduates in the Class of 2006 went on to

postsecondary education. Of those students who entered college, eight percent failed or did not receive credit in English Language Arts courses, while that figure jumped to nearly 14 percent for math and computer science courses.

5. Achievement Gap

It is completely unacceptable that only nine percent of African American eighth-graders are proficient in reading on the NAEP, while 35 percent of Caucasian eighth-graders are proficient in this same subject. Between 2003 and 2007, the achievement gap actually *widened* between African American and Caucasian students scoring proficient on NAEP in fourth-grade reading and eighth-grade math. In 2008, there was a 100-point difference between reading, math, and writing scores of African American and Caucasian students in South Carolina on the SAT. On a national scale, South Carolina's achievement gap between racial and socioeconomic groups on NAEP math and reading is in line with the national average in these subject areas, which underscores that this is a problem plaguing all states. According to the Alliance on Excellent Education, more than \$2.6 billion would be added to South Carolina's economy by 2020 if minority students graduated at the same rate as Caucasian students.



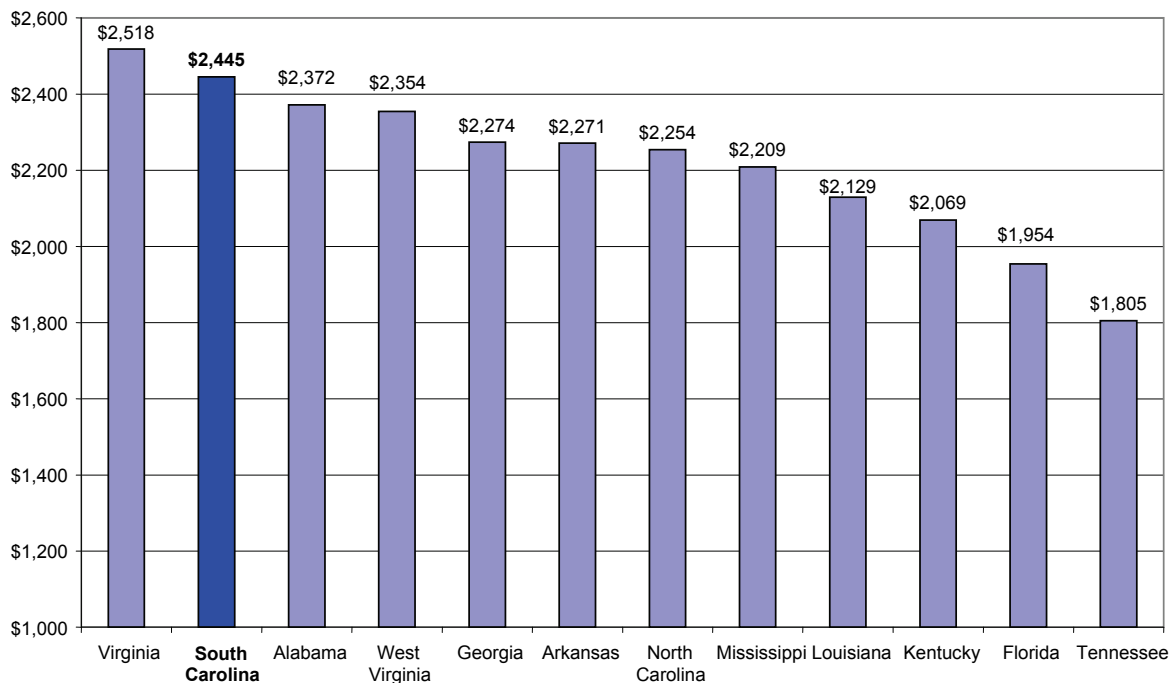
The Need for A Postsecondary Education

For many years, South Carolinians were able to find decent paying jobs in manufacturing or other industries requiring a high school diploma or less. A high school diploma alone, however, is no longer sufficient to find a job in our competitive world. Lacking a postsecondary education also leads to a drain of state resources for several reasons. First, students who take longer to graduate represent increased costs for the state for each year they remain in the system (the average cost to educate one student in our state is almost \$11,500). Second, students who drop out to pursue the General Educational Development diploma (GED) and do not continue on to attain an associate's degree are more likely to rely on the state's social services. Third, low-skilled workers have reduced earning potential, which lowers their quality of life. According to the Alliance for Excellent Education, \$7.4 billion in lifetime earnings is lost in South Carolina for the 28,000 students of the Class of 2008 who dropped out. Lastly, our state would save more than \$320 million in health care costs over the course of these dropouts' lives had they earned their diplomas. We believe much more needs to be done to improve the likelihood that students finish high school on time and are ready for life in the postsecondary world.

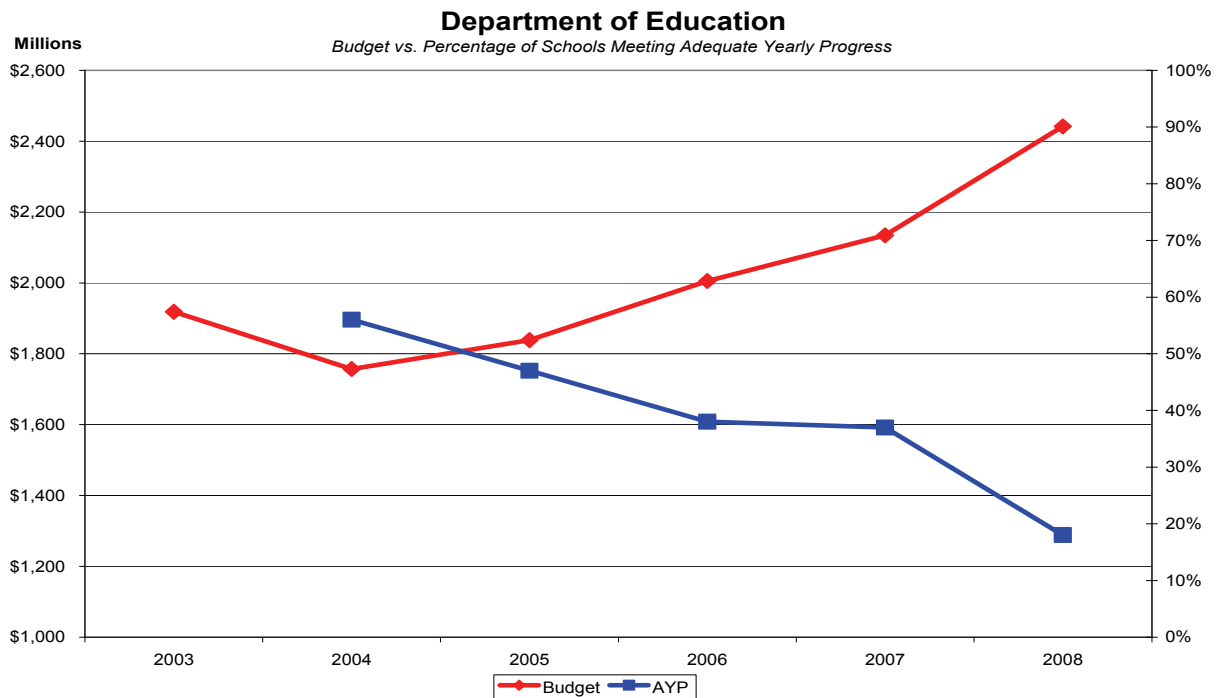
Spending More, Getting Less

Adjusted for inflation, education spending in our state has increased 126 percent since 1972. During that same period, student population has grown by only eight percent. Despite increased education spending at a rate faster than the national average over the years, our high school completion rate has seen no significant improvements and fewer of our public schools are meeting federal yearly progress goals.

Per-Capita Education Spending, Southeast



Source: Public Policy Institute Analysis of Census Bureau State and Local Government Finances: 2005-06



Throwing ever-increasing amounts of money into a flawed system will not change the quality of our system's educational product. We need reform in the academic system – as well as reform in the funding system – to improve our academic achievement. We believe that streamlining funding so that more money gets to the classrooms would go a long way toward achieving these goals.

Providing a 21st-Century Education

If we expect our students to compete in an ever-changing global society, then we must equip them with a 21st-century education. Providing such an education will ultimately require that we implement major reforms to improve the educational system. A key element in separating an average school system from a great one is the culture of low expectations that allows students, parents, teachers, and other stakeholders to accept mediocrity. We believe that taking a hard look at changes that will take South Carolina to the next level is long overdue, and we understand that mediocrity is not good enough. In order to move toward offering a comprehensive 21st-century education program, we propose implementing the following initiatives:

1. Provide school choice through scholarships and charter schools
2. Offer students incentives to succeed
3. Consolidate school districts and services
4. Reform the education funding formula and get more dollars to the classroom
5. Offer merit pay for teachers
6. Upgrade the public school transportation system

1. Offer choices to students in the lowest-performing schools

It is estimated that 74 percent of American students remain in government-assigned public schools, and the majority of South Carolina's students are bound to a particular public school because of the students' zip code. Unfortunately, too many of our students are zoned to public schools that are failing to meet their academic needs. According to School Report Cards – which are issued annually to districts and schools by the Education Oversight Committee – in 2007 only nine percent of schools in our state were rated “Excellent,” while 42 percent of schools in South Carolina were rated “Unsatisfactory” or “Below Average.” While the Report Card isn't the tell-all indicator of a school's success, it goes to show that there is wide disparity in the quality of education offered in South Carolina. Some of our state's students receive a high-quality education; however, the same is not true for students in the 296 failing schools deemed “Unsatisfactory.” Until we can ensure that every student has access to high-quality instruction, parents should have the freedom to enroll their children in a program that gets the results they need.

Recognizing that choices must be given to our neediest students, the Education Oversight Committee (EOC) has recommended school choice be provided to students in chronically underperforming schools. For schools that have received three years of technical assistance funding (due to an “Unsatisfactory” or “Below Average” Report Card) and show declines or no change in the Absolute Rating of their 2008 School Report Card, students in these schools will be allowed to transfer to a different public school with a higher Absolute Rating inside or outside the district of residence. The child's district of residence would provide to the receiving district an amount equal to the local revenues per pupil of the receiving district. A Department of Education report released to the EOC in October 2008 identified 151 schools with “persistent underperformance.” These schools had an Absolute rating of “Unsatisfactory” or “Below Average” for the years 2004 to 2007.

We fully support the EOC's recommendation and give credit to this group for putting the needs of students first. The EOC's recommendation also supports our notion of “backpacking” funds, which allows money to follow the child to the school he or she chooses to attend – whether it be inside or outside of their district of residence.

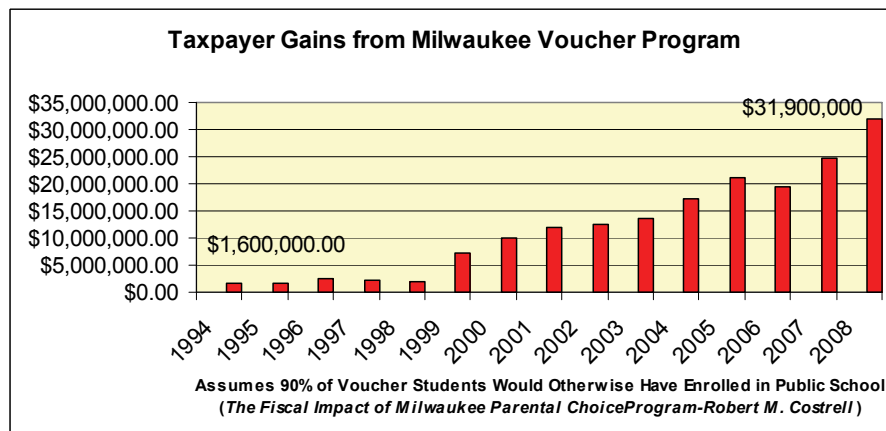
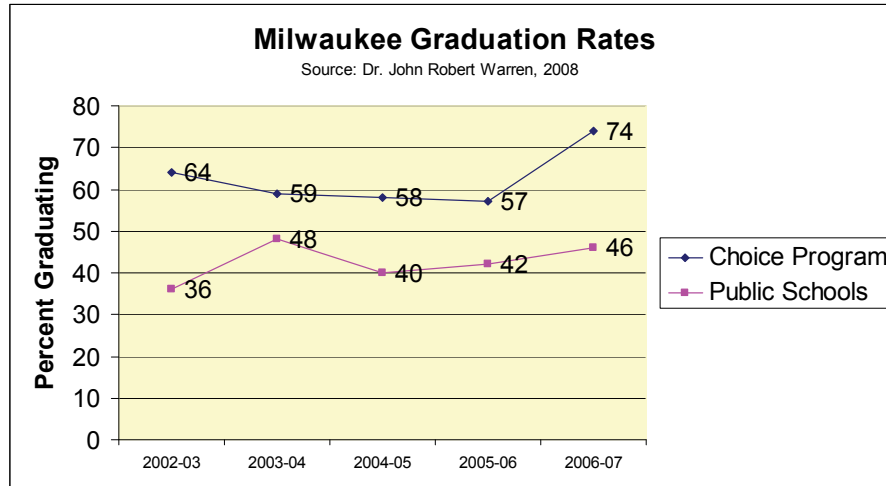
Additionally, we believe the freedom of choice can be provided through education scholarships targeted at the student populations that are least likely to receive high-quality education services. These scholarships should support students with special needs, low-income students, students enrolled in failing schools, or students who score “Below Basic” on any component of the state standardized exam. We believe that until parents have the flexibility to control where and how their children are educated, our ability to create a high-quality system will be limited.

Many other states are giving parents the flexibility they are demanding for their children's education. Eight states and the District of Columbia have policies that provide taxpayer-funded scholarships to help students attend private elementary or secondary schools of choice: Georgia, Arizona, Florida, Maine, Ohio, Vermont, Utah, and Wisconsin. Seven states offer incentives for contributions to scholarship programs or allow tax credits or deductions for education expenses, including private school tuition: Arizona, Florida, Illinois, Iowa, Minnesota, Pennsylvania, and Rhode Island. The chart below describes a few of the choice programs that have been implemented in other states:

Publicly-Funded Education Scholarships in the United States	
State	Description
Vermont	Town Tuitioning Parents are permitted to use up to \$7,500 toward transferring their child to a public or private school of their choice.
Maine	Town Tuitioning Parents are permitted to use up to \$6,000 toward transferring their child to a public or private school of their choice.
Florida	McKay Scholarship A student receives the full amount of funds for which he would have been eligible under the Florida Education Finance Program (FEFP). For the 2007-2008 school year, the average scholarship amount was \$7,295.
	Corporate Tax Credit Corporations receive tax credits for contributions to Scholarship Tuition Organizations. Credits are limited to 75 percent of a corporation's tax liability.
	Opportunity Scholarships Scholarships up to \$3,500 to attend private school or \$500 to change public schools. Scholarships are limited to students in schools rated "F" on the Florida accountability system.
Iowa	Deduction Families could deduct up to \$1,000 per child from their state income taxes for education expenses. Taxpayers using the standard deduction could take a tax credit of up to \$50 for education expenses for each child. Scholarships are limited to families earning less than \$45,000 per year.
	Tax Credit Tax credit of 25 percent of the first \$1,000 spent on their children's education.
Illinois	Tax Credit Parents receive a tax credit worth up to 25 percent of annual education related expenses. Tax credits range from \$250 to \$500 per family.
Wisconsin	Milwaukee Parental Choice Program Vouchers are worth the lesser of the full amount of private school tuition or \$6,000. Scholarships are limited to families earning less than 175 percent of the federal poverty level.
Georgia	Special Needs Scholarship Begun in the 2008-09 school year, this scholarship allows K-12 students with special needs to transfer to another public school, a private school, or to one of Georgia's three state schools for the deaf and blind. Scholarship amount depends on the type and severity of the disability.
	Tax Credit Individuals or business can contribute donations to the Georgia Student Scholarship Organizations, which, in turn, provides scholarships for students to attend private schools.

One example of the positive effect of education scholarships can be seen in Florida, where scholarships were introduced in 2001. After the first four years of implementation, several independent studies found that students who were offered scholarships outperformed other Florida public school students on state assessments.

In Milwaukee – the nation's largest and oldest scholarship program – graduation rates and achievement have improved and achievement gaps have narrowed compared with students who remained in the Milwaukee public school system. The Milwaukee program has also achieved substantial savings for taxpayers.



South Carolina provides scholarships to four-year-olds through the Child Development Education Pilot Program. We'd like to see scholarships extended to all students in our state to give them an opportunity for a quality education. As previously mentioned, we are not alone in our support of publicly-funded education scholarships for elementary and secondary students, as several states have already adopted similar school choice legislation.

Efforts to implement choice programs similar to those in Florida and Milwaukee have repeatedly been stymied by the South Carolina General Assembly. Each year since 2003 there has been an education scholarship introduced in the General Assembly. In 2004, "Put Parents in Charge" was introduced to offer a tax credit of \$3,600 to all parents in the state. In 2005, "Put Parents in Charge" was modified to target low-income students in failing schools by providing them with a scholarship at the beginning of the school year. These scholarships were available for private sector use as well as public use – as public school districts charge tuition for students who reside out-of-district. The Education Opportunity Scholarship was introduced in 2006 and reintroduced in 2007, creating a tax credit for middle-income families and a scholarship for low-income families of students in failing schools. The Education Opportunity Scholarship also offered a scholarship to

special needs students, regardless of income or school, and a tax credit to parents of homeschooled children.

Other attempts have been made to provide choice in our state, including the introduction of the public school choice program known as the Open Enrollment Bill in 2007. The fact that the Open Enrollment Bill was able to pass both the House and the Senate speaks to the recognition in the Legislature that more educational choices are needed. Unfortunately, the bill was rife with capacity limitations and student transfer acceptance prioritization that combined to empower school districts and *not* students. We believe that this legislation failed in giving parents and students choices within the education system. At the end of the day, this bill likely would have had – at best – an insignificant impact on expanding choices for students most in need of improved educational options. As a result, this administration vetoed this legislation, and it was sustained by the General Assembly.

Offering a combination of scholarships and tax credits could save millions of dollars in our state each year. South Carolina was among five states studied by the Cato Institute, which issued a report entitled “The Fiscal Impact of a Large-Scale Education Tax Credit Program.” The July 2008 report calculates that South Carolina could save **\$1.1 billion** over a 10-year period if the state operated on the Institute’s Public Education Tax Credit (PETC) model legislation.

Cato’s program is a combination of the tax-credit model in Illinois and the scholarship donation program in Pennsylvania and Florida. In Illinois, families can claim up to a \$500 state income tax credit if they choose to send their children to private school. In states such as Rhode Island, Arizona, Pennsylvania and Florida, children are benefiting from educational choice through the scholarship donation program that allows an individual or business to make a donation to a non-profit agency. In turn, that non-profit distributes scholarship tuition assistance to low income families. Cato’s PETC provides tax credits to parents who send their children to private schools, and to other taxpayers – including businesses – who donate money for scholarships. Under the PETC, the amount of tax credit parents can claim varies with the family’s income, so there is true incentive for low-income families.

The Cato report uses a “Fiscal Impact Calculator” to determine the amount of per-pupil spending for the next 10 years, the number of students migrating to private schools, and the annual financial impact to the state and to districts. In the first year, per-pupil spending in South Carolina is estimated by the calculator at \$12,900 with 142,000 kids enrolled in private schools and 591,873 students enrolled in public schools. During year one, the state would save \$96 million, while districts would potentially lose \$26 million. However, to counter the districts’ loss, the Legislature could appropriate state savings to the districts, resulting in total financial savings of \$67 million in year one alone. By year ten, the Fiscal Calculator assumes that more than half of the state’s students would now be enrolled in private schools, thus resulting in a financial saving of \$1.1 billion.

Cato Institute's Public Education Tax Credit Program
Fiscal Impact on South Carolina

Year	Public School Funding Per Pupil	Net State and District Impact
1	\$12,992	\$67,587,305
2	\$13,152	\$66,550,428
3	\$13,366	\$74,223,260
4	\$13,651	\$91,063,504
5	\$14,024	\$116,541,962
10	--	Total Impact: \$1,080,516,318

The issue of school choice has long been advocated by conservatives who want to see true reform. Now, more and more Democrats are realizing the potential positive impact that school choice can bring. In 2008, Reverend Al Sharpton, who had always opposed school choice, cited continuously seeing achievement scores of African Americans and Hispanics lag behind achievement scores of white students as the reason he has joined the choice movement. Last June, Sharpton joined New York City Schools Chancellor Joel Klein in co-chairing the newly-formed Education Equality Project, a non-partisan group advocating for more charter schools and greater accountability. Supporting charter schools is certainly a step in the right direction, and we hope that other influential leaders and lawmakers – in Congress and in our state General Assembly – will also begin to advocate for true school choice that includes private school choice as well.

South Carolina Public Charter School District

In 1996, South Carolina's General Assembly recognized the need to offer parents more options in directing the quality of the education their child received. To fill this need, the General Assembly passed charter school legislation that gave parents, educators, business leaders, and community members the flexibility to collaborate to create schools that offer innovative opportunities for students.

As a result, South Carolina has been able to create a variety of charter schools. However, there are some places in the state where such creative educational opportunities are blocked by local school boards of trustees or district officials. We advocated for the creation of an alternative authorizer, the South Carolina Public Charter School District (SCPCSD), to offer prospective charter schools another sponsor. In the spring of 2006, the General Assembly enacted legislation that allowed for the creation of the statewide district. The SCPCSD has a fully functioning Board of Trustees as well as district staff, and in the fall of 2007 it began receiving applications for prospective start-up charters. For the 2008-09 school year, there were two "brick-and-mortar" charter schools under the SCPCSD jurisdiction, and three virtual schools, serving nearly 2,600 students. Two more schools have been approved to open in the 2009-10 school year.

In order to continue the work of the SCPCSD specifically, and the charter school movement generally, we request that the school district receive the funding necessary to offer applicants and approved charters the technical assistance and administrative support they need to become

operational. For FY 2008-09, state funding for students in the SCPCSD is estimated at \$3,400 per student while that figure jumps to \$4,867 for traditional public school students. Including federal funds and local funds, the statewide charter school district receives about \$5,000 per student while traditional public school districts average \$11,480 per student. We must do more to equalize funding for students enrolled in the charter school district.

2. Offer Students Incentives to Succeed

It has been culturally accepted for decades in many South Carolina public high schools for seniors to expect their last year of high school to be full of social interaction with few academic challenges. This holds particularly true of students who earn most of their course credits prior to their senior year, allowing them to complete their required 24 credits long before they graduate. Some of these advanced students pursue dual enrollment courses for college credit while still in high school, or they take a light course load so they can have free time to share with friends during their last year. Too many of our students are pursuing the latter option.

The “senior year off” mentality presents the state with two challenges. First, it creates an unnecessarily high cost to educate the student. Though the students aren’t participating in a full course load, the full per-pupil expenditure of \$11,867 is still being taken out of the wallets of taxpayers. Second, the “senior year off” mentality potentially sets the students up for failure upon entering their first year of postsecondary education. By the time they graduate from high school, it’s possible that many students have been an entire year without math or science courses, which makes it difficult to draw upon these essential skills during their postsecondary studies.

Several states have found ways to address the lack of rigor in the senior year. Texas, Arizona, and Utah have all implemented early graduation scholarship programs. In Texas, the Early High School Graduation Scholarship Program rewards students who finish high school prior to the spring semester of their senior year. Under the program, students receive a scholarship based on the amount of time spent in high school. The sooner they finish high school, the greater the scholarship they receive.

Texas Education Agency Early High School Graduation Scholarship	
Scholarship Amount	Requirements
\$3,000	<ul style="list-style-type: none"> ◆ Successfully complete high school curriculum in 36 consecutive months (spring of junior year) ◆ Graduate with at least 15 hours of college credit
\$2,000	<ul style="list-style-type: none"> ◆ Successfully complete high school curriculum in 36 consecutive months (spring of junior year)
\$1,500	<ul style="list-style-type: none"> ◆ Successfully complete high school curriculum in 36 – 41 consecutive months (fall of senior year) ◆ Graduate with at least 30 hours of college credit
\$1,000	<ul style="list-style-type: none"> ◆ Successfully complete the high school curriculum in 41 – 45 months (spring of senior year) ◆ Graduate with at least 30 hours of college credit
\$500	<ul style="list-style-type: none"> ◆ Successfully complete the high school curriculum in 36 – 41 consecutive months (fall of senior year)

During the 2007-08 school year, more than 5,700 students in Texas earned the Early High School Graduation Scholarship, with award amounts totaling \$5.5 million.

This administration proposes implementing the **Palmetto Early Graduation Reward Program** for students who complete the required 24 credit hours before the spring semester of their senior year. Based on the Texas Early High School Scholarship Program, our program offers a reward to students who master the required course of study in a shorter period of time than the traditional four-year program of study. At the same time, it reduces the cost of educating that child. By extending student scholarships worth up to **\$2,000** (for finishing in six semesters) **or \$1,000** (for finishing in seven semesters), we provide students with true incentives to focus on their individual graduation plans early in their secondary education, with the hopes that hard work can lead to a financial reward when they finish high school.

Palmetto Early Graduation Scholarship	
Scholarship Amount	Requirements
\$2,000	<i>Complete South Carolina High School curriculum in six semesters</i>
\$1,000	<i>Complete South Carolina High School curriculum in seven semesters</i>

We recommend the scholarships be paid with revenues that would have followed a student, who graduated earlier, during his or her senior year. During FY 2009-10, it is estimated total funding per student will be \$11,867— providing more than enough to fund fully this program starting with the senior class of 2010. In fact, if just 400 South Carolina seniors from the Class of 2010 were to complete their coursework in six semesters, the state could realize a savings from per-pupil expenditures of \$3 million. We thank Rep. Nathan Ballentine for his effort in including the early graduation scholarship in last year's General Appropriations Act. Along those same lines, we hope both bodies of the General Assembly will consider legislation for this type of incentive.

3. Consolidate School Districts

District consolidation is a concept that has been underway in South Carolina for some time, and this administration still believes that more consolidation is needed to create an efficient and equitable education system. Since 1950, the number of school districts in South Carolina has declined from 1,220 to 85 school districts shared by 46 counties in 2006 – not including the South Carolina Public Charter School District or the Palmetto Unified District, which serves the state's inmates. Despite the reduction in the number of school districts, there remains wide variation in district size – ranging from more than 70,000 students in Greenville County Schools down to fewer than 860 students in Dillon School District One.

Similar to the inefficiencies of having too many independent state agencies, we find that so many separate school districts require duplicative and unnecessary administrative costs. For example, while Greenville County only has one school district, neighboring Anderson County has five separate school districts and Spartanburg County has a total of seven. More than half of our school districts only have one high school. An extensive study conducted by a team of consultants for the

Education Oversight Committee in 2003 found that the cost per student demonstrates the inefficiency of smaller districts. The report said that districts rated “Unsatisfactory” are spending almost \$1,200 more per student than the districts rated “Excellent.” The underperforming districts spend too much on fixed costs for leadership and operational costs and not enough on teachers’ salaries or hiring better-qualified teachers. The study concluded that if districts would merely consolidate to reach a minimum population of 2,500 students, “we could save nearly **\$26 million** in administrative costs that could be spent directly for students in their classrooms.” Likewise, the Office of State Budget estimated fiscal savings from school consolidation to be \$21 million.

Recent examples of school or district consolidation in South Carolina have initially proven to bring more money to the classrooms. In 2008, our administration supported the consolidation of Sumter School Districts 2 and 17, which will phase-in their merger over the next three years. In Union County, the school board voted in the spring of 2007 to combine the county’s three high schools under one roof. Students from the small schools of Jonesville and Lockhart – which served fewer than 250 high school students each – were sent to the campus of Union High School, creating Union County High School. While this merger initially caused emotions to run high as the smaller towns felt they were losing their identity, the first school year of consolidation went smoothly and district officials estimate \$1 million in savings by not operating the facilities of the smaller high schools.

Unnecessary expenditures on district and program-level management hinder the impact of the educational investment made by taxpayers. While we are optimistic that financial and economic realities will cause more district consolidations, the fact remains that until there is initiative to reduce the number of smaller districts in our state, districts must become more effective at reducing administrative costs. Other states are already realizing the effect that shared services have in driving more of the educational dollar into the classroom.

- Dallas and Houston Independent school districts pooled resources to increase buying power in purchasing health insurance and to reduce duplicative administrative overhead in procuring employee health benefits.
- Rural districts in Texas have reduced accounting costs by 50 percent per year by sharing the service provision of accounting and payroll services.
- Through cooperative purchasing, the Shared Services Program in Middlesex County, New Jersey, contributed to a five percent savings on electricity for public buildings during the first year of the program by reducing costs on water/wastewater programs and by purchasing natural gas, electricity, equipment, services and supplies.
- Lawrence-area Massachusetts school districts have banded together to provide special education services, saving taxpayers approximately \$13 million over the next two decades.

Sharing services need not be limited to school districts. District offices should consider sharing services with other local, municipal, county, and regional agencies as well as private providers. The Lincoln Unified School District in Stockton, California, created a mutually beneficial contract with a private fitness center operator to build a facility on site at a newly planned school. Clients use the facility in the morning and evening – outside of school hours – granting the school access to the facility during the school day.

Since the early 1980's, the Northville Parks and Recreation Department in Michigan and the local public schools have engaged in a joint services contract where the public schools allow the department to use their facilities to provide youth and senior citizen recreational services. In South Carolina, potential service partners include other districts, other schools, institutions of higher education, municipalities, nonprofits, and privately owned businesses. This concept was supported in the South Carolina Education Reform Council Report to the Governor in which the Council recommended providing "a structure and regulatory authorization for districts and schools to readily share resources developed for school districts with other community organizations or businesses for their needs, when those resources are not being used by the school."

In 2005, the General Assembly created the School District Study Committee to evaluate the size of school districts in our state and make recommendations on district size that will allow more direct spending on teacher salary and instructional support. The study committee issued its report in January 2006 and concluded that the school districts could realize a cost savings of more than \$21.1 million by consolidating management functions that occur at the school, district, and regional levels.

Achieving the savings discussed by the study committee does not require drastic changes in services, nor does it require increased oversight on the part of the State Department of Education or the General Assembly. By simply requiring that districts limit per-pupil expenditures on the District Management Level and the Program Management Level to the lowest average expenditure for each county, the General Assembly can force districts to consolidate governance and services, or offset per-pupil expenditures on District and Program Management Level activities with local operating funding.

Expenditures on District and Program Management 2005		
School District	Enrollment	Per-pupil Expenditure
Dillon	913	\$374
Barnwell 19	946	\$685
Barnwell 29	981	\$302
Marion 7	984	\$457
McCormick	1,028	\$836
Bamberg 2	1,078	\$1,008
Richland 1	25,909	\$161
Berkeley	26,998	\$161
Horry	31,036	\$104
Charleston	43,161	\$287
Greenville	63,313	\$112
State Average		\$277

In light of our state's budget shortfall and in order to maximize the dollars that get to the classrooms, we support funding only one office of district-level administrators per county. For example, Charleston County serves 43,000 students and has one superintendent, as well as chief administrators for instruction, finance, and human resources, to name a few. In Spartanburg County, which also serves 43,000 students, there are seven districts that all have a superintendent and other district-level administrators. Funding salaries for seven districts is excessive in such tight financial times when we are losing funding to pay teachers to remain in our classrooms. We support funding administrative salaries for only one district office per county, and we encourage districts to pay for additional administrators if they choose to continue operating multiple school districts per county.

To encourage more consolidations for the purpose of resource savings, this administration recommends offering incentives to districts that consolidate voluntarily. Education Superintendent Jim Rex appointed a Task Force on Funding for World Class Learning in 2007. In the Task Force

proposal, incentives were offered to districts that consolidate, and we agree with the incentives with a few minor modifications:

1. Allow consolidated districts to receive general state aid at the level of the district receiving the most aid prior to consolidating for two years after merger.
2. Allow consolidated districts to receive state grants to compensate for any difference in teacher salaries, so that salaries for all teachers are increased to the same level. This should be allowed for a three-year period following the merger.
3. Allow consolidated districts to receive a one-time grant to cover a portion of the negative fund balance that any district brings into the consolidation.
4. Allow consolidated districts to receive a “hold harmless” on the district report card rating for a period of three years following consolidation, with individual schools receiving report card ratings as usual.

4. Our “Funding The Child” Proposal

Our current funding system has dozens of spending categories, making it difficult for school districts to be innovative in their student-based programs. The present system also places limits on what districts can purchase, while imposing cumbersome accounting management for administrators. Ultimately, we need a system that funds the child – not one that solely funds programs.

Last year, the state’s Board of Economic Advisors estimated that we spend \$11,480 per pupil – which is \$2,220 more than the national average and higher than neighboring states. Yet, we have still seen no dramatic gains on national assessments. Funding estimates are expected to increase to \$11,867 by FY 2009-10. These examples show that we are spending enough on K-12 education – *how* these resources are spent is what this administration aims to address.

We support a system of funding that adheres to the following principles:

- Allow funds to follow children to whichever school they attend;
- Tie funding levels to the individual needs of the child;
- Allow school funding to arrive at the school as real dollars and not as staff positions or teaching ratios; and
- Simplify the funding system, make it more transparent, and make it more accountable to taxpayers.

This administration supports a simplified funding stream for schools based on an updated Education Finance Act formula that includes factors for family poverty (using the Department of Social Service’s qualifications for Food Stamps to define poverty), student disability, and gifted and talented students. The current system has weightings for students with disabilities, and the weighting unit depends on each student’s particular special need. We think this system should remain intact. Schools would be given the flexibility to select and purchase the services they believe best meet their students’ needs.

The funding system we propose would not only allow greater spending flexibility for districts but also greater transparency for the public. Our funding plan would allow parents and taxpayers to find out how funds are spent at the school level via a user-friendly online database.

The “Funding-the-Child” approach that we propose has gained broad support across the country. School districts in Cincinnati, Milwaukee, and Houston are using various aspects of this model. In Oakland, California, the shift to weighted student funding has led to a redistribution of the best qualified teachers to the schools that need the most academic improvement. The bottom line is that moving to a more simplified funding system can address the inequities produced by current budgetary practices, reduce the impact of perverse incentives established by programmatic funding, and force schools and districts to focus on responding to students’ needs rather than sustaining existing bureaucracies.

Our proposal for education funding reform will also fulfill a primary objective of our education budget proposal: driving more dollars directly to the classroom. In doing so, we propose measures that would give school districts greater flexibility in spending decisions. Attempts at offering districts financial flexibility have been proposed. For the 2002-03 school year, the General Assembly adopted the flexibility proviso, which offered school districts the flexibility to transfer up to 100 percent of the funds between programs to any instructional program, provided the funds are used for direct classroom instruction. The idea behind adding such a proviso is that it would offer district leaders the flexibility to make less regulated spending decisions. When given greater flexibility, districts reallocate resources to funding categories that are less restrictive.

District funding flexibility is certainly a move in the right direction, but we believe this particular proviso is still too restrictive. First, the proviso permits district-level flexibility, which is simply not the same as school-level or site-based flexibility. Second, while well-intended, the flexibility proviso simply does not go far enough to truly demonstrate how school leaders would reallocate resources given student performance goals and real flexible spending. Of the \$3.7 billion in education appropriations for FY 2008, only \$345.6 million was subject to the flexibility proviso, representing only 9.34 percent of district revenue. In FY 2008, 70 school districts and one special school district utilized the flexibility proviso. These districts transferred a total of \$31.4 million, which is nine percent of the total funding available for transferring. According to the Department of Education’s 2008-09 Funding Manual, several programs are excluded from this flexibility.

Programs Excluded from the Flexibility Proviso
♦ EEDA 8 th Grade Career Awareness
♦ EEDA Career Specialists
♦ Refurbishment of K-8 Science Kits
♦ Child Development Education Pilot Program
♦ School Employer Contributions
♦ Junior Scholars Program
♦ National Board Certification Salary Supplement
♦ Teacher of the Year Awards
♦ Teacher Salary Increase
♦ Teacher Supplies
♦ Principal Salary/Fringe Increase
♦ Bus Driver Salary Supplement
♦ EAA Technical Assistance

We propose that the multiple funding streams be consolidated, giving the districts spending flexibility. Until that happens, we support continuing the Funding Flexibility Proviso with three modifications:

- Public schools – rather than districts – should be given the flexibility to reallocate resources;
- Rather than focusing on increasing instructional spending, hold schools accountable for results on a nationally-recognized norm-referenced test;
- Reduce the list of programs excluded from this flexibility so that Education Accountability Act funding may be reallocated based on school-level managerial decisions.

In addition to extending the scope of the Funding Flexibility Proviso, we propose that the General Assembly enact a permanent statute to provide school districts more flexibility in how they spend the allocated funds. This proposal, Streamlined Management and Accounting Resources for Teaching (SMART) Funding, would put more education spending decisions in the hands of the communities, rather than dictating policy from Columbia. First introduced by Representative Roland Smith in 2004, SMART Funding was later co-sponsored by Former Speaker David Wilkins and former House Ways and Means Chairman Bobby Harrell. It passed overwhelmingly in the House in 2003 and came very close to passing in the Senate. The SMART Funding bill faded away in the Senate and was not enacted by the General Assembly in the 2006 legislative session. Under the leadership of House Speaker Bobby Harrell and Representative Jeff Duncan, Joint Resolution 3531 was introduced in 2007 in order to create a study committee to review how best to allow the state's portion of education funding to be allocated to schools through a weighted student formula. We continue to support SMART Funding legislation and will work closely with the General Assembly in the upcoming legislative session to complete this work.

5. Reward Teachers for Positive Performance

School districts in our state seek to find the best and brightest teaching workforce to instruct and enlighten young minds, and offering competitive pay is one way to reward teachers for their dedicated service. This administration also realizes the importance of teacher pay in influencing the ability of school leadership to recruit and retain high-quality teachers, which is why South Carolina has been aggressive in raising the average teacher salary.

In past executive budgets, we have supported raising teacher pay in South Carolina to at least \$300 above the Southeastern average during years when sufficient funding is available. Unfortunately, this budget year produced deep and painful budget cuts, which affected K-12 education. We believe teachers are the most vital factor in educating children. However, even by concurring with the proposal of State Education Superintendent Jim Rex and the EOC to maintain the existing funding level for teacher salaries, we believe the current system of pay is unconnected to the quality of the service a teacher offers.

Like employees in many other industries, teachers respond to the incentives placed before them. Merit pay, commonly referred to as “pay for performance” or “diversified compensation systems,” is a way to pay teachers that rewards success. Several urban areas have implemented pay-for-performance plans, but states are now moving forward with merit pay plans of their own. In 2007, Arkansas enacted the Rewarding Excellence in Achievement Program (REAP) Act. The two-year pilot allows up to 12 public school districts, schools, or charter schools to receive a grant for alternative teacher compensation.

In Denver, the ProComp program for public schools was introduced in 1999, and more than 1,200 teachers are currently enrolled in the program. The ProComp system is a results-based pay system that uses multiple criteria to assess a teacher’s performance. Teachers do not receive a salary bonus until they demonstrate improvement on the criteria specified in the four specific areas.

Components of the Denver ProComp Pay System		
	Criteria	Bonus Amount (Percent of Index, based on \$35,568 salary in 2007)
Knowledge and Skills	Professional Development Units	\$711 (2 percent)
	Graduate Degree/National Certificate	\$3,201 (9 percent)
	Tuition Reimbursement	\$1,000 (3 percent)
Professional Evaluation	Probationary	\$356 (1 percent)
	Non-probationary	\$1,067 (3 percent)
Student Growth	Meeting Annual Objectives	\$356 (1 percent)
	Exceeding Student Performance Expectations	\$1,067 (3 percent)
	Distinguished Schools	\$711 (2 percent)
Market Incentives	Hard to Staff Position	\$1,067 (3 percent)
	Hard to Staff Schools	\$1,067 (3 percent)

The Denver ProComp system reflects current knowledge about merit-pay systems. First, it is imperative that teachers feel they have a choice to participate in the program. ProComp allows teachers to opt-into the program over a seven-year phase-in period or to continue with the traditional teacher salary schedule that bases salary increases on years of experience accompanied

with inflationary adjustments. All new teachers are automatically enrolled in the program. This approach balances the fact that teachers new to the profession – either as first-time entrants into the workforce or as career changers – are generally more receptive to merit pay as a way to increase their pay based on demonstrated proficiencies.

Second, the ProComp system takes into account the fact that teachers are able to demonstrate proficiency in several areas – all of which can ultimately improve the quality of student instruction. An ambitious teacher, for instance, might pursue salary bonuses in all four areas, increasing their salary nearly \$10,000 in a school year.

In 2006, South Carolina was awarded more than \$40 million by the U.S. Department of Education to create the South Carolina Teacher Incentive Fund (SCTIF). The SCTIF supports South Carolina's Teacher Advancement Program (TAP), a school-wide pay for performance-based system that is based on a national TAP model but has been modified to fit our state's needs. TAP is currently in 45 schools in 14 districts. Teachers in participating schools are eligible to receive salary bonuses ranging from \$2,000 to \$10,000 based on classroom observations, improved student achievement in their respective classrooms, or school-wide performance improvements.

The TAP program builds on four elements that include merit-based compensation, multiple career paths for teachers, ongoing professional growth, and instructionally-focused accountability. Under the TAP model, teachers work along self-selected career paths that differentiate master teachers – who are more experienced – from novice teachers. Master teachers instruct fewer courses and spend more time offering novice teachers targeted professional input on ways to raise the student achievement levels. Career paths are not determined by years in the profession, but by demonstrating the ability to raise student achievement. Thus, young professionals have a real incentive to enter and stay in teaching. South Carolina's TAP model is so strong that when creating the Minnesota Compensation plan – QComp for Quality Compensation – Governor Tim Pawlenty based the statewide initiative on the services being offered under the TAP model.

In 2008, a survey of 10 schools that have TAP averaged a 33 percent improvement in teacher turnover. One highlight is at Bell Street Middle School in Laurens District 56. Before Bell Street implemented TAP in 2002, the average teacher turnover rate hovered around 40 percent. The turnover rate dropped to about 30 percent during the first year of TAP and has remained below 10 percent during the past three years.

State-level investment in National Board Certification Salary bonuses is an area where we believe the state's investment in teacher pay could be better used toward fulfilling our goal of raising student achievement. We are committed to honoring the work of teachers who have already completed the certification program. However, expanding the program beyond its current participation level limits the state's ability to invest in raising teacher pay in a manner that has a real impact on student achievement. We support the Education Oversight Committee's recommendation of discontinuing the state supplement for National Board Certification after all current obligations are met.

Rather than expanding this expensive bonus system, we propose limiting National Board Certification salary bonuses to teachers who complete the application process prior to June 30, 2009. Going forward, funds currently devoted to National Board Certification salary bonuses should be set aside for a performance-based bonus program. Specifically, we propose targeting these funds

toward block grants that can be used by school districts to establish merit-pay programs similar to the TAP model.

6. Transportation

The costs associated with transporting students to and from schools continue to be some of the largest direct expenditures made by the Department of Education. South Carolina is the only state with a centralized school bus service and purchasing arrangement. The effectiveness of our purchasing practices are of particular concern, as the average age of South Carolina's school bus fleet is well above what would be acceptable in the private sector.

In 2006, the state Department of Education's Director of Transportation received a memo from the TransPar Group, a professional organization that helps schools resolve transportation issues, highlighting the efficiencies the state Department of Education would gain by leasing a portion of its buses from a private provider rather than making outright purchases. In 2006, 89 percent of the state's school bus fleet was older than 10 years or had been driven more than 100,000 miles. By leasing buses, the Department of Education would reduce the time it will take to get to the industry standard of maintaining an average vehicle fleet age of seven years by 25 percent, while also reducing overall maintenance costs. The strategy recommended by TransPar included using \$9 million out of the \$36 million in annual bus purchase appropriations to lease 1,000 new buses rather than using the entire amount to purchase only 475 new buses – a cost savings of \$27 million. The average life of a school bus is 15 years, so we could send students to school in newer buses at a lower cost with a shorter replacement cycle by leasing.

We recommend that the state Department of Education strongly consider the possible benefits of leasing a portion of the new school buses. This would save time and money for our state and would provide us a more stable and up-to-date fleet of buses to take our children safely to school.

We also recommend that the use of buses that run on natural gas and hybrid electric diesel technology be considered. The hybrid buses average 13 miles per gallon versus seven miles per gallon for traditional diesel buses. At a time when gas prices are so volatile, we should find more efficient and cost-effective means of transportation.

Conclusion

This administration's education proposal is quite simple: provide multiple options for all students to get the best possible education so that all of our students can graduate from high school ready for college or the workplace. We believe this can be accomplished through a combination of reforms, including getting more dollars to the classroom and providing choices so each child can thrive in the educational environment that is best for them. While we have made progress over the last few years on some measurements of education, we still lag in many critical areas – primarily in high school graduation rates. With the growth of educational options in other states and nations, we simply cannot afford to rely on incremental change to improve our competitiveness. We should aim to get to the top of the list, and we believe our initiatives offer the transformational opportunity to succeed.

Emphasize Economic
Development

Emphasize Economic Development

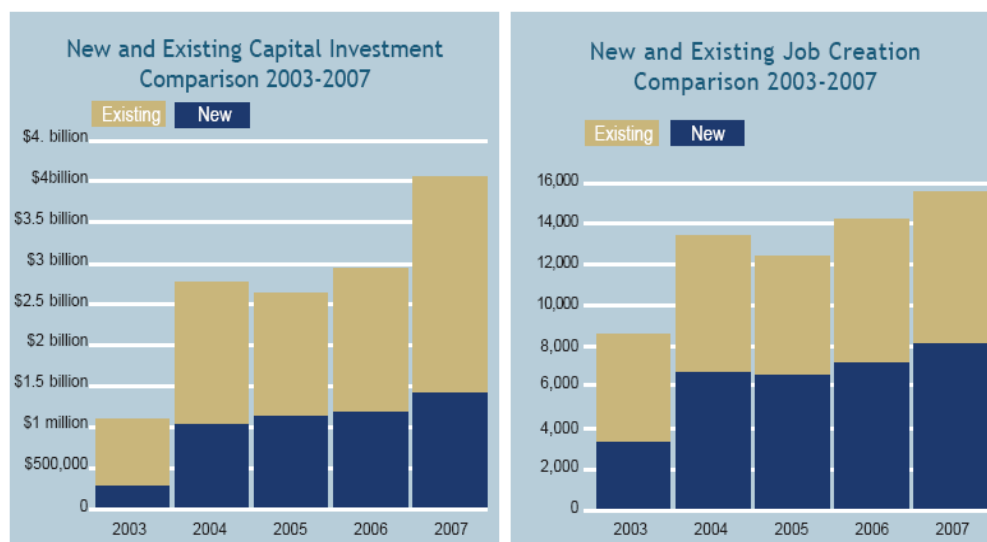
The world is changing very fast. Big will not beat small anymore. It will be the fast beating the slow.

– Rupert Murdoch

South Carolina continues to face persistent competition from all over the world. As the above quote implies, those who respond to this change quickly will be the most adept at competing in the ever-evolving global marketplace. In spite of this competition, and even with the current fiscal situation, our state has met this challenge and continues to have success in attracting new business while allowing existing businesses to grow and compete in an increasingly global marketplace.

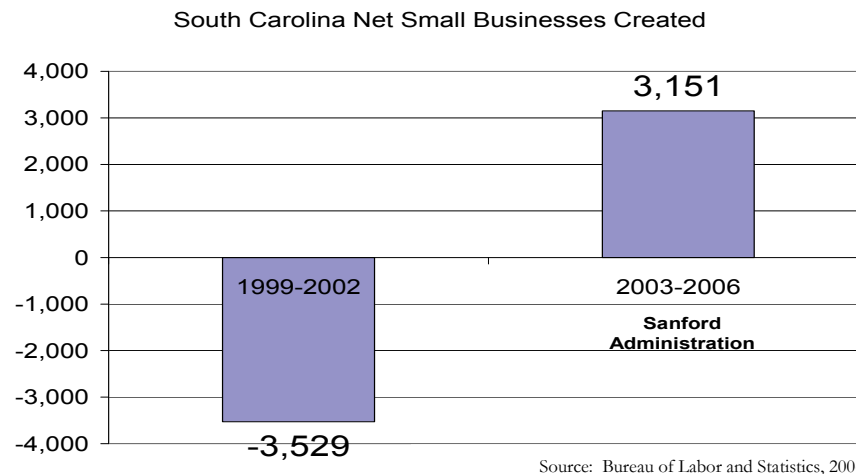
South Carolina consistently is recognized for its business climate by one of the nation's leaders in providing site selection and corporate relocation services. In 2008, the Pollina Corporation again named South Carolina among "America's Top Ten Pro-Business States." In this study, South Carolina was honored for its progressive, pro-business policies that result in job growth. The state has been ranked either #1 or #2 in the Pollina study each of the past four years. The continued push by this administration and the Department of Commerce is at the root of this success, as the state continues to yet another year of record levels of capital investment, job creation, and opportunities for South Carolinians.

From the beginning of our administration, the Department of Commerce has been recruiting jobs and capital investment to South Carolina at a robust pace. In 2008, the Department of Commerce had another record year for investment and job creation – recruiting more than \$4 billion in capital investment and more than 16,000 jobs.



Small Business Growth

South Carolina continues to place an emphasis on growing small businesses – the backbone of our state’s economy. Small businesses employ more than half of our state’s workers, and 97 percent of all businesses in the state are classified as small businesses. Because our administration believes that small businesses are the driving force behind South Carolina’s economy, we pushed for a reduction of the business tax rate from seven percent to five percent. This reduction increased opportunities for small businesses in the state to grow, as well as created new investment and jobs. We believe that this pro-business reform will continue to foster small business growth in South Carolina. The state now has over 3,000 more small businesses than it had when our administration began. During the four years prior to our administration, the state lost over 3,500 small businesses.



During the State of the State address last January, we called on the General Assembly to pass legislation that would give small businesses greater opportunity to provide health insurance to their employees. We applaud the General Assembly for passing this legislation, which allows small employers to form non-profit cooperatives to provide employee health insurance. By grouping together, small employers are able to gain the buying power of large companies.

Attention to the importance of small business in enhancing our overall economic climate continues to pay dividends, and we look forward to advocating for changes that will add to this success.

Improve Soil Conditions for More Job Creation

The global economy continues to diversify, and emerging markets across the globe are becoming more adept at competing with the United States. South Carolina must focus on recruiting the best of the best – high quality companies committed to growing their business and creating high paying jobs for South Carolinians.

South Carolina continues to sell its strengths and existing framework for business while working to minimize or eliminate our weaknesses. An emphasis on the state’s access to markets, transportation and power infrastructure, available sites for development, nationally recognized worker training programs, and a strong technical college system will continue to be major points of interest for

companies seeking to relocate to or expand in South Carolina. Fortunately, South Carolina's weaknesses are identifiable and can be solved with the right approach. This administration firmly holds to the idea of making policy choices based on what we can do to improve our weaknesses – from strengthening our education system, to providing a more business-friendly environment for companies large and small seeking to locate or expand here – while also maintaining our competitive edge in the global marketplace.

Cultivating our economic soil conditions for business will improve South Carolina's ability to compete. A recent *Wall Street Journal* article commented that the Competitiveness Index created by the American Legislative Exchange Council (ALEC) identifies “16 policy variables that have a proven impact on the migrations of capital – both investment capital and human capital – in to and out of states.” Its analysis shows that “generally speaking, states that spend less, especially on income transfer programs, and states that tax less, particularly on productive activities such as working or investing, experience higher growth rates than states that tax and spend more. The simple answer is that governance, taxes and regulatory policy matter. The playing field among the states was not flat. Business conditions were better in the successful states than in the lagging ones. Capital and labor gravitated to where the burdens were smaller and the opportunities greater.” As we have advocated since taking office, reforming the tax structure in South Carolina will significantly increase the numbers of investors coming to South Carolina.

The broad-based changes we have advocated are devoted to transforming South Carolina into an economy poised for the 21st century and beyond. These changes include reducing taxes to stimulate the economy, reforming the judicial system to stop frivolous litigation that costs businesses millions of dollars, and helping small businesses provide their employees with health insurance.

While we have made progress, we can always do more. To fully illustrate to the world that South Carolina can and should compete on the global stage, we continue to examine and propose solutions that will ensure our meeting that end.

Broad-Based Incentives

We have expressed our concerns that our tax code has far too many incentives carved out for only one area of the state or for only one business that may come to our state. In fact, we asked the Department of Commerce to review our incentive system, and they reported back that “some of the current incentives contained within the tax code have become obsolete or have been amended to the point that they no longer serve their original purposes.” Accordingly, we believe it is time to stop singling counties or businesses out and take a look at our tax code in a much broader perspective.

1. Film Incentives

While we support the need for reasonable and effective film incentives, we continue to believe that South Carolina's current film incentives are neither creating permanent jobs for South Carolinians nor developing a sustainable, self-sufficient film production industry. Rather, in many cases film producers have used the generous wage rebates offered under the current program to provide jobs to out-of-state film crews that temporarily locate to South Carolina during filming and then leave the state. A recent study conducted by economist Frank Hefner of the College of Charleston confirms that film incentives are not producing positive returns for the state. For instance, Hefner's study

shows that the state's general fund loses what amounts to 81 cents for every dollar the state invests in film incentives. If the film incentive program was achieving its intended goal of creating jobs for South Carolina residents, then more income tax revenue would be coming into the state. However, in its current form, the film incentive program merely subsidizes jobs for non-residents with hard-earned dollars from South Carolina taxpayers.

We are not alone in questioning whether film incentives are effective in creating jobs and encouraging economic development, as several other states are presently considering eliminating or modifying their film incentives. Moreover, we are pleased that the South Carolina Senate has joined us in our efforts to improve the film incentive program by creating a study committee this year to review the program's effectiveness. We hope the Senate – and the General Assembly as a whole – will follow our recommendation to more narrowly focus wage rebates on film jobs for South Carolina residents. We believe that will have a more significant and longer lasting economic impact for the state and, consequently, the state's taxpayers.

2. Cabela's and Bass Pro Shop Incentives

When incentives are designed to heavily favor large job tax credits for one specific company, like Cabela's, but give no equal incentives to smaller competing businesses, there is the need to examine which incentives work and which do not. The original Cabela's incentive package allowed it to qualify for the job tax credit for the first time and entitled it to a possible 50 percent rebate of its sales tax revenue for reinvestment in its infrastructure – which could total an additional \$1.4 million per year. These incentives also included a \$2,500 per-job tax break every year for five years – amounting to \$3.75 million in incentives that the average small business or chain retailer does not get. Despite our objections, the provision became law. And instead of repealing these unfair incentives during the following legislative session, the General Assembly made a bad provision worse by applying these incentives statewide, lowering the standards necessary to qualify for state money, and guaranteeing the 50 percent rebate of the sales tax – all in an effort to recruit Bass Pro Shops.

We would love for these retailers to come to our state. Our only objection lies in paying them to come, which effectively gives their companies unfair advantages over smaller competitors around the state. This administration is not alone in our hesitancy. For example, Kentucky's legislative body rejected legislation that would have provided some \$20 million in tax incentives to Cabela's. For these reasons, we are attaching proviso language in this budget that will repeal the special incentives granted to retailers like Cabela's and Bass Pro Shops.

This administration is committed to allowing fair and equitable competition among businesses in the Palmetto State – no matter their size or capital investment. We believe that creating incentives for an individual business to come to South Carolina – while asking existing business in the state to subsidize those incentives – is unfair and contrary to the ideas of a market economy. Government should not be in the business of choosing winners and losers in the marketplace. Moreover, we believe that economic development legislation would be more efficient and better coordinated if it were vetted by the Department of Commerce.

A flat tax is a simple reform that will make South Carolina more competitive in the ever-evolving global marketplace, attracting jobs and capital. Currently, seven states have a flat tax: Colorado (4.63%); Illinois (3.0%); Indiana (3.4%); Massachusetts (5.3%); Michigan (4.35%); Pennsylvania (3.07%); and Tennessee (6%).

We believe it is time South Carolina taxpayers have the choice of a lower, flat income tax rate. Two other states have recently gone down this path by opting to give their taxpayers this choice. Rhode Island is currently in the process of phasing in an optional flat 5.5 percent rate as an alternative to their current "progressive" tax schedule. Current Rhode Island House Speaker William Murphy, a Democrat, said of the flat tax that "the ultimate goal is to put more money directly into people's pockets both by giving relief to those who need it and by making Rhode Island a more attractive place for business." Likewise, in Utah taxpayers now have the choice to calculate their individual income taxes based on a flat tax rate of 5.35 percent. Both of these flat tax options make for a simple calculation – exempting the need for deductions and exemptions.

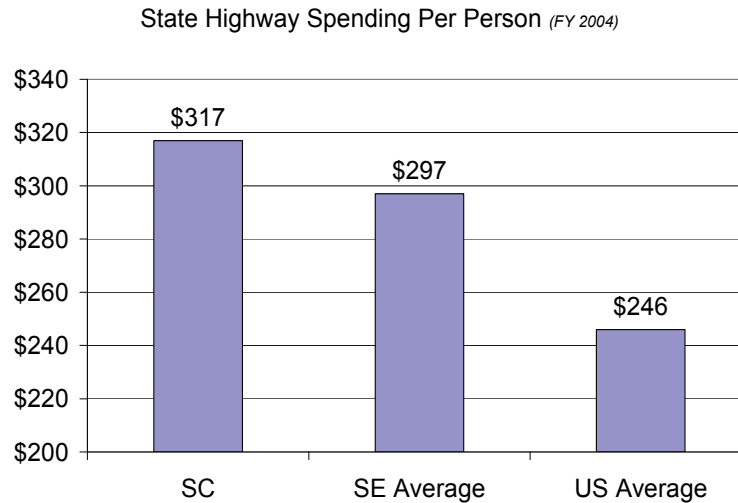
Other countries have also experienced success by implementing a flat tax as a means of improving their economic climate. Currently, over 20 nations have some form of a flat tax. Lithuania and Estonia adopted the flat tax only a few years after the collapse of the Soviet Union in the mid-1990s. These nations have reported increased tax revenues and a decline in unemployment. Lithuania has experienced some of the fastest growth in Europe since adopting the flat tax. Subsequently, Russia introduced a flat income tax in 2001, and four years after implementation, total real receipts from personal income taxes have more than doubled.

The benefits of our plan would end complex tax compliance and tax returns. The flat tax option is simply about giving the choice of a simpler, lower, and flatter income tax rate to the taxpayer. Our plan specifically calls for a 3.7 percent optional flat income tax rate with no deductions or exemptions – ultimately providing \$95 million in income tax relief. We also recommend full indexation of the individual income tax brackets – giving all income taxpayers relief for a total of \$7.2 million. We propose to offset the income tax revenue decrease with a cigarette tax increase of 30 cents.

A More Effective Way of Funding Roads

In January 2007, the U.S. Department of Transportation (USDOT) suggested that states consider leasing and selling their roads and infrastructure to private investors. USDOT Secretary Mary Peters offered model legislation for states to use to authorize public-private partnerships for "building, owning or operating highways, mass transit, railroads, airports, seaports or other transportation infrastructure." Some states, including Virginia, Texas and Indiana, have already passed legislation along these lines.

Currently, South Carolina funds its roads at a rate of \$317 per person – a level higher than the Southeastern average of \$297 per person and the U.S. average of \$246. In 2005, the General Assembly approved a 16 percent increase for SCDOT (\$86 million in recurring dollars). To put SCDOT's budget in a larger framework, the agency's total budget has outpaced the total state budget since FY 1995 – at 123 percent versus 77 percent. We think we should explore additional ways to improve our state's transportation infrastructure without placing more burden on South Carolina's taxpayers.



Indiana and Texas are examples of states already advancing this goal. In Indiana, the state Legislature and Governor Mitch Daniels authorized the 75-year lease of the 157-mile Indiana Toll Road to private investors for \$3.85 billion in up-front cash. In Texas, Governor Rick Perry has launched a 50-year plan to build nearly 1,500 miles of privately run toll roads along the portions of I-69 and I-35 that cross the state. But not just Republican governors are advancing public-private partnerships. In Pennsylvania, Democratic Governor Ed Rendell proposed entering into a long-term lease agreement for the Pennsylvania turnpike. The 75-year lease agreement, which was ultimately rejected by the state Legislature, would have ultimately netted the state \$12.8 billion from private investors. The private company would have also paid to operate and maintain the facility over the course of the lease.

Ultimately, entering into public-private partnerships to build and improve our roads and infrastructure would not only provide alternative means by which to fund repairs and improvements, but it would also have the potential to create new jobs and perhaps billions of dollars in investment in South Carolina while helping to improve the quality of our infrastructure – allowing us to better compete in a global economy.

In South Carolina, we believe that the I-73 project presents an opportunity for the state to utilize private investors to assist in moving this project forward. I-73 is a \$1.4 billion project, with \$100 million currently raised. At the rate money is being secured for this project, I-73 will not be built for decades. We believe that South Carolina should look for private investors who can finance this project and bring it to fruition in a timely manner.

We are encouraged by the formation of the Public-Private Partnership study committee. We hope that this committee produces meaningful legislation that will allow the Department of Transportation to explore the most effective way to utilize the private sector in ensuring all South Carolinians have safe roads.

Workers' Compensation

Two years ago, this administration signed into law comprehensive workers' compensation reform designed to enhance South Carolina's business climate. The law's goal is to stop increasing workers' compensation insurance costs and inject much-needed consistency into our state's workers' compensation system.

Businesses had been faced with alarming increases in premiums tied to compensating employees who are injured on the job. This problem was never more evident than when the National Council on Compensation Insurance proposed a 33 percent overall rate increase in 2005.

Key provisions of the workers' compensation reforms signed into law by this administration included abolishment of the Second Injury Fund, stronger language for costly repetitive trauma claims, stricter requirements for medical expert testimony, and reversal of a court decision that denied the employee's physician or health care provider from contacting the employer about the employee's injury.

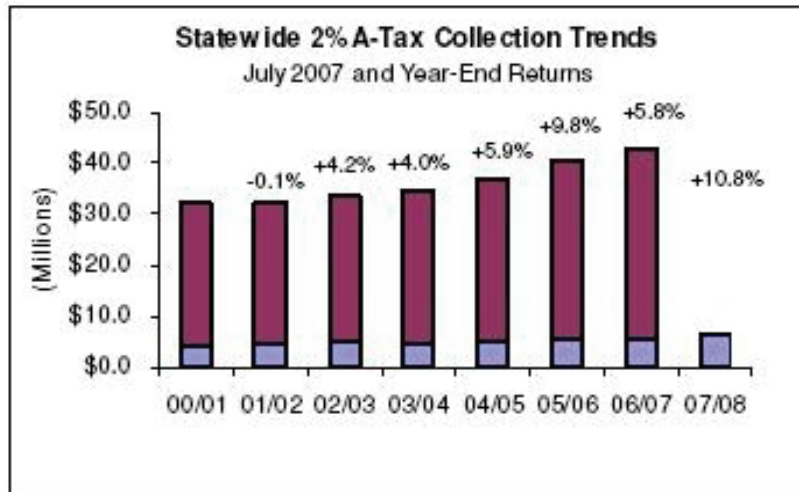
One critical marker that has not been reached by the Legislature is the adoption of objective standards. We fell short of truly comprehensive reform by not introducing a strict American Medical Association (AMA) provision – a requirement that commissioners must use objective standards in making disability award determinations. The current objective practice of awards has proven to be unfair to the South Carolina business community, as the workers' compensation awards are currently 181 percent of the medical guidelines that are used by other states.

While this marker was not met, we are very encouraged that reforms have had an impact on the workers' compensation system. For example, in November 2008, the National Council on Compensation Insurance recommended a decrease in premiums – for the first time in seven years. Also, in 2007 the Workers' Compensation Commission adopted a new form for claimants not represented by an attorney, requiring physicians to use the American Medical Association guidelines in determining medical impairment.

With these cost-lowering moves in the workers' compensation system, we believe more advances are possible for South Carolina's business community with a meaningful set of standards by which to evaluate workers' compensation injury claims.

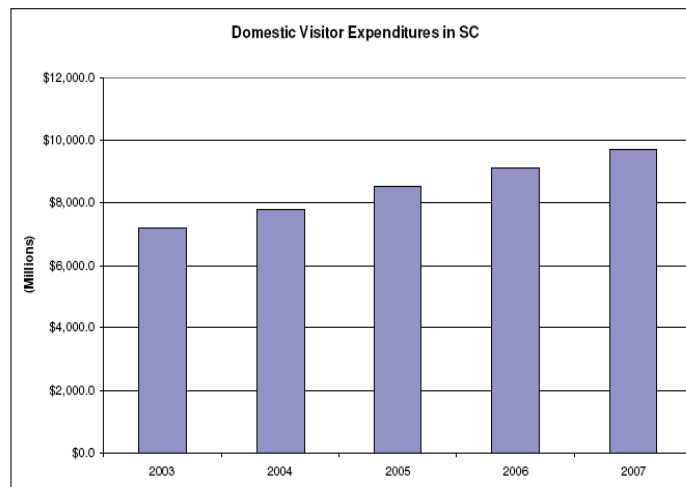
Tourism

The Department of Parks, Recreation, and Tourism excels at promoting South Carolina, while also providing jobs and opportunities for our workforce. Our state's \$16.7 billion tourism industry generates new dollars for the state's economy rather than recycling existing dollars. Tourism generates employment for 11 percent of the entire workforce and is the leading industry in our state.



Each year, more than 32 million people take trips in South Carolina, and tourism represents nine percent of our total Gross State Product or \$14.6 billion. In fact, when looking into the details of this overwhelming number, the tourism industry is only getting better. Last year, South Carolina had its highest level of hotel occupancy in the past seven years – and in May and June 2008, state accommodations tax collections were up 6.3 percent.

Continuing to focus tourism resources to provide the greatest impact to South Carolina's economy remains a priority of this administration. Further development of effective marketing techniques is critical to attracting out-of-state visitors. PRT continues to improve in this area as can be seen in total visitor spending. Since 2003, domestic travel expenditures in South Carolina have continued to grow a total of 26.3 percent. Domestic travel expenditures totaled more than \$9.7 billion in 2007, up 6.5 percent over 2006.



Whether it is informing international visitors about all that South Carolina has to offer for their vacations, or making folks in Georgia aware of our 46 state parks, publicizing the South Carolina brand brings visitors into our state and increases our state's revenue stream.

Moving the state's economy forward into the future by improving our state's underlying soil conditions for business is a significant priority of this administration. Maintaining a robust small business community, eliminating inherent regulatory barriers for companies when conducting business in South Carolina, making thoughtful government reform, and continuing to emphasize limited government spending and a low tax burden on the citizens of the state will all prove worthwhile in providing South Carolina with further opportunity in job creation and economic growth.

Meet the Health Care Challenge

Meet the Health Care Challenge

The blockbuster 2000 hit movie, *The Perfect Storm*, was based on a book written about ‘the storm of the century’ that hit off the coast of Maine in 1991. The strongest storm in recorded history, this perfect storm was actually two separate storms and one hurricane that combined into a single fury of 100-foot, unnavigable seas. America’s health care system is nearing the edge of its own perfect storm. The system is broken.

– Newt Gingrich, *Saving Lives & Saving Money*, 2003

Health care greatly impacts the quality of life in South Carolina. Overall, it encompasses more than a third of the entire state budget. In preparing this budget, one of the biggest challenges we face is dealing with the rising cost of all aspects of health care.

The National Association of State Budget Officers predicts double-digit growth nationwide in state spending on Medicaid over the next few years. South Carolina already spends roughly 20 percent of its state budget on Medicaid. In the next decade that number could rise to 30 percent, according to the South Carolina Department of Health and Human Services.

To combat the rising costs, our administration will continue to support market-based health care options that not only improve the quality of life, but also slow the growth of health care spending. A key part to managing Medicaid-related health care costs and enhancing the quality of care lies in giving recipients the tools and opportunities to become smarter health care consumers, as well as fostering competition within the system.

In this section of the executive budget, we will emphasize “Where We Are Succeeding” by highlighting several health initiatives touching the lives of our citizens – whether they be newborns, new parents, students, small business owners, patients, or senior citizens. The second section focuses on several “Opportunities for Improvement.” These topics include smoking cessation and surcharge, adoption and foster care, offering “mandate free” insurance, encouraging more government transparency, and health care restructuring.

Where We Are Succeeding

South Carolina is leading the nation when it comes to giving more health care options to Medicaid recipients that best fit their needs and implementing innovative and cost-saving reforms. Over the past five years, South Carolina has made significant headway in addressing health care costs – implementing a preferred drug list to save on Medicaid prescription costs, reducing fraud and abuse in the Medicaid system, implementing Medicaid fee-for-service co-payments, supporting a life-saving organ donor registry which conserves an estimated \$24 million Medicaid dollars, and becoming the second state in the nation to offer Health Savings Accounts (HSAs) to state employees as part of the State Health Plan.

This past year we have had additional accomplishments that will have a positive effect on the health of our citizens which, in turn, will help save taxpayers money. Accomplishments we are highlighting relate to the areas of health insurance, mental health, prevention, early detection and treatment efforts, rehabilitation, and nutrition.

Health Insurance Options

To provide another tool in helping make insurance more affordable for workers and small businesses in our state, we supported and signed Senate bill 588 that allows small businesses to band together to purchase health insurance for their employees. This reform is an important step toward helping small businesses compete and making health care more accessible to our state's workforce.

Our Medicaid recipients also now have more health care options. Medicaid is no longer a one-size-fits-all program. By implementing “South Carolina Healthy Connections,” we can now give individuals a choice in their health care plans and empower them to pick the plan that best suits their needs. Along with the traditional fee-for-service plan, beneficiaries have ten available options.

- To allow market-driven competition, South Carolina has engaged eight health plans that compete to serve our Medicaid beneficiaries which, ultimately, may provide extra benefits beyond traditional Medicaid. A key component of this reform is that beneficiaries will get connected to one primary care physician, or “medical home,” to help them better coordinate their care and get better quality care.
- To offer even more individualized services and encourage responsible use of Medicaid health dollars, the state designed a pilot program to study the benefits of offering HSA-style accounts to Medicaid beneficiaries. These accounts, called Health Opportunity Accounts (HOAs), are the first effort of their kind in the country. HOAs encourage prudent use of health care services and can support a beneficiary’s transition off Medicaid since a portion of any unused HOA funds can be used by the individual for health care, education, or job-training needs.

Prevention and Screenings

The importance of prevention as well as screenings cannot be stressed enough. The Hollings Cancer Center at the Medical University of South Carolina (MUSC) and the Department of Health and Environmental Control (DHEC) continue to promote healthier behaviors and prevention programs. With more public and private efforts and programs, the number of South Carolinians being screened is increasing. We have succeeded on many levels during the past year.

- To treat those living in medically underserved areas, the Hollings Cancer Center’s Mobile Health Unit traveled throughout 12 Lowcountry counties, providing more than 2,000 screenings. The center is working to expand partnerships with employers as well as school districts.
- To improve the health of our citizens, raise awareness of health issues, and encourage healthier decisions in day-to-day life, we continue to support the “Healthy South Carolina Challenge.” Each year, the First

Family participates in or hosts a number of fitness events, such as the 5K run on Sullivan's Island and bike rides through various small towns.

- To give free vaccines for underinsured children and youth, DHEC continues to work with many partners by developing agreements with the 20 Federally Qualified Primary Care Centers. DHEC is developing a Memorandum of Agreement with the National Association of School Nurses to partner in the development of web-based educational modules on diabetes care in the schools for school nurses. South Carolina is the pilot state for this program.
- To conduct the "WISEWOMAN" (Well-Integrated Screening and Evaluation for WOMen Across the Nation) program that provides screening and lifestyle interventions for many low-income, uninsured, or underinsured women aged 40–64, DHEC received a Centers for Disease Control and Prevention five-year grant. In addition, the "Best Chance Network" was expanded to enroll an additional 9,000 women for breast and cervical screenings, cardiovascular risk assessment, and follow-up. Funds were also received to support colonoscopy screenings for the uninsured.

Mental Health

As is true nationally, people with mental illnesses and substance abuse disorders continue to wait long hours in emergency rooms for treatment. The Department of Mental Health (DMH) and the Department of Alcohol and Other Drug Abuse Services (DAODAS) took the following steps to help alleviate this on-going problem:

- To help solve the difficulty in placing mental health patients waiting in emergency rooms, DMH was awarded a \$3.7 million grant from the Duke Endowment to use telemedicine technology for psychiatric consultations. South Carolina is the first state to use this type of telemedicine statewide. With video and voice equipment placed in emergency departments in hospitals throughout the state, hospitals will be directly linked to DMH where psychiatrists will be available 24 hours a day to conduct "face-to-face" consultations.
- By working through partnerships with private non-profits and local mental health centers, DMH is financing affordable housing for clients. Since its inception, almost 1,600 housing units have been established. People who have serious mental illnesses have better clinical success when treated in the community rather than living in state mental hospitals.
- By opening new beds in the community, stable mental health patients are able to move from psychiatric hospitals to community beds. These new community beds make more space available in psychiatric hospitals to admit those waiting in emergency rooms. In addition, DMH mental health centers established several projects geared toward providing crisis and other services, including providing on-call staff after hours, placing

mental health staff in local emergency rooms, and purchasing beds in local hospitals.

Detection and Treatment

The state recognizes the positive impact that early detection and proper treatment of diseases have on the quality of life of South Carolina communities. Whether it relates to cancer, substance abuse or the treatment of a disability, the state has seen success in many areas.

- To allow cancer patients the opportunity to benefit from promising treatments that are not currently available to the general public, MUSC continues to participate in a large number of clinical research trials. For example, MUSC's pediatric bone and marrow transplant program, which recently celebrated its 20th anniversary, is the state's oldest and largest of its kind.
- By continuing to offer a wide array of treatment services through its statewide network of nationally accredited county alcohol and drug abuse authorities, DAODAS is making great strides in an attempt to stop the disabling effects of alcohol, tobacco, and other drug abuse or dependence, and to prevent their recurrence. Tailor-made programs (i.e., day treatment, detoxification services, intensive family services) meet the unique needs of each individual. This past year, DAODAS reports marked improvement for their clients: more than 70 percent report no alcohol use following discharge from services (35 percent increase from 2007), and more than 75 percent report being employed following discharge from services (7 percent increase from 2007).
- To keep families together using the most cost-effective service approach for taxpayers, South Carolina continues to do a great job of supporting caregivers. This past year, the Department of Disabilities and Special Needs (DDSN) served more than 80 percent of the 29,000 consumers in their homes compared to only 60 percent nationally.

Rehabilitation

By enabling eligible South Carolinians with disabilities to prepare for, achieve and maintain competitive employment, the state encourages these citizens to become taxpayers instead of tax consumers. Estimates indicate rehabilitated clients will pay back \$3.20 for every vocational rehabilitation dollar spent. That results in the client repaying the cost of rehabilitation within 5.6 years – which is an 18 percent annual rate of return.

- With support from DDSN and the South Carolina Vocational Rehabilitation Department (SCVRD), more than 250 workers with disabilities will be hired by Walgreens (42 percent of the facility's workforce), which is the nation's largest drugstore chain. Walgreens became a showcase for the employment of people with disabilities when it opened its new distribution center in Anderson, South Carolina, last year.

- Last year, SCVRD had the nation's second highest rate of persons rehabilitated (per 100,000 population). The department rehabilitated 8,520 people with disabilities into employment.

Nutrition

Unhealthy eating and inactivity contribute to between 300,000 to 600,000 deaths each year, according to the U.S. Department of Health and Human Services – that's 13 times more people than killed by guns and 20 times more people than are killed by drug use. To motivate our citizens, there are several programs aimed at creating greater access to proper food and nutrition. For senior citizens, we propose to do the following:

- Ensure access to proper food and nutrition. DSS has designed the "Elderly Simplified Application Project" which simplifies the Food Stamp application process for low-income elderly. Since the inception of the federally approved project, the number of cases in South Carolina has doubled in three years from 11,134 (Sept. 2005) to 22,144 (July 2008).
- Increase the consumption of fresh, locally grown fruits and vegetables by seniors 60 years and older. The Senior Farmer's Market Nutrition Program provides low-income seniors with coupons that can be exchanged for eligible foods at farmers' markets and roadside stands. The program operates in 34 counties and provides benefits to approximately 24,000 low income seniors.

We also want to help the three out of every five South Carolina adults who are overweight and the one out of three students who are overweight. To do so, we support the South Carolina Eat Smart, Move More Coalition. This coalition is an ongoing collaboration between state agencies, business and industry, health care organizations, schools, and community members.

Additionally, First Lady Jenny Sanford and State Superintendent of Education Jim Rex joined together last year to promote the Healthy SC School Video Contest. This four-month contest, which offered cash and other prizes, challenged middle and high school students to create commercial-like videos about the importance of healthy lifestyles.

AIDS Drugs and HIV Testing

While investment in treatment and research is helping people with HIV/AIDS live longer and more productive lives, HIV continues to spread at a staggering national rate of more than 40,000 new infections a year. Last year, more than 700 South Carolinians were diagnosed with AIDS, bringing the total number of South Carolinians facing this disease to more than 9,000. To provide access to HIV/AIDS treatments to low-income, uninsured, and underinsured people living with HIV/AIDS, the South Carolina AIDS Drug Assistance Program (ADAP), managed by DHEC, has taken steps toward this mission.

To expand HIV testing primarily in clinic settings and to reach more African Americans, DHEC received a grant from Centers for Disease Control and Prevention. This grant allows the department to create new partnerships with three hospital emergency departments to initiate routine

HIV testing in counties with the highest rates of infection. This grant also supports funding to three community-based organizations for expanding HIV rapid testing and other interventions to reach high-risk African American men.

Opportunities for Improvement

While all of these successes are steps in the right direction, many challenges remain. In this executive budget we call for improvements in the state's adoption and foster care services, continue to encourage state employees to stop smoking, support offering health plans that are "mandate free" and, once again, request that the General Assembly reorganize our government in a manner that better serves our citizens. We can and must do better.

Smoking tobacco is one of the greatest sources of preventable disease and death in our population.

- **Dr. Louis Wade Sullivan, former Secretary of U.S. Health and Human Services**

Smoking Cessation and Non-Smoker Discount

With almost 65,000 employees, state government is one of the largest employers in the state. We believe it ought to use the same best practices being used by other employers to improve the productivity and quality of life of their workers by controlling health care costs. For example, many private programs offer smoking cessation programs with premium incentives because it makes good business sense. It is no secret that healthier workers are more productive workers.

Since 2005, the Budget and Control Board has included smoking cessation as part of the State Employee Insurance Plan. Interest is growing, and the results are encouraging. In 2006, more than 1,600 Plan participants were enrolled in the "Quit for Life" program. Since that time, it has more than doubled to include almost 3,300 participants. With a 45 percent quit rate, our hope is that more state employees will take advantage of this opportunity to beat their nicotine addiction.

Recognizing that non-tobacco users should not have to pay for the poor health choices of their coworkers, our administration pushed for the initiative to give state workers a discount if they do not use tobacco products. In August, the Budget and Control Board approved a \$25 monthly discount for employees who do not use tobacco products. We propose increasing this discount to \$40 to offset the \$115/month in tobacco-related costs to the State Health Plan. Although our administration recommended the discount begin January 1, 2009, it will be assessed in January 2010. With 400,000 participants, including employees and their family members, estimates show that around 75 percent of state workers will receive a discount.

The Budget and Control Board passed the measure, in part, to compensate for the approximately \$75 million per year that the state health insurance plan spends on tobacco-related illnesses. However, the discount does not completely cover the estimated \$115 monthly cost to ensure tobacco users. Accordingly, we propose to increase the non-tobacco users' discount to \$40 per

month and begin implementation on July 1, 2009. If individuals choose to use tobacco, that is fine. But they should not expect everyone else to pay for their poor health decisions.

Adoption and Foster Care

Currently, it takes nearly four years to finalize the average child adoption process in South Carolina. This is six weeks longer than the national average. A recent study shows that South Carolinians expect the adoption process should not take more than two years.

This administration has consistently called for improvements in the state's adoption and foster care services – from leading the fight starting in 2004 to restore adoption incentives from \$250 to \$1,500 to looking for ways to give foster parents some of the same rights as biological parents, to pushing for more case workers.

Over the past 10 years, more than 4,000 children were adopted in South Carolina, with more than 400 of those adoptions occurring just this past year. Still, there remain about 1,600 children seeking an adoptive home in South Carolina.

To help identify ways to improve the efficiency and quality of the state's foster care and adoption processes and, in particular, to reduce the time it takes to find permanent adoptive homes for the most vulnerable children across our state, we created the Children in Foster Care and Adoption Services Task Force in 2007.

The task force report makes a number of recommendations, including:

1. creating a registry for birth fathers to help expedite the termination of parental rights process;
2. streamlining the process for serving notice in adoption hearings;
3. accelerating hearings for termination of parental rights;
4. more aggressively recruiting foster and adoptive parents; and
5. hiring more DSS and court personnel dedicated to reducing the termination of parental rights caseload.

We have long believed that one of the state's primary roles is to protect and provide for vulnerable children. We hope to see the General Assembly evaluate the task force recommendations, which we believe will start us on the path toward more efficiency and reduced wait times for adoption, resulting in an improved quality of life for hundreds of children and parents across South Carolina.

Consumer Choice

While we celebrate the final passage of the health insurance reform bill that makes it easier for small businesses to band together to purchase employee health insurance, small businesses are still saddled with numerous mandates that, while well-intentioned, make the health care they offer less affordable.

The South Carolina Department of Insurance reports 30 different mandates cost families almost \$550 a year. Mandates not only increase the cost of health insurance premiums to the individual and

overall costs to employers, they also affect the marketplace. Although larger insurance companies can absorb these costs because of their volumes, smaller companies find them harder to absorb. This allows bigger providers to grab ever larger portions of the health care marketplace. Less competition ultimately leads to higher health insurance pricing for all families in this state.

To alleviate the mandate burden, we propose a “consumer choice” individual policy that could be made available for \$150 per month for those who only want coverage for large catastrophic expenses. This is less than half of the \$354 that the Kaiser Family Foundation states is the average monthly premium cost. Many of the uninsured are healthy young adults who could benefit from this type of coverage who may not want or need to pay for mandated coverage items (i.e., maternity benefits).

Transparency

To give the public an overview of how tax dollars are spent in support of Medicaid, our administration supports initiatives that increase transparency in government.

Recently, the South Carolina Department of Health and Human Services launched a searchable website that allows residents to see how much money individual Medicaid providers receive and how many patients they treat. The goal of the site is to provide a direct connection between Medicaid funding and purchasing.

Another goal of the site is to review and investigate any unusual provider billing patterns. It was quickly discovered that a pediatrician was excessively billing Medicaid but did not have documentation to support the claims filed. Ultimately, the case was referred to the Attorney General's office, and the provider was arrested and charged with fraud.

Using the transparency website, combined with several fraud algorithms, has allowed DHHS to open fraud and abuse reviews of multiple other health care providers. For example, data analysis revealed a top billing pharmacy was possibly “upcoding” in order to increase reimbursement. This case has also been referred to the Attorney General's Office, and similar investigations are currently on-going. As a result of this type of claims review process, DHHS expects to recoup at least a million dollars in state funds this fiscal year.

Health and Human Services Agency Restructuring

The Legislative Audit Council recommended in 2003 that the General Assembly consolidate the state's health and human service programs. This would eliminate duplication, allow more comprehensive planning and budgeting, and reduce administrative costs. In October 2004, the LAC produced a follow-up report, which concluded none of the health and human service restructuring recommendations had been implemented.

As we have said in the past, our largest obstacle to improving health care in South Carolina continues to be the fractured health care system we have within state government. Currently, we have separate government agencies answering to four different authorities, providing health services. Many programs and services in these agencies overlap in functions and lack coordination. In

addition, the administrative burden of operating those agencies takes dollars away from the frontline services of providing expedient and adequate care and protection to the patient.

Our health care restructuring proposal is focused on reducing these overlapping functions into fewer health care agencies. We propose the merger of these health and human services agencies into one accountable and affordable delivery system under a cabinet-level director to improve accountability, care, and responsiveness to our citizens.

Our recommendations include renaming the Department of Health and Human Services to the Department of Health Oversight and Finance. This agency will continue to be the lead agency for Medicaid oversight and finance of Medicaid expenditures.

Additionally, the Department of Health Services will consist of four divisions:

1. Division of Public Health (currently the health programs at the Department of Health and Environmental Control);
2. Division of Mental Health (currently Department of Mental Health);
3. Division of Disabilities and Special Needs (currently Department of Disabilities and Special Needs); and
4. Division of Addiction Services (currently Department of Alcohol and Other Drug Abuse Services).

To better utilize limited resources, we also recommend creating the Department of Rehabilitative Services which merges the Vocational Rehabilitation Department and the Commission for the Blind.

While we continue to believe a much larger health care restructuring bill is key to improving service delivery and accountability within this area of state government, this administration strongly supports the restructuring efforts taken by the House of Representatives in 2008. We look forward to working with both the House and Senate in 2009 to move a meaningful restructuring bill across the finish line. Our Health Care Restructuring Plan is discussed in greater detail in the Modernize Government section of this executive budget.

Improve K-12 Student Performance

Improve K-12 Student Performance

The public education system is one of the most important functions of any state government – intertwined with a state’s economic development, healthcare, public safety, and quality of life. With the flattening of our world, South Carolina’s students are now – more than ever – competing with students from Baltimore to Brazil to Bangladesh.

We must ensure that our students are adequately prepared to compete in the global economy, and this must be achieved at a time when our state and nation are facing unprecedented economic difficulties. During lean budget years we believe it is important to continue to focus the maximum amount of resources into the classroom – not on administrative programs. Now, more than ever, it is critical that we eliminate duplicative, non-performing programs and services and use our limited dollars to achieve our goals of raising scores on state and national assessments, closing the achievement gap between racial and socioeconomic groups, and producing more graduates who are ready for college and the workforce.

State Education Superintendent Jim Rex and the Education Oversight Committee have recommended that the state freeze teacher salaries for the FY 2009-10 school year. This administration has found other ways to keep budget cuts from affecting teacher pay – such as eliminating administrative overhead at the Department of Education – but deep budget shortfalls have prompted us to concur with the recommendation to freeze teacher salaries for FY 2009-10.

Operating our education system on limited resources does not mean that quality should suffer; rather it presents an opportunity to find innovative ways to teach our students, which we believe can be done by providing school choice. At the end of the day, we believe school choice is an important route to improving education in our state. Every child is unique, and we believe that parents are best positioned to determine what would most benefit their children. We want to introduce market competition and educational choice, restore parental control of education, improve public school performance, and expand educational opportunities for low and middle-income families by offering scholarships to help cover tuition costs.

Developing Our Purchasing Priorities

Our goal since the beginning of this administration has been to see every child make academic gains in kindergarten through 12th grade and to obtain a high school diploma. To that end, we examined

Administration's Goals for Improving K-12 Student Performance are to:

- ✓ Increase high school completion rate.
- ✓ Increase student participation, completion, and achievement in rigorous college-preparation courses.
- ✓ Raise the national performance ranking of South Carolina’s students on the SAT, ACT, and NAEP.
- ✓ Eliminate the academic achievement gap.
- ✓ Improve efficiency with which education dollars are spent.

the major indicators of success to determine whether our state is reaching its goal. These indicators helped to determine our purchasing priorities. We have found that South Carolina is making some progress; however, there remain many opportunities for improvement.

Where We Are Succeeding

We have made some progress in K-12 education, especially during this past school year. Palmetto Achievement Challenge Test (PACT) scores improved in all grades, in all subjects, and for all demographic groups. Additionally, we are increasing participation, scores, and the number of students taking Advanced Placement exams.

On the End-of-Course tests – which are required for high school students – more students earned passing grades in English and physical science in 2008 than in the previous year.

On a national level, we are delighted that nineteen of our schools earned recognition through the 2008 *U.S. News and World Report* rankings as “America’s Best High Schools.” The news magazine ranks high schools across the nation each year based on the school’s efforts to prepare students for college. Charleston County’s Academic Magnet High is ranked ninth among the nation’s top 100 “gold” schools, which is a jump from the school’s ranking of 27th in 2007.

Pickens High School in the Pickens County School District earned national recognition for drop-out prevention efforts in 2008. The school earned the National Dropout Prevention Center's Crystal Star Program Award of Excellence in Dropout Recovery, Intervention and Prevention for its model program called “Star Academy.” The academy opened in 2005 as a public-private partnership, which takes students at-risk for dropping out through a rigorous course that allows them to complete eighth and ninth grade in one school year. During its three years of operation, the Pickens Star Academy has progressively improved its success rate, advancing 73, 76 and 90 percent of over-aged eighth and ninth-graders to the 10th grade in just one year. The program has now expanded, as there are 14 Star Academies in 12 South Carolina districts.

Additionally, Jobs for South Carolina’s Graduates is another drop-out prevention model that has proven successful. Our office has been supportive of JAG-SC – which is adopted from the national model called “Jobs for America’s Graduates” – since its inception in 2005. Begun under the State Workforce Investment Board, JAG-SC uses a vocational skills curriculum and local businesses partner with participating high schools to offer job training, mentoring, or internships to at-risk students. JAG was piloted in 14 schools and 95 percent of students returned to school after participating in the program. Suspensions and absenteeism decreased, while academic gains increased. The model was implemented in five new schools in the 2008-09 school year with the help of funding through our state’s Education and Economic Development Act.

Opportunities for Improvement

Although we have made some progress in educational performance due to outstanding efforts of teachers, students, and parents on the frontlines, we cannot ignore the glaring statistics that indicate we have much farther to go to close the gap that exists between South Carolina and the rest of the nation. Ultimately, we want to see every child succeed. To accomplish this, we have established a

set of five goals, one of them being paramount: increase the high school completion rate. Our four other goals will aid in achieving our primary goal.

1. Increase the high school completion rate.

No matter how it is calculated or which research group reports it, South Carolina's high school completion rate is entirely too low. It is unreasonable to expect our state to progress if only half of South Carolina's students are completing high school on time. Our goal is to significantly increase the percentage of entering high school freshmen who complete the 24 credits required for high school graduation in eight semesters or less.

A 2008 report using the National Governor's Association (NGA) Graduation Counts Compact rate shows that only 55.6 percent of South Carolina's students graduated on time, which is 15 percentage points below the national average of 70.6 percent. This abysmal completion rate places South Carolina fourth from last in national rankings.

In this year's executive budget, we outline several major goals and invest in activities that increase the likelihood that a student will be prepared to enter and complete high school within four years.

2. Increase student participation, completion, and achievement in rigorous college-preparation courses.

South Carolina's position in the global economy can largely be determined by the rigor of the education we provide for our students. As we focus on getting more students to finish school on time, we must also monitor the quality of their education. It's one task to get students through high school, and it's quite another to have our students finish high school ready for the workplace or college.

To increase participation and success in rigorous courses, our budget funds activities that challenges students who are proficient, remediates students who have fallen behind, and ensures that our youngest learners have a strong foundation. To measure South Carolina's progress toward these goals, we will evaluate high school participation rates in college preparatory courses, dual enrollment programs, Advanced Placement courses, and International Baccalaureate (IB) programs. We measure elementary school rigor by tracking participation in gifted and talented programs and IB offerings.

3. Raise the national performance ranking of South Carolina's students on the SAT, ACT, and NAEP.

Though South Carolina's average test scores for graduating seniors on the SAT and ACT have increased slightly since 2007, these gains have had no major impact on the state's overall national ranking – indeed most other states are improving at a faster rate. South Carolina's scores on the National Assessment of Educational Progress (NAEP) have improved to the point that they approach and even surpass the national average on some assessments, but we still lag in comparison to other Southeastern states. We must increase the number of students who are scoring "proficient" in every subject. The Education Accountability Act of 1998 set ambitious goals for the performance levels, with the hope that South Carolina will rank in the top half of the states on the SAT, ACT,

and NAEP by 2010. We are one year away from the target date set in the legislation and have made little progress toward meeting this goal.

We will continue to measure progress toward this goal by tracking student performance on NAEP, the ACT and the SAT – in terms of average score, national rank, and proficiency levels in all subject areas.

4. Eliminate the achievement gap.

The fact that only nine percent of African American eighth-graders are proficient in reading on NAEP compared to 35 percent of Caucasian eighth-graders is unacceptable. Between 2003 and 2007, the achievement gap actually *widened* between African American and Caucasian students scoring proficient on NAEP in fourth-grade reading and eighth-grade math. In 2008, there was a 100-point difference between reading, math and writing scores of African American and Caucasian students in South Carolina on the SAT. According to the Alliance on Excellent Education, more than \$2.6 billion would be added to South Carolina's economy by 2020 if minority students graduated at the same rate as Caucasian students.

The second achievement gap is in the difference in the performance of more affluent students compared with those students from low-income homes. These gaps present our state with the challenge of understanding and closing these gaps by raising the performance levels of lower-achieving students.

We propose purchasing activities that help all students excel, while focusing on raising the achievement of lower-performing students. Progress toward this goal will be measured using scores from the new state assessment known as Palmetto Assessment of State Standards (PASS), the exit exam, NAEP, the SAT, and the ACT. We will also track high school completion rates among low-income and minority students – which have been historically lower on a national and state level than that of Caucasian and affluent students.

5. Improve the efficiency with which education dollars are spent.

Our current fiscal state requires us to operate with significantly limited resources, and reaching our educational goals is directly tied to maximizing the percentage of the educational dollar spent directly in the classroom. This maximization is done by eliminating expenditures on services that are not linked to specific goals, reducing or eliminating expenditures associated with activities that have weak outcomes, minimizing duplicative services, and improving productivity. One recent example of poorly prioritized spending can be found in Richland School District One, which is spending more than \$400 million on a 17-school building program. Within this project, \$64 million will be spent on “architecture, engineering and professional services,” according to the Columbia Business Report. At a time when this school district and others are considering laying off certified teachers in the 2009-10 school year to deal with budget cuts, we think it is an unwise decision to be focusing on capital projects. In fact, we would be surprised if this were the only example in South Carolina where funding needs could be better prioritized. This is money that we believe could be better spent on teacher pay.

Reducing administrative overhead is another way that money could be saved and better spent in classrooms. For example, we believe there is wasteful spending on administrative salaries at the State Department of Education. The department employs a total of 961 personnel, 400 of whom are school bus shop employees. However, we are far from convinced that it requires the remaining 561 staff to run the Education Department, particularly when the school districts are largely independent in their program offerings and operations. At a time when state budget woes have eroded the base student cost, we should focus on keeping as many dollars as possible in the classroom and reducing funds in administration through elimination or consolidation of certain positions.

Our state budget shortfall left a hole that totaled close to \$1 billion in FY 2008-09. This resulted in multiple cuts to K-12 education, which eroded the Base Student Cost from \$2,578 to \$2,255.

Our purchase plan maintains many educational services but redirects some existing funding to activities that directly impact students and teachers in the classroom. Many activities that, while inherently good, are not essential to reaching the goals we have established. Overall, we recommend funding \$2.237 billion from the general fund toward K-12 education. We believe that these dollars should be directed to the frontline of education – teachers and classrooms – which is why we are concurring with the proposal of State Education Superintendent Jim Rex and the EOC to maintain teacher salaries at the current average of \$47,376. Rather than offering an across-the-board salary increase, we believe students are best served by requiring that districts institute merit-pay systems to determine each teacher's salary increase.

In the tough fiscal year that our state faced, across-the-board cuts proved detrimental to K-12 education. Millions of state dollars were depleted from school district budgets, which ultimately eroded the Base Student Cost. We are recommending restoring the Base Student Cost to \$2,339, and we believe it is important to emphasize that this number does not represent all funding dollars. Including local, state, and federal dollars, the Board of Economic Advisors has estimated total funding per student to be \$11,867 in FY 2009-10. Though the Base Student Cost is sometimes used as the ultimate measurement of education funding, we believe it is more important to consider all types of funding when making this analysis.

Purchasing Priorities

After identifying opportunities for improvement, we next looked at the following strategies that will enable us to set priorities for our purchasing plan and how best to achieve our goal:

1. Ensure that every child is ready to enter first grade.

If children are not adequately prepared to learn in their early years, it becomes increasingly difficult for them to catch up and meet academic challenges as they progress through the school system. Making sure that all children are well-prepared for formal schooling requires that developmental deficits are addressed by early childhood educational experiences. Effective early childhood programs – whether public or private – are vital for children whose home environments are not preparing them for successful elementary school experiences. High-quality early childhood developmental education will evolve as standards for developmental education are more clearly defined and communicated.

2. **Provide all students an education that equips them with the skills necessary to compete in the regional, national, and international marketplace.**

Our students must be prepared to complete high school and enter college or the workforce with the skills needed to be successful. Our investments in education activities cannot lose sight of the fact that a key purpose of an education system is to cultivate a productive workforce. A high-quality education is one that challenges students to meet high expectations while engaging them in experiences that are relevant to the real world.

3. **Provide all students with a customized learning experience.**

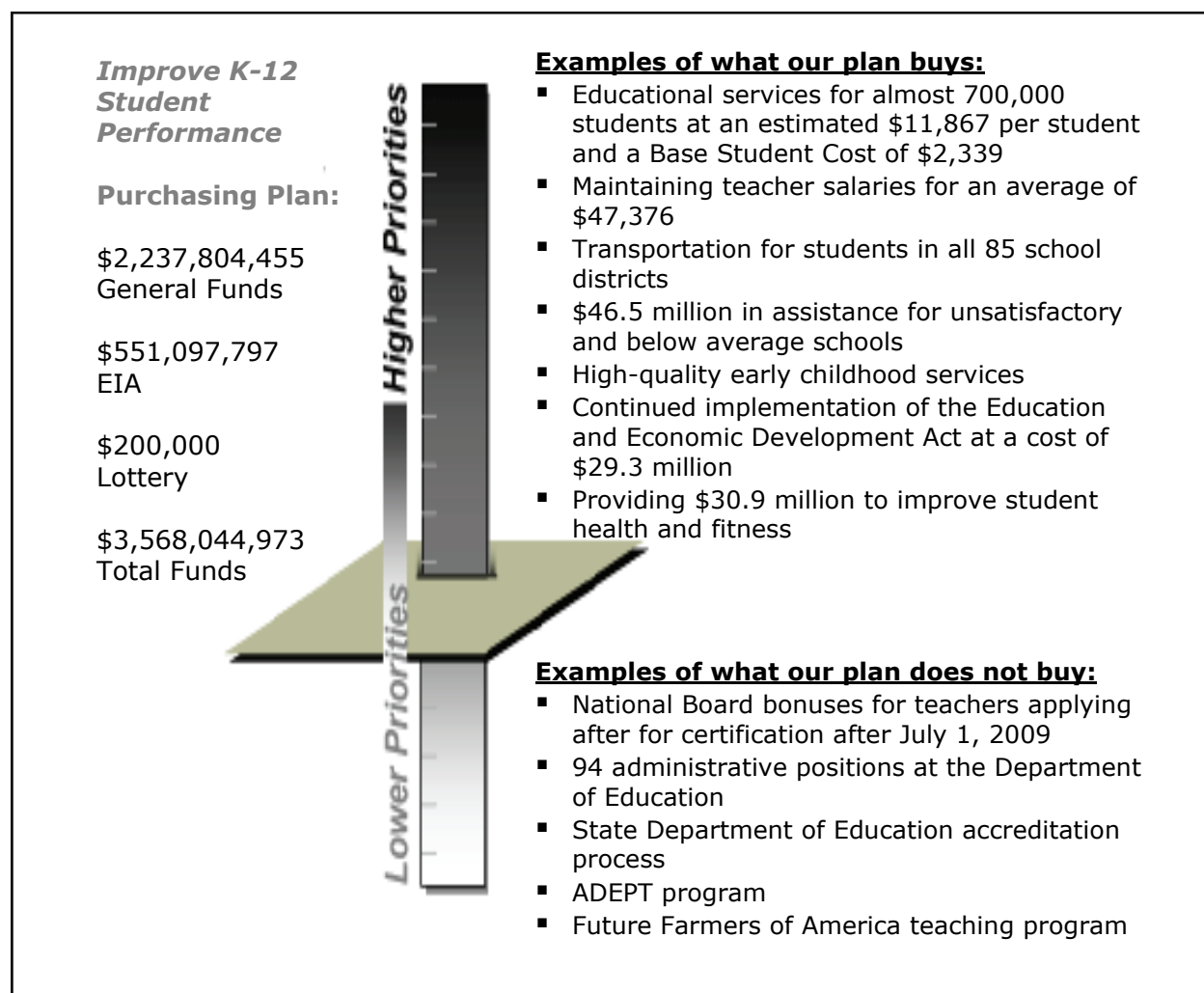
Before the school system can even begin to provide students with the skill set they need, their minds have already been shaped by various societal forces. These forces include family life, stress level, cultural factors, social life, health, emotions, and previous educational experiences, which all work together to shape how a child's mind works. Since there are so many factors that influence how, when, and whether a child learns any given lesson, it stands to reason that an effective school system is one that offers a multitude of learning environments so that parents have the options they need to find the right fit for their children.

4. **Provide public, clear, specific, and timely data about the effectiveness and competitiveness of public schools in the state.**

South Carolina's existing accountability system provides report cards that help parents understand how well their children's district or school fares in comparison to others. In the spring of 2008, major revisions to the accountability system were made. The state's standardized test, PACT, will be replaced with a new exam for students in third through eighth grades called the PASS, Palmetto Assessment of State Standards. With this exam, teachers and parents should now receive student performance data earlier than they received the PACT data. Although we have concerns about how the new scoring system and performance ratings system will affect our national competitiveness, this administration let legislation regarding the new standardized test and revised accountability measures become law without signature because we recognized teachers' desire for more diagnostic data in a timely fashion to assist students who are falling behind. While it is fine to change the assessment tool, we believe it is also vital to change the underlying system.

Governor's Purchasing Plan – Highlights

As we address our state's unprecedented financial problems, it is important to focus on purchasing only those education services that deliver the greatest impact on improving K-12 performance. In many cases, we have had to use cost savings methods to simply maintain current funding levels for high priority services. We do not purchase services that, while still considered valuable, have been identified as lower priority. The following table identifies key purchases within our executive budget's total state K-12 spending plan as well as examples of what is not purchased. Detailed highlights of our purchasing plan are provided below the table.



Our Plan Buys:

Basic frontline education services for nearly 700,000 students served in the 85 school districts throughout the state, in addition to the South Carolina Public Charter School District and the

Palmetto Unified District. Our plan restores funding per student according to the Education Finance Act (EFA). With funding of \$2,339 per weighted pupil unit distributed through the Base Student Cost formula, we are granting local school districts complete funding flexibility to provide educational services required for kindergarten through 12th grade students. We believe that this flexibility should be used to prioritize funds to the classroom first, with teacher salaries being a key part of this. Granting school districts maximum flexibility will allow us to **maintain teacher salaries for the FY 2009-10 year, as recommended by State Education Superintendent Jim Rex and the EOC**, to fulfill our goal of driving dollars directly into the classroom.

Creating the Palmetto Early High School Graduation Scholarship program in order to reward students who finish high school early through the creation of grants that can offset the cost of attaining postsecondary education or training. Beginning with the Class of 2010, students who finish high school in less than eight semesters qualify for the program. This program would provide our high-achieving students an incentive to finish coursework early, while addressing the need to eliminate the “senior year off” mentality that has become an entrenched part of the student educational culture in South Carolina. By **committing \$1,200,000 to the Palmetto Early High School Graduation Scholarship**, we can provide grants worth up to \$2,000 for students who finish high school in six semesters.

Supporting South Carolina Public Charter School District, which offers parents more educational options for their children. Facilities and transportation are the two major hurdles that charter schools face during their approval process. To help clear these hurdles, we will **maintain funding of \$3,437,741 in total funds** to continue services offered through the statewide charter schools district.

Addressing childhood obesity through the FitnessGram assessment. Dr. Kenneth Cooper of the Cooper Clinic in Texas developed the FitnessGram, a health program that tests the strength, endurance, and agility of children. In 2007, Texas Governor Rick Perry signed into law new requirements for public school physical fitness classes and also mandated that each school test its students annually in the FitnessGram. After one year of implementation, preliminary surveys found that Texas students who performed at high levels on the FitnessGram were also more likely to perform better in academics, attend school more regularly, and have fewer discipline problems. We believe that South Carolina can realize the same positive results as Texas through this program.

There is a saying that “You can’t manage what you can’t measure.” We believe that implementing the FitnessGram in our schools will help us begin to manage obesity among our children. In 2008, this administration and Superintendent Jim Rex of the State Department of Education formed a partnership to promote FitnessGram. Thanks to a private donation, the cost of purchasing software for each district will be covered without the need for any state funds – providing a noteworthy example of public-private partnerships. As early as the fall of 2009, schools can voluntarily give the FitnessGram assessment to students in grades 3 through 12, and a “report card” with each student’s results will be sent home to parents to encourage them to keep their children healthy and fit. We will fully support this initiative, as we realize the impact that healthy living has on academic performance.

Funding the Student Health and Fitness Act of 2005 to address the growing obesity epidemic among the youth of our state. The Student Health and Fitness Act is an effort to combat the

growing health concerns that are emerging as a result of the declining health of our students in South Carolina. Starting at an early age, increasing the awareness of citizens about health choices can lead to a healthier life. We propose **maintaining funds of \$30,929,614** for its continued implementation. Our appropriation is \$300,000 less than the previous fiscal year, as Superintendent Rex believes this amount could be offset through the private sponsorship of the FitnessGram software, which would aide in meeting physical fitness assessment requirements under this legislation.

Funding the Education and Economic Development Act (EEDA) in order to restructure elementary and secondary school curricula so that they are more effective and relevant to student interests. The EEDA can increase the chances that more students in South Carolina will receive a competitive education, which will encourage students to enter postsecondary studies or enter the workplace in the field that most interests them. To support the objective of the EEDA, we **recommend funding of \$29,255,091** for the fourth year of implementation of this legislation.

Supporting the South Carolina Virtual School programs in order to shatter the barrier that geography places on student access to high-quality educational experiences. Students in smaller, rural schools are currently taking advantage of rigorous courses such as advanced computer programming or Advanced Placement Calculus that currently are limited to students in schools with large enrollment levels. At the same time, we provide the opportunity for lower-performing students to receive high-quality remedial education that is currently denied them simply because their assigned school lacks the expertise to address their specific learning need. While we recommend freezing vacant positions for this program in this difficult budget year, **we support maintaining \$2,574,005 for the South Carolina Virtual School program.**

Providing transportation to and from school for more than 700,000 students. We understand the need to provide support for a state school transportation system, which is crucial for those students unable to provide their own means of transportation. We propose **maintaining total funding for the transportation needs of our students at \$124,727,767.** In addition to fully funding fuel for our public school transportation system, our purchase plan provides more than \$48,164,212 in general funds for school bus and \$46,528,048 in maintenance staff salary adjustments. Even though we are laying these dollars on the table, we continue to urge the General Assembly to look at the idea of leasing our current system. In an analysis commissioned by the Department of Education, the TransPar Group highlighted the fact that the state could reduce both the costs and the time necessary to improve the school bus replacement cycle by leasing more of its fleet rather than by purchasing the fleet. To date the recommendations of the TransPar Group have gone largely ignored. During these tight budget times we, once again, propose that the State Department of Education issue a request for proposals for leasing agreements that could be used to accelerate the rate at which our older buses are replaced with newer, up-to-date vehicles. The leasing option will provide safer transportation for our children at a better price for the taxpayer.

Assistance and accountability for underperforming schools. The 2007 School Report Cards, issued annually by the Education Oversight Committee (EOC), make it clear that our lower-performing schools need more effective technical assistance options than are currently being offered. But in a tight budget year, the Department of Education will have to find creative ways to implement effective technical assistance options. The Report Cards show that 15 percent of students in South Carolina are enrolled in 172 schools with a rating of “Unsatisfactory,” while nearly

27 percent of students are enrolled in the 296 schools with a rating of “Below Average.” These figures make it evident that many schools are simply not improving at the rate necessary to reach the goals established by the Education Accountability Act.

Periodic exposure to high-quality teaching will not improve the student achievement in our “Below Average” and “Unsatisfactory” schools. Sustained improvements in schools that need technical assistance will not occur unless the teacher and leadership turnover issues are addressed. Put simply, these schools need access to options that will mitigate the high teacher and principal turnover rates that cripple the schools’ efforts to improve. In order to assist these schools in overcoming the obstacles that have limited their success, we concur with the EOC’s recommendation of reducing technical assistance funding by \$32 million, which leaves **\$46.5 million to fund this item**. With a reduced amount of technical assistance funding, and with more schools that will meet criteria to receive this funding in FY 2009-10, we concur with the EOC that the State Department of Education set levels of funding for “Unsatisfactory” (which will be known as “At-Risk”) and “Below Average” schools, with the Education Department working persistently with underperforming districts to implement innovative strategies for improved student achievement.

High-quality pre-school programs that provide direct services for almost 25,000 pre-kindergarten children throughout the state. First Steps works across our state to prepare youngsters for school. Although it is a program that was started by the previous administration, we feel that by coordinating the services provided by state agencies and by fostering public-private community partnerships, First Steps can help prepare our children for the challenges they may face in the future education system. For this reason, we recommend **appropriating \$16.9 million** to support its efforts. Additionally, we will continue to support the Childhood Education Development Pilot Program, and we recommend funding **\$20.5 million** for this program, with administration being housed only at South Carolina First Steps.

Our Plan Saves By:

Discontinuing National Board Certification salary bonuses for teachers completing the process after June 30, 2009. We accept the recommendation of the EOC, as our state invests more than any other state in our region in this incentive, which is not directly tied to improving student achievement. Though it is important for the state to honor the commitment made to teachers who have already completed the process, we believe that expanding the program to newly certified teachers in FY 2009-10 would be an irresponsible use of state funding during times of economic downturn, especially when these bonuses are not limited to teachers working in low-performing schools or teaching critical subjects. In FY 2008-09, more than \$45 million of EIA funds and \$8.4 million in general funds were appropriated for National Board incentives. In December 2008, there were 750 more teachers who earned the certification, which obligates our state to \$56.2 million over the next 10 years to support bonuses just for these new entrants. Discontinuing the bonus will result in a **cost savings of \$3,250,000 million**.

Suspend funding for textbooks for one year. We accept the Education Oversight Committee’s recommendation on suspending funding for textbooks for one year. They suggest that the Department of Education could look at other options to provide student materials, including

electronic versions of textbooks and online learning materials for the 2009-10 school year. This will result in a **cost savings of \$23,904,571.**

Freeze Hiring at the Department of Education. At a time when resources are limited, it is important that every dollar be focused first to the classroom. Currently, the Department of Education has 93 unfilled positions. In their FY 2008-09 budget projections, the department has taken into account freezing 40 of these positions. We recommend freezing the remaining 53 positions which results in a **cost savings of \$2,650,000.** Further, we believe that, by virtue of operating without these positions up until this point, the Department of Education has shown that these positions are superfluous and unnecessary. We recommend that the department eliminate these positions entirely.

Reducing funding for assessments, evaluation and review of the High Schools that Work Model through the EEDA. State Department of Education officials have recommended suspending any assessments during FY 2009-10 that are not required by federal regulations. The assessments required by High Schools that Work (HSTW) fall in this category. We recommend that these tests be suspended during FY 2009-10, resulting in a cost savings of \$438,480. Additionally, we recommend suspending professional development for the 175 high schools that have already implemented the HSTW model, which results in a savings of up to \$1,137,500. In FY 2009-10, we recommend funding HSTW in the amount of \$308,000 for professional development in the 28 schools implementing HSTW for the first time. This results in a net **cost savings of \$2,792,800.**

Making Tough Choices:

The current economic challenges have forced many South Carolinians to make some serious decisions about how they will spend – or save – their personal income. Similar to the challenges facing households across South Carolina about how to prioritize spending, the finite resources of the state require that we make difficult choices about how we will direct the limited resources available to us. These choices better reflect our desire to be fiscally responsible with taxpayer dollars by limiting government spending only to activities that are of the highest necessity. Our choices are not a criticism of the merit of the forgone activities. The following items represent some of the difficult choices we've made on educational activities that we chose not to purchase in this year's executive budget.

Reducing administrative costs at the Department of Education. We strongly emphasize that our goal is to maximize the impact our education dollars have on South Carolina's children. To do that, these funds *must* make it to the classroom in the form of instructional dollars and teacher salaries. When times are tight, our first move should be to eliminate duplicative and non-essential administrative costs – particularly at the state level – rather than making cuts to the Base Student Cost. Unfortunately, the Department of Education has chosen to limit the difficult cuts that should be made in Columbia, and instead has slashed classroom funding. Accordingly, we propose cutting **94 positions out of the 961 administrative positions at the State Department Education saving \$6,806,248, and redirecting this funding to the base student cost.** In tough fiscal times, it is incumbent upon us to make sure all of our K-12 education dollars make a difference in the classroom. We are confident that the department will remain capable of fulfilling its statutory obligations after this reduction in force.

Eliminating the funding for the State Department of Education school accreditation process and requiring the Department of Education to fully implement the 2004 recommendations of the Legislative Audit Council review. We commend the Department of Education for adopting a portion of the LAC recommendations, thus reducing annual state expenditures on this activity by \$280,000. However, we believe this agency should fully adopt the recommendations of the LAC by completely eliminating their accreditation process, and instead only use the Southern Association of Colleges and Schools (SACS) accreditation process. The State Department of Education should encourage all eligible schools to pursue SACS accreditation – which most schools already use – thus eliminating this duplicative regulatory function at the state level. Making these changes will result in a **cost savings of \$269,483.**

Eliminating funds for Agricultural Education Teachers. This funding comes to Clemson University and is a pass through to the K-12 school districts. It supports Future Farmers of America teaching positions. While the agricultural science lessons learned through the FFA courses are valuable, they reach only five percent of high school students and are not required courses. Additionally, the South Carolina Department of Education says there are no other special teacher line items in the K-12 budget (including other vocational courses such as computer or business technology); therefore, it would be unfair to continue to support this special funding. In the tough financial times our state is facing – when we are at the point of freezing salaries for all other classroom teachers – we should focus primarily on funding teaching positions that will aid our students in earning a high school diploma. While agricultural courses have merit, our focus must be on funding core subject areas such as reading, writing, and math. If a student cannot read or write, it is likely that they will not be successful in the business management aspect of farming, which is why we must focus on supporting core subjects in K-12 education. This will result in a **cost savings of \$405,599.**

Eliminating the ADEPT program. This program, which is similar to the National Board Certification process, is input-driven and is not tied to statistically-significant increases in student achievement. The Assisting, Developing, and Evaluating Professional Teaching (ADEPT) program has merit, as it can lead to more introspective teaching when properly implemented. However, the quality of program implementation varies significantly from school to school and district to district. Additionally, the professional development offered by the ADEPT program is duplicative of a specific professional development program that the state currently funds at the same time. It is less effective than other professional development models such as the Teacher Advancement Program and the South Carolina Teacher Incentive Grant, both of which we support, and both of which are directly tied to academic gains in student performance. In tough budget years, there is no need for our state to have duplicative teacher evaluation programs. This will result in a **cost savings of \$2,150,728.**

Please see the Appendices for a complete listing of the Governor's Purchase Plan for this goal area and for a detailed listing of what our plan saves and what our plan does not buy.

Improve Our Higher Education
System and Cultural Resources

Improve Our Higher Education System and Cultural Resources

Our goals for South Carolina's higher education system are to better prepare our workforce for the challenges of a competitive global marketplace, raise the standard of living for South Carolinians, meet changing workforce needs, and create economic development opportunities. The challenge is to achieve these goals with dwindling resources, as significant budget shortfalls resulted in cuts to higher education budgets by more than 22 percent during the 2008-09 Fiscal Year. We want more South Carolinians to be able to access our higher education system, so they can survive in an increasingly competitive job market, but this feat will be difficult to accomplish if current trends in tuition increases remain unchecked.

At a time when families are making tough decisions on household spending, we want higher education to be a realistic option for South Carolinians, which is why we support increasing aid for needs-based grants. In the fall of 2008, the South Carolina Higher Education Study Committee issued a report which stated that "our financial aid portfolio is not balanced between need and merit, with the result that many students from poor families cannot afford to attend. Yet it is precisely from these families that much of South Carolina's increased participation must come." Unfortunately, we believe that our higher education system will remain unaffordable and inefficient if South Carolina's 33 public colleges and universities continue to operate independently without the guidance of a statewide plan, which is why we continue to support the creation of a Board of Regents to develop a coordinated higher education system.

Our mission for higher education is simple: to provide a quality education at an affordable price for the citizens in our state. The result will be greater accessibility for more students in our state who want an opportunity to achieve a higher quality of life.

In addition, our citizens enjoy a variety of cultural resources through our state's historic sites, arts agencies, and museums. Our state is fortunate to have rich cultural opportunities, and we believe in the notion of maximizing private and non-profit resources to enhance our many wonderful community arts and cultural programs.

Administration's Goals for Improving Our Higher Education System and Cultural Resources are to:

- ✓ Provide for greater access and affordability of our Higher Education system.
- ✓ Provide for employability and quality of life opportunities for graduates.
- ✓ Provide for an efficient and effective statewide Higher Education system by creating a Board of Regents.
- ✓ Provide for a greater level of South Carolina-based, derived cultural opportunities.

Developing Our Purchasing Priorities

In order to develop our purchasing priorities, we first looked at major indicators that help determine whether state government is currently reaching its goal of improving our higher education system and cultural resources. While South Carolina is making progress, there are many areas that need improvement. This section identifies the measures that help explain whether our state is or is not achieving our goal.

Where We Are Succeeding

There are many reasons for South Carolinians to be proud of our higher education system. Our technical college system is internationally recognized for its programs that advance workforce development, and our universities have strong reputations for the productivity and quality of their services. Here are a few highlights from the past year:

- A few of our colleges received national recognition for the value of their programs through *U.S. News and World Report* rankings.
- The University of South Carolina-Upstate is in its second year of offering the Scholars Academy, a competitive tuition-free program that provides on-site dual enrollment courses for academically advanced high school students from participating school districts in Spartanburg County.
- Winthrop and Lander Universities have increased safety measures by alerting students of urgent news via cell phone text messages – a precaution that possibly could have saved lives during the Virginia Tech shootings in 2007.

Additionally, enrollment in South Carolina's higher education system is increasing. In the teaching and research universities, there are 7,700 more students enrolled now than in 1998 – a 17.3 percent increase. As a result, the number of degrees awarded has steadily risen at all levels of higher education. Over the last decade, we have experienced a 24.1 percent increase in the total number of degrees awarded by our colleges, universities, and technical colleges. Additionally, minority enrollment went up nearly four percent between 2006 and 2007. Our technical college system saw a 5.2 percent increase in enrollment during the 2008-09 year, but the cause may be two-fold: first, more South Carolinians are realizing the value of obtaining a postsecondary degree to increase employability; and second, technical college enrollment has historically increased during economic downturns. The latter reason likely explains the enrollment increase for the 2008-09 school year, according to officials at the State Technical College System, which means it is crucial that we make higher education accessible and affordable to our citizens.

Opportunities for Improvement

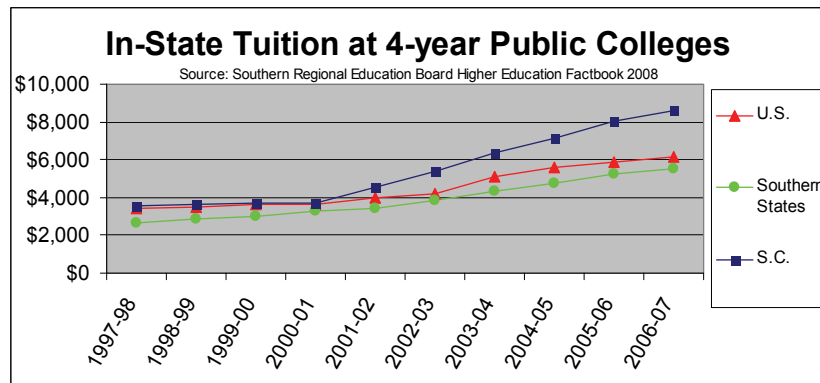
To achieve our goals of preparing the workforce for the global economy and creating economic development opportunities, our institutions of higher education must keep up with workforce needs. This administration has focused on attracting higher-paying, knowledge-based jobs. In order to be more successful at attracting businesses to our state, we need well-prepared graduates at varying

degrees of education levels. There are four primary levels of preparedness: high school graduation, two-year degree, four-year degree, and graduate degree completion. If our state is going to be more competitive, we must increase the number of skilled workers currently available in the workforce. Increasing the number of skilled workers means that more citizens need access to our higher education system. Unfortunately, rising tuition costs are making college less accessible for many people in our state.

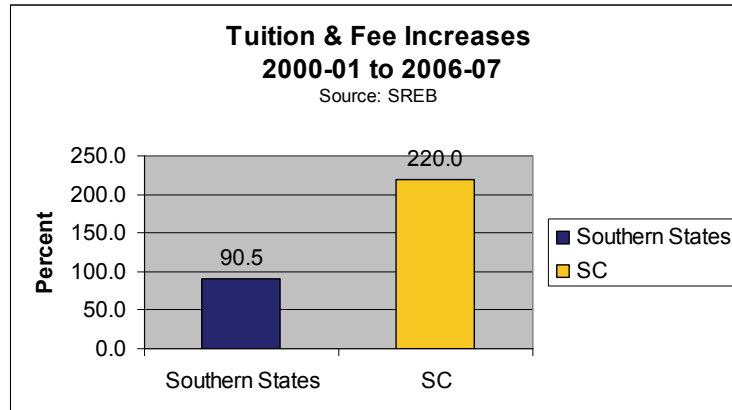
Rising Costs of Higher Education

In 2007, the General Assembly authorized a Higher Education Study Committee which released a report in September 2008 outlining four goals to ensure our state's competitiveness in the knowledge economy. The committee's first goal is to make South Carolina one of the most educated states, and making college affordable is one way to achieve this goal. The committee found that college affordability is shutting out many low-income families who would benefit from postsecondary education.

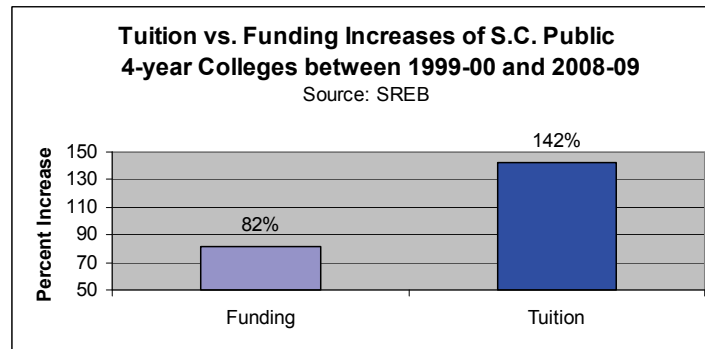
Offering a first-class, postsecondary program is useless if our citizens cannot afford to attend school. Nearly double-digit percentage hikes in tuition in recent years are putting higher education out of reach for many in our state. According to The College Board, the current national average of in-state tuition and fees at public four-year institutions is \$6,585, marking a 6.6 percent increase from the 2007-08 fiscal year. In South Carolina's public four-year colleges, in-state tuition grew by seven percent and averages \$8,965, which is \$2,380 higher than the national average and is almost double the average of other Southeastern states.



As illustrated by the chart below, tuition and fees in South Carolina increased at more than double the rate of average tuition and fees for other southern states in just a five-year period.



Despite the fact that total funding (including state, local, and supplemental) has increased for our state's four-year public colleges by 82 percent, tuition has increased by 142 percent over the past 10 years.



To combat these overwhelming increases, we once again recommend a proviso that would limit tuition and fee increases to the prior year's Higher Education Price Index (HEPI), which was 3.6 percent in FY 2008-09.

The Need for Reform

In FY 1998-99, an in-state student at Winthrop University paid \$4,000 a year in tuition. In today's unstable economy, that same student is being asked to pay more than \$10,000. Dramatic tuition increases like this have taken their toll on the average student's ability to obtain a higher education degree. In fact, the National Center for Public Policy and Higher Education gave South Carolina an "F" for affordability in their "Measuring Up 2008" higher education report. It is important to note that this report is published every two years, and this is the third consecutive report in which South Carolina has received the lowest possible grade regarding college affordability. Even after receiving aid, poor and working-class families devote 34 percent of their annual family income to attend public four-year colleges, according to the report.

Additionally, tuition comprised only 35 percent of the state's higher education budget for public 4-year colleges just eight years ago. According to data from the Southern Regional Education Board, at least 66 percent of our higher education budget is now derived from tuition and fees, which is imposing an ever-increasing burden on students. Although some would attribute our tuition increases to reductions in state funding over the past two fiscal years, our state devotes 18.3 percent of the total state budget to higher education. This administration believes that we are spending enough on postsecondary education in our state, and we should be questioning the manner in which these dollars are being allocated.

With 33 public colleges and universities operating at more than 50 different campus locations, our state maintains too many postsecondary institutions with overlapping programs. Because the Commission on Higher Education has little oversight authority, the political process has created too many schools that operate with too few students. While this growth occurred with the intent of making higher education *more* accessible to everyone in our state, the unintended consequence is that higher tuition is needed to sustain our inefficient system of underutilized campuses, making higher education *less* accessible to many in our state. At a time when all state agencies weathered harsh budget cuts during FY 2008-09 and as economists project a grim economic outlook for FY 2009-10, it is critical that now, more than ever, we scale down the number of higher education facilities in this state.

Purchasing Priorities

We developed our purchasing plan by prioritizing activities using proven or promising strategies that achieve the best results for our goal. The key strategies we identified are as follows:

Provide for an efficient and effective statewide higher education system by creating a Board of Regents. The current structure of our higher education system includes 17 public universities and 16 technical colleges, each independent in mission and focus, and each controlled by its own governing board of trustees. While each campus is unique and desires to establish its own identity, the absence of a unified plan for higher education has promoted mission creep and duplication. During the past few years, we have seen a few examples illustrating the need for a statewide plan for higher education:

- USC-Sumter circumvented the Commission on Higher Education (CHE) by seeking special authorization to move from two-year to four-year status. The CHE – the coordinating body charged with effectively advocating for the best interests of the state system as a whole – did not approve this action.
- USC-Upstate has entered into an agreement with Greenville Technical College to build a USC-Upstate satellite campus in the Greenville area. This action undermines the purpose of the University Center of Greenville, which is a consortium of colleges in the Greenville area collaborating to offer four-year degrees to area residents.

In both of the above instances, the universities initiated their projects without notifying CHE, either because the universities did not want the Commission's approval or because it was unnecessary to have the Commission's approval. This structural weakness and lack of planning will continue to contribute to rising costs and duplication in the higher education system. Therefore, we propose once again that a statewide plan for higher education in South Carolina be developed by establishing a Board of Regents.

Tennessee and Kansas each have a Board of Regents, and Louisiana has had one for more than 30 years. Georgia's university system has had a Board of Regents since 1931. With this act, public higher education in Georgia was unified under a single governing and management authority, and a board-appointed chancellor serves as chief executive officer of the state's 35 colleges.

In light of our bleak economic outlook, now is the time to make permanent changes that will strengthen our higher education system. We strongly encourage the General Assembly to create a Board of Regents – or to give more regulatory authority to CHE – to oversee South Carolina's 17 public universities. The Board would develop a coordinated higher education system and would supervise all affairs of the constituent institutions. Additionally, we believe it is important that the South Carolina Board of Regents be allowed to set tuition and enrollment levels at the institutions, so we can ensure that college is affordable and accessible for our students.

Ensure access to and affordability of higher education. The current credit crisis has made it more difficult than ever for students to obtain loans for college, which emphasizes why we must ensure that higher education is affordable. We can slow the growth of tuition costs by limiting tuition increases for in-state, undergraduate students to the Higher Education Price Index per academic year, beginning with the 2009 fall semester. We believe an institution can control its own costs by coordinating duplicative programs, and by finding internal cost savings. Finally, we can also limit the growth and mission creep of our 17 public universities by strengthening the Commission on Higher Education – or creating a Board of Regents – and developing a statewide plan for higher education in South Carolina.

Increase the employability of graduates. Earning a degree is certainly a measure of achievement and an indication of a base of knowledge. However, today's economy requires more than just a diploma and a presumed proficiency. Graduates must have life skills, technology training, and communication strengths to go with their academic credentials, and they must be prepared to become productive citizens. Also, from a different perspective, students should be made aware of employment opportunities in critical areas as well as employment opportunities associated with chosen majors. While student choice is a cornerstone of the academic experience, we must be certain that students have a realistic understanding of the workplace and how their academic choices can impact their ultimate ability to support themselves.

Increasing the employability of graduates will play a major role in improving the economic climate of our state. Apprenticeship Carolina is in its second year and apprenticeships have increased by 24 percent, giving technical college students on-the-job training with the prospect of a job offer upon graduation. This program is helping to create a larger pool of qualified workers in the areas of health care, tourism, and advanced manufacturing to name a few. We will continue to support

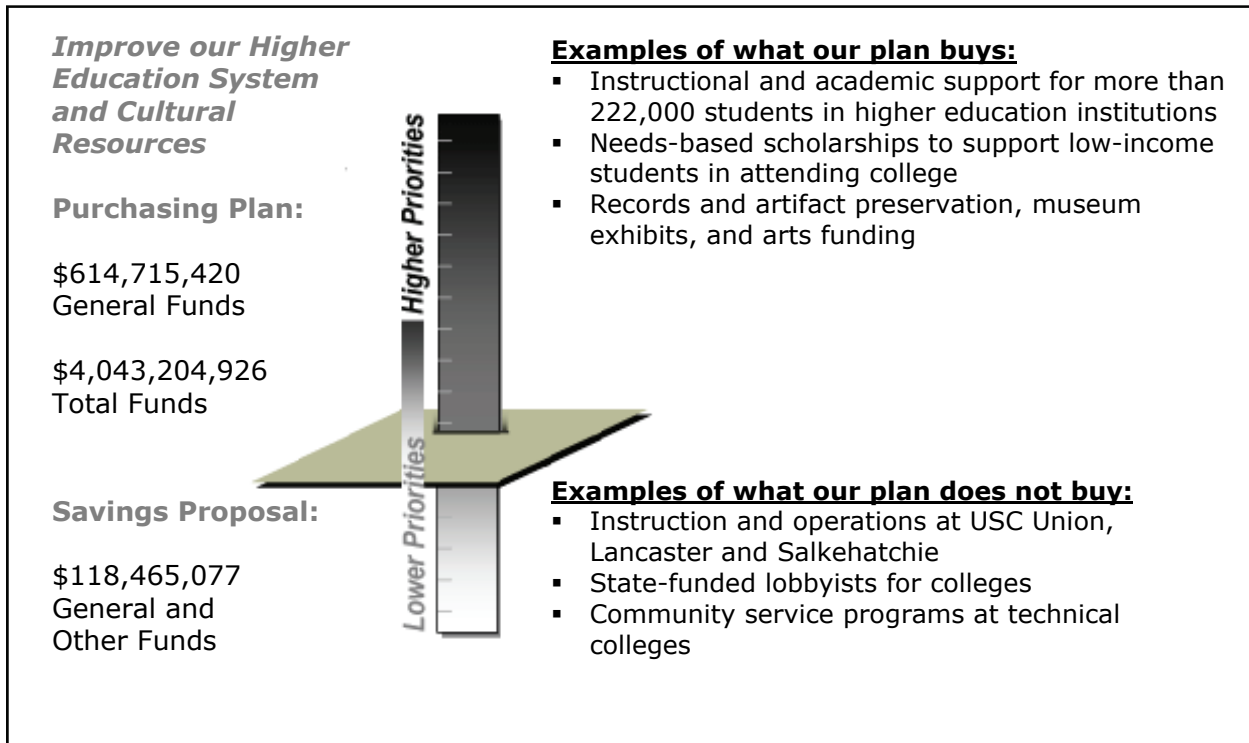
programs that help South Carolina become an attractive option for potential employers and that will attract higher-paying jobs and businesses to our area.

Increase the effectiveness and efficiency of cultural opportunities and agencies through consolidation of duplicative services. There are opportunities for consolidation among arts agencies and their administrative tasks that could prove beneficial. This administration continues to believe in the notion that duplicating services is not the most efficient use of taxpayer money. There are ways for this area of government to combine efforts and save taxpayer dollars – from cultural agencies sharing building space, to the same agencies streamlining administration functions. The State Library, Arts Commission, State Museum, and Department of Archives and History have discussed sharing Human Resource functions, and we would like to see this discussion turn into action.

Increase awareness of available cultural opportunities through a coordinated marketing effort linked to tourism. Our state's historic sites, arts agencies, and museums must be marketed in full cooperation with our tourism regions. The state's cultural resources complement our natural attractions, helping to make South Carolina a prime destination for visitors and potential future college students and residents. We believe careful and constructive marketing would not only draw more attention to these sites, but would also attract capital investment and create jobs.

Governor's Purchasing Plan – Highlights

As we address our state's unprecedented financial problems, it is important to focus on purchasing only those higher education services that deliver the greatest impact on improving K-12 performance. In many cases, we have had to use cost savings methods to simply maintain current funding levels for high priority services. We do not purchase services that, while still considered valuable, have been identified as lower priority. The following table identifies key purchases within our executive budget's total state higher education spending plan as well as examples of what is not purchased. Detailed highlights of our purchasing plan are provided below the table.



Our Plan Buys:

Educational and general funding for our state's 33 two-year and four-year campuses, research universities, and technical colleges. This activity provides the core support for the operation of the higher education system in our state. We only support funding the two-year campuses of USC for the next three fiscal years, as we propose they phase out by 2013. We will once again recommend a proviso that limits tuition and fee increases to the prior year's Higher Education Price Index. We propose funding these activities in the amount of **\$502,643,526** in recurring general funds.

Program coordination and oversight by the Commission on Higher Education. The CHE, while limited in authority, provides reviews of academic and scholarship programs, comprehensive

data collection, and facilities coordination. Until the CHE is given more authority, or until a Board of Regents is established, we propose **maintaining the recurring general fund** in the amount of **\$49,415,109**.

Scholarship programs at all levels. The LIFE, HOPE, and Palmetto Fellows scholarships, along with needs-based grants, help parents and students pay for tuition. Our focus this year will be on increasing funding for needs-based grants, while maintaining funds for other state-supported scholarships. Our state has an imbalance in that we offer more merit-based scholarships than needs-based, and in today's world, an ever-increasing number of students need financial assistance because of their limited family income. Additionally, we propose that the overall scholarship program be re-evaluated to strengthen the qualifications for receipt of scholarship assistance. Far too many freshmen are becoming ineligible for scholarship retention because they were underprepared for the academic challenges of higher education. If the trends in our state continue as they have in recent years, less than 50 percent of the students who received a LIFE scholarship in the fall of 2008 will retain it in the fall of 2009. However, it is our priority to offer a greater level of affordability to higher education students. Therefore, we propose allocating lottery funds appropriated to these scholarship and grant awards as follows:

- **Needs-Based Grants** for total funding of **\$17,817,025**.
- **LIFE Scholarships** for total funding of **\$148,686,444**.
- **Palmetto Fellows Scholarships** for total funding of **\$37,435,700**.

Tuition grants for students attending independent colleges in South Carolina. This investment is returned many times over by using the capacity of these schools instead of additional “bricks and mortar” at state-supported colleges and universities. Since its inception in 1970, the tuition grants program has provided assistance to nearly 290,000 South Carolina students, totaling \$600 million. We propose **funding in the amount of \$22,038,058 in recurring general funds and \$35,915,094 in total funds**.

The Lottery Tuition Assistance Program is designed to aid students bound for two-year technical colleges. Each student is awarded an amount based upon the number of eligible recipients and the amount of available funding each year limited to the cost of tuition. This program assists students by giving them an opportunity to achieve an education at a higher level. We propose **funding in the amount of \$47 million in lottery funds**.

Our Plan Saves By:

Consolidating administrative functions of the South Carolina Technical Colleges. In the first six months of FY 2008-09, the technical colleges each received budget cuts in excess of 21 percent, which is why we believe that now is the time to consolidate administrative functions to realize cost savings. One way to do so is to consolidate the administration of our 16 technical colleges into three regions. We recommend housing the schools' central administrations at Greenville, Midlands, and Trident technical colleges – as they have the largest enrollments – with the merger and proposed cost savings as follows:

Upstate-region (Greenville):

- Piedmont: \$993,561
- Spartanburg: \$983,375
- York: \$1,251,293
- Tri-County: \$2,010,356
- Northeastern: \$707,690

Midlands-region (Midlands):

- Aiken: \$1,049,995
- Orangeburg-Calhoun: \$1,034,237
- Denmark: \$592,355
- Central Carolina: \$993,963

Low-Country-region (Trident):

- Horry-Georgetown: \$1,753,378
- Williamsburg: \$289,967
- Florence-Darlington: \$2,998,466
- Technical College of the Lowcountry: \$1,166,958

Consolidating school administration will produce cost savings by reducing the number of staff members responsible for executive-level administration, financial aid services, Information Technology support, and procurement services. However, we believe it is important for each college to retain its name and its president because each school has an established presence in its surrounding community. After adding 30 percent to the savings above to represent employee benefits, our proposal would **save an estimated \$20.5 million**.

Georgia approved a similar consolidation in October 2008, which merged 13 technical colleges into six, and is estimated to save the state \$3.5 million. It is also important to note that the distance between schools should not discourage consolidation – Valdosta and Central technical colleges in Georgia will consolidate even though they are 70 miles apart.

In lean budget years, we encourage the Technical College System to adopt our proposal, or to create and implement a similar proposal that would realize equal cost savings.

Consolidating administrative functions of the four-year colleges, excluding the three research institutions. Each of South Carolina's higher education institutions faced cuts is excess of 21 percent during FY 2008-09, which is why we believe it is more important now than ever before to streamline resources and consolidate administrative functions. We propose that the administrative functions of Winthrop, The Citadel, Lander, Coastal Carolina, the College of Charleston, Francis Marion and South Carolina State universities be administered in Columbia at the Commission on Higher Education. Consolidating school administration will produce cost savings by reducing the number of staff members responsible for executive-level administration, financial aid services, Information Technology support, and procurement services. However, as with our technical college proposal, we believe it is important for each college to retain its name and its

president because each school has an established presence in its surrounding community. Our proposal would **save an estimated \$11.5 million**.

In estimating cost savings for a consolidation of administrative functions with the four-year universities, we reduced each college's total amount of administrative funding by 15 percent. Reducing administrative funding by this amount would help realize similar savings calculated from technical colleges that have similar enrollment to the four-year colleges. For example, Spartanburg Community College serves just over 4,440 students, while South Carolina State University serves just under this amount. We estimated savings at Spartanburg to be \$983,375, and we applied a 15 percent cut in administrative costs to South Carolina State to realize a total of \$841,069 in savings. The other proposed college savings are as follows:

Citadel	\$1,340,775
Coastal Carolina	\$2,060,558
College of Charleston	\$2,469,273
Francis Marion	\$750,431
Lander	\$504,437
South Carolina State	\$841,069
Winthrop	\$894,449

After totaling the figures above – which represent salaries – we then added an additional 30 percent which represents employee benefits. This brings our **estimated total savings to \$11,519,290**.

We recommend that Clemson and the Medical University of South Carolina retain executive-level administration at their respective universities, as they are among our state's three research institutions. Additionally, we recommend that our third research institution – the University of South Carolina at Columbia – perform all executive-level administrative functions for the entire USC system, which is currently not being done.

Phasing out the USC branches of Union, Lancaster, and Salkehatchie over a two-year period. In a December 9, 2008, newspaper article, University of South Carolina President Harry Pastides said that closing regional campuses of USC may be considered in order to absorb deep budget cuts. We propose phasing out these three USC campuses over a two-year period, as we believe that students currently attending the underutilized two-year campuses could access existing larger campuses in nearby communities. Enrollment at some of these two-year colleges is not increasing at the rate of other nearby colleges and universities. For example, USC-Salkehatchie saw only 2.9 percent student growth between 2006 and 2007. Located less than 25 miles away from the Allendale campus of USC-Salkehatchie is Denmark Technical College, which has seen enrollment increase by 14.1 percent in a year. In the Upstate, USC-Union served fewer than 400 students in 2007 and in 2008. It is located within 25 miles of USC-Upstate and Spartanburg Community College. Additionally, USC-Lancaster is located within 30 miles of Winthrop University, two regional campuses of York Technical College, and the Pageland campus of Northeastern Technical College. First-year **savings for this phase out are \$2,371,657**, which we propose using to fund

needs-based scholarships to provide assistance to students who otherwise may not be able to afford postsecondary education.

Cutting state funding for college lobbyists. At a time when all state agencies are facing extreme budget cuts, we do not believe it is essential that state funding continue to be spent on university lobbyists. For example, Clemson has three full-time lobbyists and one part-time lobbyist and has leased office space in Columbia for these staff members. If public colleges choose to support lobbyists, then they should do so with foundation or other funds, but not on the taxpayers' dime. We estimate the cost savings will amount to **\$1,589,706** in general funds.

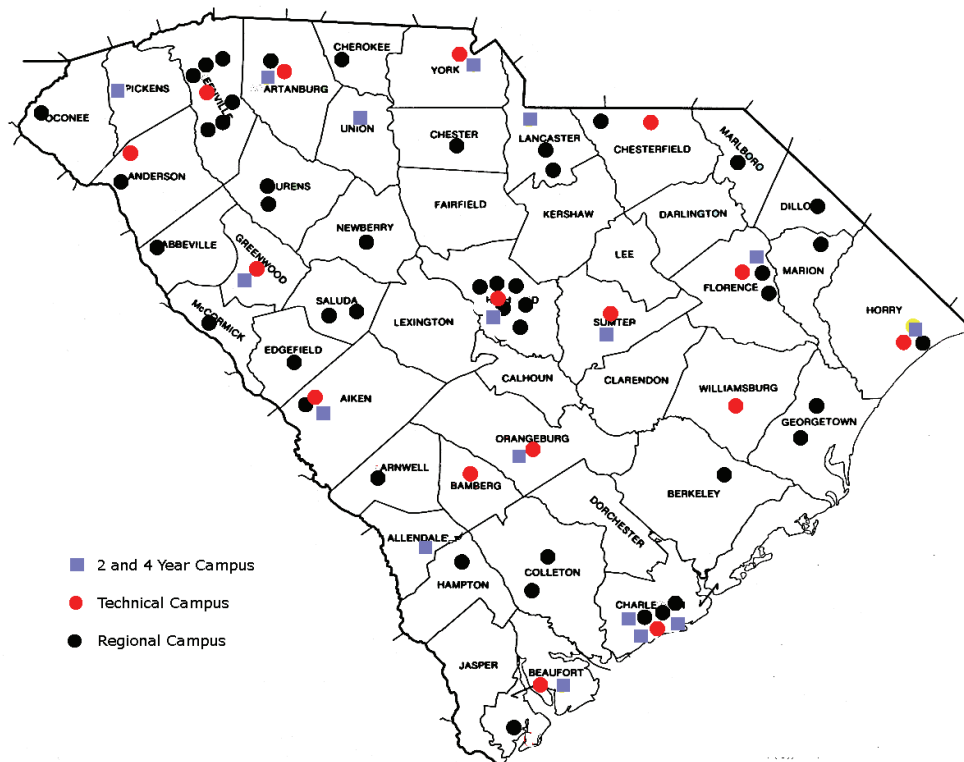
Consolidating the Cultural and Arts Agencies. By moving the Arts Commission into the State Museum, we project **savings of \$202,893** in recurring general funds by reducing space requirements, systems duplication, and equipment.

Terminating the lease of the Tuition Grants facility. Based on the recent cuts to the Tuition Grants Commission, we do not believe that the agency has sufficient funds to meet the obligations of its current lease, which should allow the Commission to cancel the terms of its current lease without penalty with the approval of the Budget and Control Board. There are only three employees that work with Tuition Grants, and we believe they could effectively carry out their mission by sharing space with another state agency. Tuition Grants officials sought space inside the Commission on Higher Education in 2000, but CHE at that time said there was no available space. Therefore, Tuition Grants employees are locked into a contract at their location off of Farrow Road until 2012. We think it is excessive and unnecessary for the state to pay operations, leasing, and maintenance costs on a building that only serves three people who could easily share space with another state agency like the State Department of Education, as they currently have 93 unfilled positions and may have extra office space. Cost savings from this consolidation will amount to **\$37,469**.

Consolidating the Institute for Archeology and Anthropology currently residing at USC-Columbia into the Department of Archives and History (DAH). This function could be easily absorbed and housed at DAH and is consistent with their overall mission of cultural preservation. DAH has adequate physical space available to incorporate this function, and it fits with DAH's defined mission. Most of our neighboring states (Alabama, Virginia, North Carolina, Mississippi, and Louisiana) house their Archeology programs at their equivalent of our Department of Archives and History. **Annual savings** will amount to **\$496,812**.

Facilities and Maintenance Cluster Initiative. Collaborating maintenance and facility operations will yield significant savings to the state without weakening the quality of the participating institutions. As indicated by the map below, many of our state's four-year institutions are located within close proximity to another four-year institution or a technical college, yet these institutions have their own independent facilities and maintenance entity. For example, in Charleston, MUSC, The Citadel, and the College of Charleston are all located within five miles of one another, yet all three have separate facilities and maintenance support staff. We believe that with three separate entities in such close proximity providing similar services, there are opportunities to combine facilities and maintenance operations and reduce costs. These types of opportunities exist

throughout our higher education system, and we encourage institutions within a 25-mile radius of one another to reduce the costs associated with their facilities and maintenance activities. We are encouraged to hear that steps are being taken in this direction, as Internet Technology directors from the public and private colleges are currently discussing ways to share IT solutions, resources, and find cost savings. We will closely monitor the formation of this collaboration. By reducing costs to the participating universities, we will prevent significant tuition increases for our state's students and families. This initiative will provide **\$7,635,592** of general fund **savings** based on the centralization of facilities and maintenance management that will afford a reduction in overhead.



Making Tough Choices:

Given the state's limited resources, we had to make some difficult choices regarding which activities to fund. While the activities listed below have merit, we did not think their anticipated outcomes would be as effective when comparing them with other activities in achieving our goal. The following activities reflect some of those difficult choices:

Community Service Programs through the State Technical College System. While community service programs are a noble effort to cultivate responsible citizenship, we are faced with being able to fund only those activities which are essential to the colleges' mission. This program offers non-credit courses to community members at all 16 technical colleges. Participants pay for the courses, which are day-long seminars on art, history, homeland security, or on topics related to the community in which they live. Funds are used to pay a portion of salary for instructors, but the

program generates three million dollars annually in user fees. Therefore, we recommend that this program be self-sustained through user fees. This will result in a **savings of \$752,752** in general funds.

University Center of Greenville is a consortium of public and private colleges and universities offering undergraduate and graduate degree programs to the citizens of the Upstate. This type of collaboration is what we support, particularly in tough financial times when our current higher education system is full of duplicative programs. However, with seven institutions participating in the Center – including Clemson, Furman, MUSC, USC-Columbia, USC-Upstate, South Carolina State University, and Lander – we believe the participating colleges should be able to cover the operations costs of the University Center, or they should seek alternative sources of funding other than general funds. This will result in **savings of \$301,886** in general funds.

National History Day in South Carolina. This is an educational program that encourages students in grades four through 12 to study, research, and develop topics related to history, and to expand their knowledge through exhibits, performances, documentaries, or historical papers. While this program is valuable in educating students about history, it reaches less than two percent of students (less than 9,000) statewide. Furthermore, we believe that students could still continue their research projects on history with the aid of streaming history videos through ETV and by forming partnerships with the local communities to study historic sites within the county where they attend school. Reducing state funding for this program will result in **savings of \$56,829** in general funds.

Please see the Appendices for a complete listing of the Governor's Purchase Plan for this goal area and for a detailed listing of what our plan saves and what our plan does not buy.

Improve the Conditions for
Economic Growth

Improve the Conditions for Economic Growth

Since the beginning of our administration, we have been working toward making South Carolina as competitive as possible for attracting large capital investment and jobs, improving the business climate, and offering reforms that will keep South Carolina moving forward in this constantly evolving global economy.

These goals continue to be a high priority for our administration. Our commitment to economic development is reflected by our strong support of the economic development efforts of our Department of Commerce. We have made significant strides in improving the department's ability to attract large-scale capital investment projects. This year alone, we have secured multi-million dollar investments and recruited more jobs by bringing in companies like Google, Starbucks, Adidas, Monster.com, Heinz and URS Corporation, and have also facilitated increased expansions to existing businesses in the Palmetto State.

Administration's Goals for **Improving the Conditions for Economic Growth**:

- ✓ Capital investment growth.
- ✓ Small business community growth.
- ✓ Provide jobs for existing workforce.
- ✓ Increase personal income.

The global economy continues to evolve on a daily basis, creating new markets and new ways of doing business. As we have emphasized in the past, South Carolina no longer competes just regionally or nationally, but globally with countries like China and India which continue to train their workforces and develop their abilities to compete across a diversity of industries. Given this ever-changing global economy and the current global financial crisis, we believe it is imperative, now more than ever, that we do what it takes to enhance South Carolina's competitive position.

It is crucial that we focus on providing the Department of Commerce with the necessary tools to compete with other states and nations when companies look to grow their operations or expand existing ones. Our administration has been consistent in its commitment to create a friendlier business climate in South Carolina.

Developing Our Purchasing Priorities

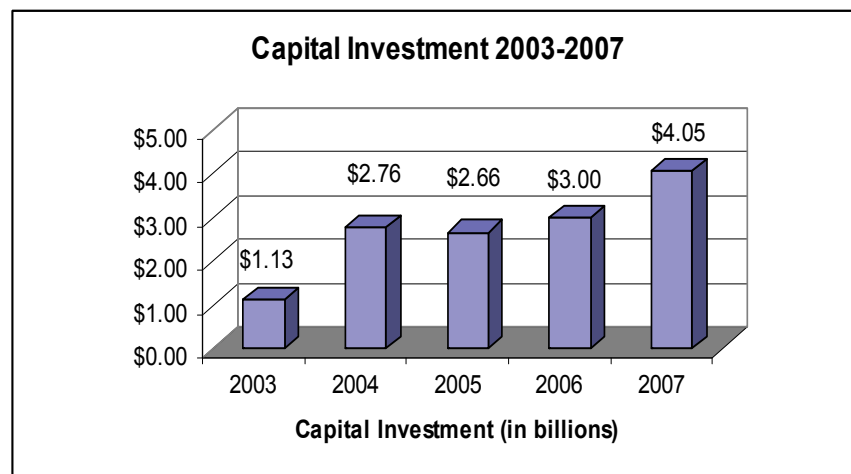
To develop our purchasing priorities, we first looked at the major indicators of success to determine whether state government is currently reaching its goal to improve the conditions for economic growth. We have found that South Carolina is making significant progress; however, there are areas that need improvement. This section identifies the measures that help explain whether our state is achieving our goals.

Where We Are Succeeding

During the 2008 legislative session, we worked with the General Assembly on a number of pro-jobs and pro-growth initiatives, including the Small Business Healthcare Act, to continue improving South Carolina's overall business climate. Ninety-seven percent of businesses in South Carolina are small businesses, and the Small Business Healthcare Act gives them another tool to remain competitive in today's global economy by enabling employers to provide insurance to their employees at a lower cost. By supporting this and other reforms, we have sent a clear signal to all prospective job creators that we are not only open for business, but are also working to make South Carolina the preferred place to do business.

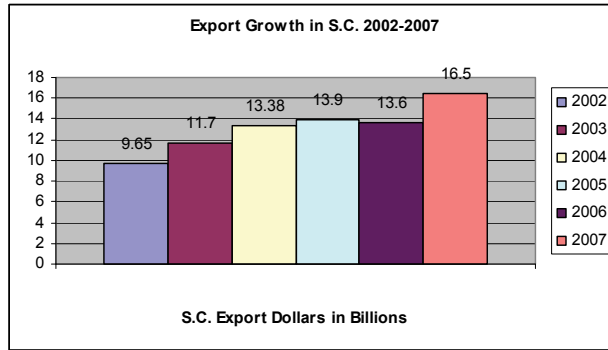
Capital Investment

In 2007, South Carolina continued to experience rapid growth in the amount of capital investment and the number of new jobs created. Through the outstanding efforts of the Department of Commerce, 103 new firms and 76 existing firms invested over \$4 billion in South Carolina. This investment represents a 35 percent growth over 2006 and encompasses more than 15,000 new jobs in the Palmetto State. Since 2003, South Carolina's capital investment has grown over 250 percent from \$1.13 billion to \$4.05 billion in 2007. The department has also recruited more foreign companies from countries such as Germany, France, Switzerland, Canada and Sweden. Investments by foreign companies account for 50.9 percent of all capital investment and 30.8 percent of all new jobs.



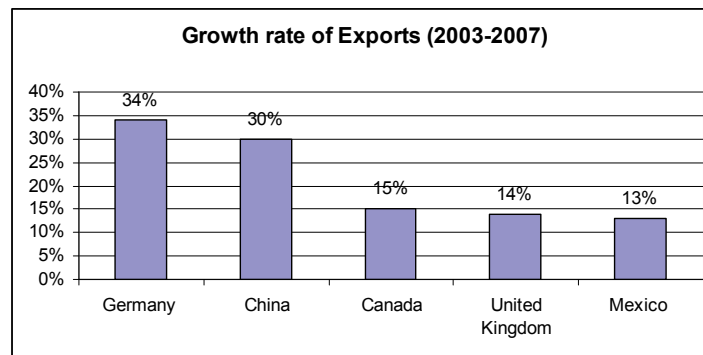
Export Growth

South Carolina has seen significant growth in its export markets during this administration. In 2007 export growth increased by 21.6 percent to a record level of \$16.5 billion, which was substantially higher than the 12.1 percent growth rate of the United States and the 14.7 percent export growth rate of the Southeast.



As the state's exports grow, so do our opportunities. About 9 percent of South Carolina's total private sector manufacturing employment is supported by exports. In 2007, South Carolina exported goods to 198 countries with traditional trading partners like Canada and the United Kingdom, while also experiencing significant increases to quickly growing and emerging markets in China and Vietnam. Also, South Carolina is the second largest exporting state or U.S. territory to Germany. South

Carolina's export business has grown 147 percent from 1996 to 2007, ranking it 19th among the 50 states and all U.S. territories. Continuing to make export business growth and development a priority for the state will result in South Carolina becoming even more diverse in the global marketplace.



Opportunities for Improvement

This administration continues to believe that job creation and business growth are predicated upon reforms that can provide a broader array of opportunity for all South Carolinians. With a reduction in the small business income tax, comprehensive tort reform, workers' compensation reform, and the small business healthcare reform, we believe some important strides have been made that give residents of our state more job opportunities.

With the influx of people coming to South Carolina, our labor force continues to grow and impact our state's employment. According to the U.S. Bureau of Labor Statistics (BLS), our labor force and employment growth are among the best in the nation, and South Carolina has over 145,000 more people employed now than just five years ago. With a continually growing labor force, it is incumbent upon us to work even harder to spur economic development and the creation of jobs in South Carolina.

State-By-State Comparison, Labor Figures, Jan. 2003 to Aug. 2008

(Source: U.S. Bureau of Labor Statistics, seasonally-adjusted figures as of 9/26/08)

Labor Force				Employment			
Rank	State	Total Growth	%	Rank	State	Total Growth	%
1	Nevada	261,371	22.86%	1	Nevada	224,644	20.78%
2	Utah	185,610	15.49%	2	Utah	205,991	18.28%
3	Arizona	397,148	14.69%	3	Arizona	381,677	14.99%
4	Florida	1,148,056	14.05%	4	Florida	987,833	12.78%
5	Georgia	550,482	12.62%	5	Washington	359,658	12.38%
6	Colorado	274,905	11.13%	6	Colorado	273,376	11.76%
7	Washington	342,084	10.92%	7	Idaho	70,982	10.93%
8	Idaho	68,131	9.92%	8	Georgia	451,168	10.87%
9	Virginia	369,316	9.78%	9	New Mexico	81,983	9.86%
10	S. Carolina	184,440	9.30%	9	Texas	1,001,737	9.86%
11	New Mexico	74,947	8.49%	11	Virginia	333,226	9.20%
12	Wyoming	22,038	8.15%	12	Arkansas	106,401	8.86%
13	Alaska	27,072	8.10%	13	Alaska	27,317	8.84%
14	Hawaii	49,603	8.07%	14	Wyoming	22,453	8.69%
15	North Carolina	340,126	8.05%	15	S. Carolina	145,191	7.82%
16	Arkansas	102,157	8.04%	16	Hawaii	44,381	7.50%
17	Texas	862,663	7.93%	17	North Carolina	296,309	7.49%
18	Montana	35,139	7.48%	18	Montana	33,532	7.47%
19	North Dakota	24,499	7.04%	19	Oregon	122,563	7.19%
20	Delaware	27,947	6.67%	19	North Dakota	24,090	7.19%
21	Illinois	404,958	6.41%	21	South Dakota	24,155	5.94%
22	California	1,034,067	5.95%	22	Delaware	23,323	5.80%
23	Oregon	106,958	5.79%	23	Illinois	334,545	5.67%
24	South Dakota	24,294	5.77%	24	Maryland	146,472	5.36%
25	Maryland	159,597	5.59%	25	New Hampshire	35,386	5.23%
26	Connecticut	98,229	5.48%	26	California	810,210	5.01%
27	Tennessee	143,583	4.97%	27	Oklahoma	76,738	4.80%
28	New Hampshire	34,030	4.80%	28	Kansas	64,035	4.71%
29	Maine	29,593	4.34%	29	Iowa	56,920	4.34%
30	Kansas	59,376	4.14%	30	Connecticut	72,264	4.26%
31	Kentucky	79,994	4.08%	31	Alabama	80,502	4.05%
31	Pennsylvania	250,948	4.08%	32	Pennsylvania	232,457	4.01%
33	Iowa	65,242	4.03%	33	New Jersey	155,566	3.79%
34	New Jersey	164,947	3.78%	34	New York	326,914	3.75%
35	Alabama	78,012	3.72%	35	Tennessee	97,518	3.56%
36	Oklahoma	55,614	3.29%	36	West Virginia	26,350	3.54%
37	New York	284,133	3.05%	37	Maine	22,861	3.52%
38	Indiana	91,471	2.90%	38	Nebraska	30,517	3.28%
39	Nebraska	27,901	2.88%	39	Kentucky	59,819	3.25%
40	Ohio	149,553	2.56%	40	Louisiana	53,870	2.84%
41	Minnesota	56,185	1.95%	41	Wisconsin	60,316	2.11%
42	Mississippi	22,092	1.69%	42	Indiana	41,998	1.40%
43	Louisiana	32,440	1.61%	43	Ohio	54,936	1.00%
44	West Virginia	12,457	1.57%	44	Vermont	3,225	0.98%
45	Wisconsin	45,234	1.49%	45	Mississippi	7,952	0.65%
46	Vermont	4,619	1.33%	46	Minnesota	10,664	0.39%
47	Missouri	29,753	1.00%	47	Massachusetts	11,857	0.37%
48	Rhode Island	5,214	0.92%	48	Missouri	-9,836	-0.35%
49	Massachusetts	-3,411	-0.10%	49	Rhode Island	-13,587	-2.54%
50	Michigan	-77,806	-1.55%	50	Michigan	-181,367	-3.87%

Improving Economic Soil Conditions

This administration has mentioned numerous times that to increase South Carolina's global competitiveness, the playing field must be as level as possible. Rural South Carolina is still lagging behind in its access to high-speed internet connections. While the United States as a whole has over 75 million total broadband subscribers on a per capita basis, the United States is ranked 24th globally in broadband penetration. Countries like South Korea and the majority of the European Union countries have more broadband penetration per capita than this country. A study by the Freedom Works Foundation shows that widespread broadband deployment would add nearly 13,000 jobs to South Carolina and increase the Gross State Product by \$4.55 billion. For South Carolina to be truly competitive, all of its citizens must have access to affordable high-speed internet.

Previous steps to provide more affordable internet access have been taken by this administration – from signing legislation that deregulates broadband services to allowing more cable companies providing internet services into South Carolina. To that end, we are pleased that the South Carolina Educational Broadband Commission was put together to make this proposal a reality.

While we have made progress in improving some economic soil conditions, South Carolinians are still burdened by the highest effective income tax rate in the Southeast. As a result, South Carolina is in danger of falling behind in global competition for jobs and capital investment. In the Emphasize Economic Development section of this budget, we have proposed offering an optional flat tax that will not only cut much of the red tape out of the current tax code, which includes confusing paperwork for exemptions and deductions, but which will also attract economic and human capital to the state. According to a recent study from the Atlanta Federal Reserve Board, “Relative marginal tax rates have a statistically significant negative relationship with relative state growth.” Put another way, the lower the tax rate the greater the state’s economic growth.

We have also expressed concerns that our tax code has far too many incentives carved out for only one area of the state or for only one business that may come to our state. The Department of Commerce reviewed our incentive system and reported that “some of the current incentives contained within the tax code have become obsolete or have been amended to the point that they no longer serve their original purposes.” We believe it is time to stop singling out counties or businesses and take a look at our tax code from a much broader perspective. Accordingly, this year we propose eliminating some of the special incentives in our tax code and replacing them with a complete elimination of our five percent corporate income tax. Phasing out the corporate income tax over 10 years would make South Carolina only the fifth state to do so – along with Nevada, South Dakota, Washington and Wyoming. South Carolina’s next closest competitor in the Southeast would be Alabama, with a 4.23 percent corporate tax. According to the Tax Foundation, the net effect of full implementation of our tax plan will move us from being the 25th best business climate in the nation to being the sixth best business climate in the nation.

Small businesses are still burdened by high costs associated with inflated awards in the workers’ compensation system. While some progress has been made due to the enactment of comprehensive workers’ compensation reform in 2007, the business community still needs the protection of objective standards for determining awards.

Finally, we remain committed to reducing the burden that frivolous lawsuits have on businesses in South Carolina. While the tort reform legislation enacted in 2005 has helped reduce the costs associated with litigation to businesses, there is still much work to be done. In the *2008 State Liability Systems Ranking Study* conducted for the U.S. Chamber Institute for Legal Reform, South Carolina ranked 43rd worst tort system in America – the worst ranking that the state has ever received. For South Carolina to remain competitive in a global economy, we need to continue to reduce these unnecessary costs incurred by businesses. We encourage the General Assembly to address tort reform in this legislative session.

Purchasing Priorities

Our five major funding priorities are those that will best achieve our goal of improving the conditions for economic growth, and those are:

IMPROVE THE CONDITIONS FOR ECONOMIC GROWTH

Provide for the growth and sustainability of all communities. We continue to approach economic and competitive challenges in South Carolina on a holistic level rather than a piecemeal level. In doing so, we increase the potential for all South Carolinians to benefit from this administration's economic development efforts. Allowing consistent and continued success throughout South Carolina remains a vital step toward global competitiveness. By effectively spreading economic development opportunities across the state and working to improve business soil conditions statewide, we stand a far better chance of growing our economy overall than by focusing on certain areas of the state as priority.

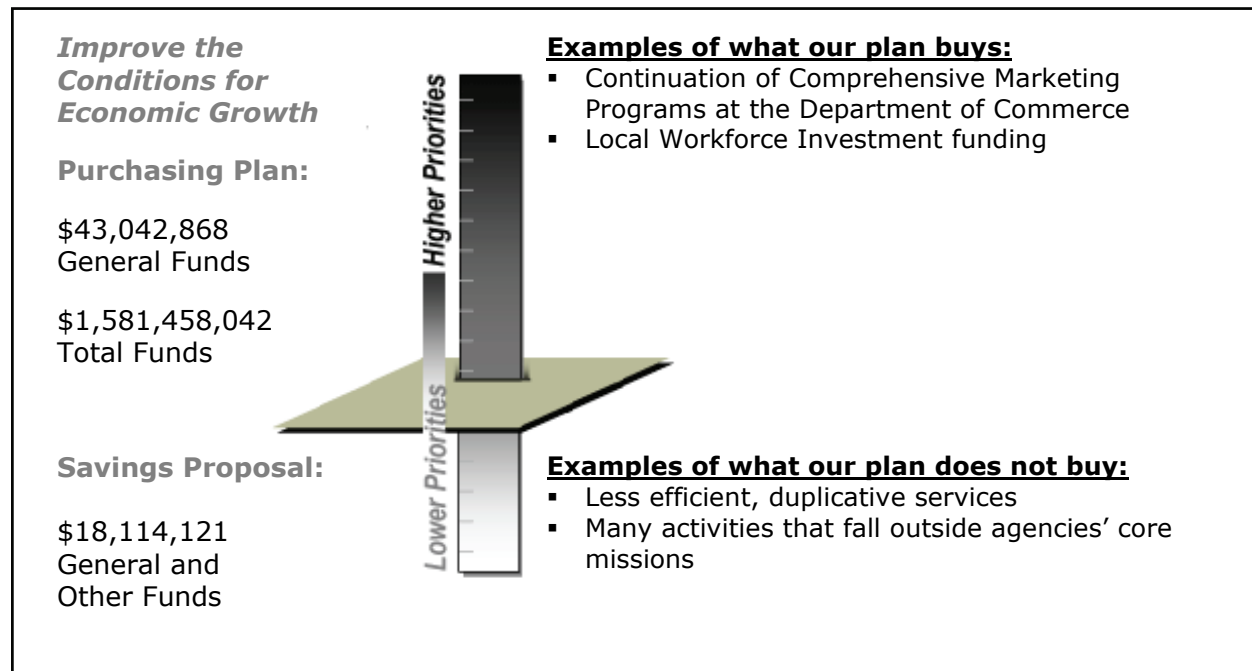
Provide for more effective and broad-based incentives and grants programs. The Department of Commerce has done a good job providing South Carolina with important information on how best to compete by providing the best mix of incentives and grants for our state's economic development efforts. By leveling the playing field for business and not favoring one specific business or industry over another, we give South Carolina the benefit of attracting capital investment and jobs in a business climate that is uniform.

Provide a more unified and focused effort in marketing our state's assets. South Carolina will maintain its reputation as a business-friendly environment by continuing to promote its strengths while working to minimize or eliminate its weaknesses. Marketing dollars spent on promoting the positive aspects of living and working in the Palmetto State provide tangible benefits – every dollar properly invested in marketing returns more than \$20 in direct tourism spending to the economy. A continued emphasis on the look and feel of South Carolina as a superior tourist destination and as a business-friendly state will serve the dual purposes of bringing in tourism and capital investment projects, both of which create jobs for South Carolinians.

Provide resources and infrastructure for a more skilled and prepared workforce. South Carolina is consistently recognized for its ability to prepare its workforce for the highly-skilled jobs of the 21st century. Through the Center for Accelerated Technology Training and its programs which are designed to work with businesses on providing labor infrastructure needs, South Carolina continues to provide top-level training for the jobs created from emerging technologies in a global economy. To continue our economic development efforts in workforce development, we remain focused on streamlining the allocation of workforce development dollars through the Department of Commerce's Workforce Development Division.

Governor's Purchasing Plan – Highlights

As we address our state's unprecedented financial problems, it is important to focus on purchasing only those services that deliver the greatest impact on improving the conditions for economic growth. In many cases, we have had to use cost savings methods to simply maintain current funding levels for high priority services. We do not purchase services that, while still considered valuable, have been identified as lower priority. The following table identifies key purchases within our executive budget's total state economic development spending plan as well as examples of what is not purchased. Detailed highlights of our purchasing plan are provided below the table.



Our Plan Buys:

Making Interest Payment on Federal Loan for Unemployment Compensation Benefits. In 2008, the Employment Security Commission (ESC) requested two loans amounting to \$161 million dollars to cover a shortfall in the Unemployment Insurance Trust Fund. According to the terms set by the U.S. Department of Labor, if the state does not repay the loan in one year, then the interest begins to accrue increasing the liability to the state by approximately \$5.1 million in FY 2009-10. While we are unable to cover the substantial loan requested for ESC, we believe it makes good sense to set aside funds in this budget to cover the interest. Accordingly, we are setting aside **\$5.1 million in general funds** to pay the interest owed on this federal loan. Some have suggested doubling the tax on every business in the state to cover future shortfalls. According to the Tax Foundation, South Carolina's unemployment tax already ranks 9th worst in the nation. We believe that any attempt to address the loan or future shortfalls must be tied to significant reforms of the ESC, and we are pleased to see a large number of legislators agree and have requested a Legislative Audit Council review of the agency.

Continuation of a Comprehensive Marketing Program at the Department of Commerce.

The Department of Commerce continues to make an impact on the global business community through its presence at trade shows and industry specific events, while also gaining attention through enhanced marketing and public relations efforts within South Carolina and around the world. It is crucial to make the global business community aware of our state's positive business environment in order to compete. We, therefore, propose maintaining **recurring funding of \$1,900,379** to the Department of Commerce for their marketing efforts of South Carolina.

Recurring funding for the Department of Parks, Recreation and Tourism's Media Placement budget.

The tourism industry will always be a major economic driver in the Palmetto State. In 2007 domestic travel expenditures in South Carolina totaled over \$9.7 billion, a 6.5 percent increase from 2006. The idea of continuing to promote South Carolina's tourism industry to the world has enormous return on investment potential. PRT's "Product Development" and "Destination Specific" programs focus on enhancing specific areas of our state's tourism industry that have the most potential for new streams of revenue. We recommend the continued allocation of funding to not only foster the growth of these new programs, but also to aid South Carolina's efforts to attract tourism revenue from all parts of the globe. We propose maintaining recurring funding of **\$7,497,609** for the agency's media placement budget.

Funding for the Center for Accelerated Technology Training. Supplying a well-trained and adaptable workforce is another important element of South Carolina's ability to compete for business opportunities. South Carolina's Center for Accelerated Technology Training program, which is coordinated through our technical college system and the Department of Commerce, is one of the major reasons companies choose South Carolina for their capital investment projects. Because of the success of this program, we propose **maintaining current funding of \$2,035,153** for this workforce training program.

Local Workforce Investment. This initiative will help to meet the employment, training, and labor market needs of businesses, job seekers, and at-risk youth. These federal dollars are spent in coordination with the state's economic development activities to help recruit high-paying jobs. The training programs are in industries and individual companies targeted by the Department of Commerce. **Projected FY 2009-10 federal funding is \$79,599,000.**

Our Plan Saves By:

Transferring the Local Government Infrastructure Grants at the Budget and Control Board to the Department of Commerce.

As lead agency on economic development for the state, the Department of Commerce should be the agency in charge of all funds directed at growing the economy of our urban and rural areas. We have long advocated that one agency appropriating economic development funds is more efficient and effective than multiple agencies doing so. Since taking office, this administration in cooperation with the Department of Commerce has had unmatched success in encouraging growth in the state's rural communities. As an example of this success, in 2007, more than 34 percent of jobs recruited to South Carolina went to rural communities. Further, in their efforts to continue improving workforce readiness in rural South Carolina, the Rural Infrastructure Fund (RIF) helped create Northeastern Technical College Information Technology Laboratory classroom at its Dillon County Community Campus. Looking

at the big picture, in 2005, rural capital investment in our state was \$842 million, up from \$635 million in 2004. We believe there is the ability for more success to occur by moving this program and all associated grant funds to the Department of Commerce. This move would generate **general fund savings of \$151,751.**

Directing gasoline tax revenue to the petroleum inspection and testing program. The Department of Agriculture is charged with inspecting and testing gas pumps for accuracy and suitability for service. The current state law provides that, “For the purposes of providing funds for inspecting, testing and analyzing petroleum products and for general state purposes, there must be paid to the department a charge of one-fourth cent a gallon...” Currently, the department runs this program with general fund dollars. We propose directing the state amount of funds from the gas tax to run this program because it is statutorily required. This will allow the agency to hire the needed inspectors to ensure this program is managed as expected. This will generate **general fund savings of \$390,606.**

Making Tough Choices:

Given the state’s finite amount of resources, we had to make some difficult choices regarding which activities to fund. While the activities listed below may well have merit, we did not think their anticipated outcome would be as effective as other activities in achieving our goal. The following reflects these difficult choices:

Reducing pass through funding. This administration has always believed that any public-private endeavor should employ an open and objective process so that the most worthy projects receive public investment. An example of these funds is the Regional Promotions pass through at the Department of Parks, Recreation and Tourism, a pass through that the agency recommended should no longer be funded. We believe that in lean budget years, funds appropriated should be directed to accountable, core functions within the agency and not to providing a limited amount of funding to the 11 regional tourism districts throughout the state. We continue to advocate that a process is needed to create a fairer way to fund these projects than with pass through funding. **General fund savings of \$1,375,000.**

Public Service Activities reaching outside of their core mission of agriculture. The administration continues to recognize the valuable role that Clemson's and South Carolina State's PSAs have played in our rural areas over the past several decades. However, we think that the agencies should narrow their focus to more closely concentrate on the core mission of serving our state’s agricultural community. Those non-core activities identified include the Rural Community Leadership Development program at Clemson and the Community Leadership and Economic Development program at South Carolina State. These are examples of programs reaching outside their core mission when the intended goal is duplicative of services provided through the South Carolina Department of Commerce. These activities represent a **general fund savings of \$1,842,858.**

Please see the Appendices for a complete listing of the Governor’s Purchase Plan for this goal area and for a detailed listing of what our plan saves and what our plan does not buy.

Improve the Health and
Protections of Our Children and
Adults

Improve the Health and Protections of Our Children and Adults

Core functions of a fiscally and socially responsible government include helping our citizens maintain or regain their health, protecting vulnerable citizens from abuse, and providing opportunities for people to keep their independence and dignity. When done well, this leads to a better quality of life for our citizens while lowering costs to the taxpayer.

In South Carolina, one out of every three tax dollars is directed toward health care. Historically, however, that significant investment has not led to satisfactory health outcomes in our state. To help South Carolinians get more value for their health care dollar, we brought the benefit of marketplace principles to health care. South Carolinians deserve a health system that encourages cost-effective preventative care and offers a menu of health plans from which to choose for themselves and their families.

Another key ingredient of a high quality of life is the ability to live in a safe and stable environment. Improving the security of vulnerable citizens – reducing child poverty, finding permanent homes for foster children, decreasing the rate of child abuse and neglect, improving the living conditions of our seniors and those with disabilities, and improving rates of self-sufficiency among our low-income citizens – can improve employment rates, educational performance, health status, and quality of life. Against the backdrop of record budget deficits and a deep economic downturn, all of these outcomes can directly benefit our children and vulnerable adults and, therefore, indirectly benefit our taxpayers.

But these efforts will continue to be compromised until South Carolinians get the efficient and accountable service delivery system they deserve and that we have called for each of the past six years. If South Carolina's government were to be recreated today, it is virtually inconceivable to believe anyone would recommend our current health care delivery structure. It is time to implement the kind of effective, efficient, and accountable government structure South Carolina taxpayers deserve.

Administration's Goals for Improving the Health and Protections of Our Children and Adults are to:

- ✓ Increase the number of citizens leading healthy lives.
- ✓ Increase access to health care.
- ✓ Increase self-sufficiency.
- ✓ Increase the number of children living in a safe and stable living environment.
- ✓ Reduce preventable injury, illness and death.
- ✓ Reduce health disparities.
- ✓ Reduce poverty.

Developing Our Purchasing Priorities

During this process, we looked at the major indicators of success to determine whether state government is currently meeting its goal of improving the conditions for the health of our citizens. We have found some modest progress, but there are many areas that need improvement. This section identifies the measures that help explain our state's level of progress in achieving our goal for a healthy citizenry.

Where We Are Succeeding

Reducing preventable injury, illness, or death through screening. One area where we have been successful in screening is in the rate of women receiving mammograms. Mammograms help detect breast cancer in its early stages; thus, it is critical that women have access to them. Although the overall number of women who get mammograms is increasing, many women – particularly those who are uninsured, older, or members of certain racial and ethnic minority groups – do not get mammograms at the same rate. To help in this regard, the first-ever state allocation of \$2 million last year provided an additional 9,000 women with access to life-saving cancer screenings. By lowering the “Best Chance Network” eligibility age from 47 to 40, the program is consistent with the American Cancer Society screening guidelines, allowing more lives to be saved.

Living in a safe, stable environment. The rate of South Carolinians living in a safe and stable environment is a direct indicator of the economic and physical well-being of children and adults.

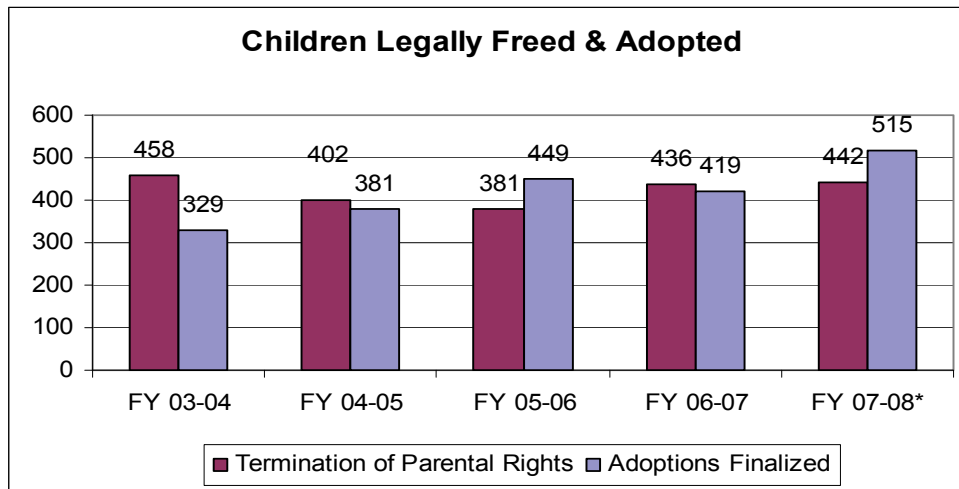
Key measures of this indicator include lower rates of child abuse and neglect. South Carolina is meeting some goals to ensure the safety of our children, adults with disabilities, and senior citizens. According to the most recent Department of Health and Human Services Child Maltreatment Report, South Carolina's child victimization rate is consistently lower than the national rate.

Year	Child Victims	Total State Child Population	Victims Per 1,000 Children (South Carolina Rate)	Victims Per 1,000 Children (National Rate)
2000	11,246	1,009,641	11.1	12.2
2001	11,199	1,018,000	11.0	12.5
2002	10,738	1,016,427	10.6	12.3
2003	11,143	1,019,266	10.9	12.2
2004	9,950	1,023,278	9.7	12.0
2005	10,759	1,030,036	10.4	12.1
2006	10,795	1,039,653	10.4	12.1
U.S. Dept. of Health & Human Services Child Maltreatment Report				

As of July 2008, the percentage of children who are re-abused after the state returns them to the home has decreased from 3.4 percent in 2002 to 2.6 percent. While any abuse is unacceptable, the Department of Social Services' top priority is protecting vulnerable children.

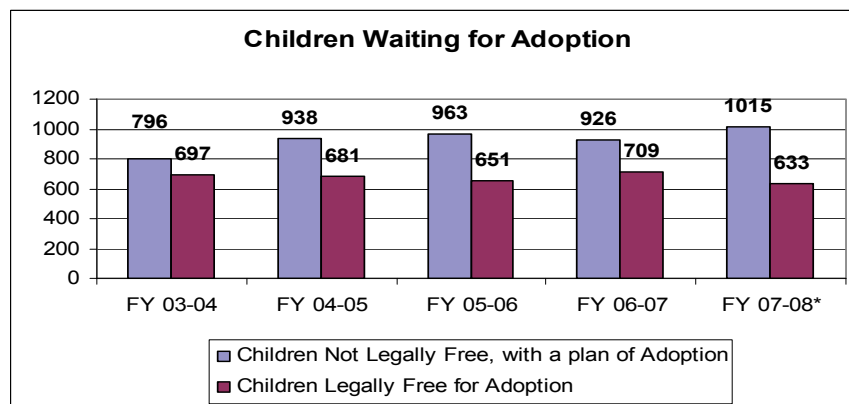
We have also seen some improvement in the area of adoption. In FY 2007-08, 631 children were placed in adoptive homes and 515 children had their adoptions finalized. This is the first time in a

state fiscal year the number of adoptions finalized has exceeded 500. To increase the number of adoptive families available, a recruiter has been added to each of the four regional adoption offices.



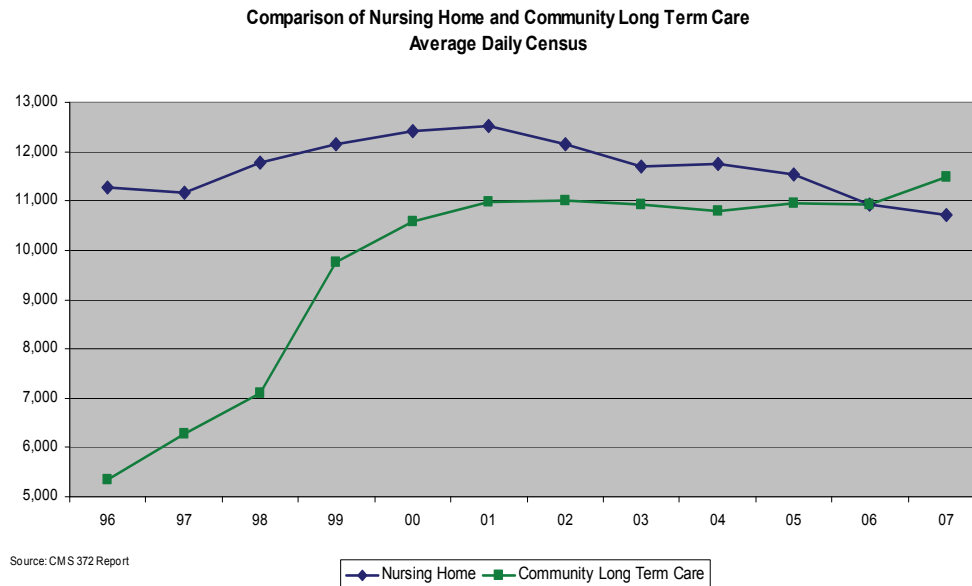
The amount of time it takes for a child to be adopted is at one of its lowest levels in five years.

In FY 2007-08, 19.4 percent of the agency's foster children were adopted within 24 months, which is an improvement from the previous fiscal year but remains well below the 32 percent national standard.



Self-sufficiency rates. Improved rates of self-sufficiency and independence are direct indicators of economic well-being. Key measures of these indicators include the percentage of South Carolinians leaving state assistance (i.e., Temporary Assistance for Needy Families-TANF), the number of seniors and disabled persons able to remain in their own homes, and the unemployment rate. Currently, families are the major providers of long-term care for seniors, providing 80 percent of care at home.

The following chart shows a comparison of nursing home care versus community (family) care. In 2007, we have seen community care surpass nursing home care. By receiving at-home community care, seniors and disabled persons are not only happier, but they help save taxpayer dollars.

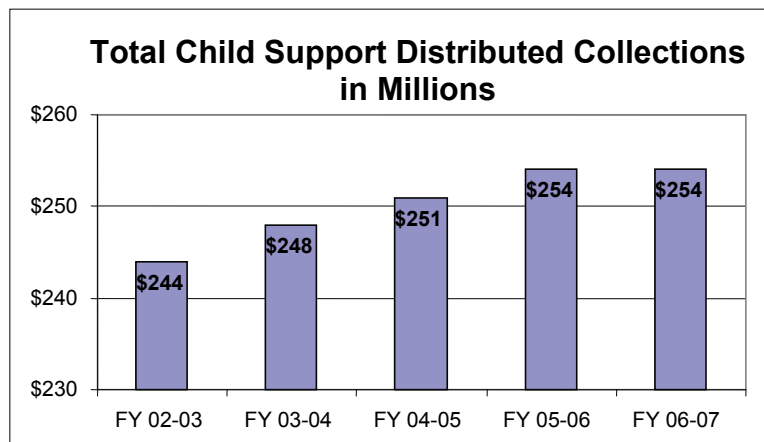


South Carolina is meeting some of its goals of increasing opportunities for self-sufficiency among low-income families and adults with disabilities by providing basic needs. For example, efforts to maximize the number of eligible persons receiving food stamps in South Carolina have been very effective – approximately 90 percent of South Carolinians in poverty are receiving food stamps, up from 50 percent in FY 2000-01. An average of 248,314 households received food stamps in FY 2007-08.

Success should not be measured simply in the number of South Carolinians receiving assistance, but also in the number of those who are able to leave the system. The number of South Carolinians who obtain employment, leave the state assistance program, and remain off assistance for at least one year continues to improve and climbed over 95 percent for the first time this century.

TANF cases closed and remained off assistance for at least a year	
Year Exited	Percent
2002	76.4
2003	78.9
2004	77.3
2005	84.1
2006	90.6
2007	95.5

In addition, child support-distributed collections have steadily increased from \$142 million in 1997 to \$254 million in 2007.



Opportunities for Improvement

The management structure of our state’s health and human services system includes eight different agencies, only three of which answer directly to the Governor. The other five agencies answer to a series of part-time boards. This structure diffuses accountability and sets the executive branch up to look more like a patchwork of competing special interest fiefdoms rather than a united team looking out for the good of the state.

When the MAP Commission first called for health agency restructuring in 2003, 21 other states were also considering, planning or executing health agency restructuring initiatives. Six years later, several of those states, including Alaska, Maine, Texas and Nebraska, have completed those restructuring plans, while South Carolina remains at the starting gate.

While South Carolina has succeeded in some areas, there is great room for improvement in addressing our health care needs. While health outcomes are poor across the South, South Carolinians generally rank worse (42nd nationally in overall health) than our neighbors in North Carolina and Georgia, who rank 36th and 40th respectively. This is despite the fact that we outrank both states in per capita public health spending. As seen in the “Public Health Spending” chart, we are clearly not getting enough value for our health care dollars – a result of the antiquated system.

Public Health Spending		
State	Dollars per Person	Ranking per Capita
SC	\$219	10
GA	\$138	28
NC	\$128	31

Increase the number of citizens leading healthy lives. Unhealthy lifestyle choices made by too many South Carolinians contribute to the state’s overall poor health. The 2007 Health Risk Factors Rankings table below indicates that we engage in behavior that puts children and adults at risk.

This table shows that we have the 18th highest smoking rate in the nation (22 percent) and the 11th highest rate of adults who engage in no physical activity (47 percent). We rank 45th with regard to the number of women receiving appropriate prenatal care and 44th in the prevalence of obesity.

2007 Health Risk Factors Rankings (SC, NC, GA)			
Indicator	Ranking Among 50 States + DC (lower number indicates better health status)		
	SC	NC	GA
First trimester prenatal care	45	23	27
Smoking rate	33	32	28
Smokers who attempted to stop smoking	37	19	22
Obesity	44	41	43
No leisure time/physical activity	40	34	42

Source: National Women's Law Center

These risk factors contribute to the poor health outcomes summarized in the following table, Health Outcomes Rankings. South Carolina's outcomes indicate poor health across our citizens' life spans – from infancy to death.

2007 Health Outcomes Rankings (SC, NC, GA)			
Indicator	Ranking Among 50 States + DC (lower number indicates better health status)		
	SC	NC	GA
Percent of pre-term births	46	37	17
Infant death rate	46	44	43
Child death rate	35	25	29
Cancer death rate	38	33	24
Prevalence of diabetes in adults	42	38	44
Stroke death rate	50	45	44
Adult obesity rate	42	32	39
Adults with no poor mental health days/previous month	32	2	13
Heart disease	33	28	39

Source: Kaiser Family Foundation

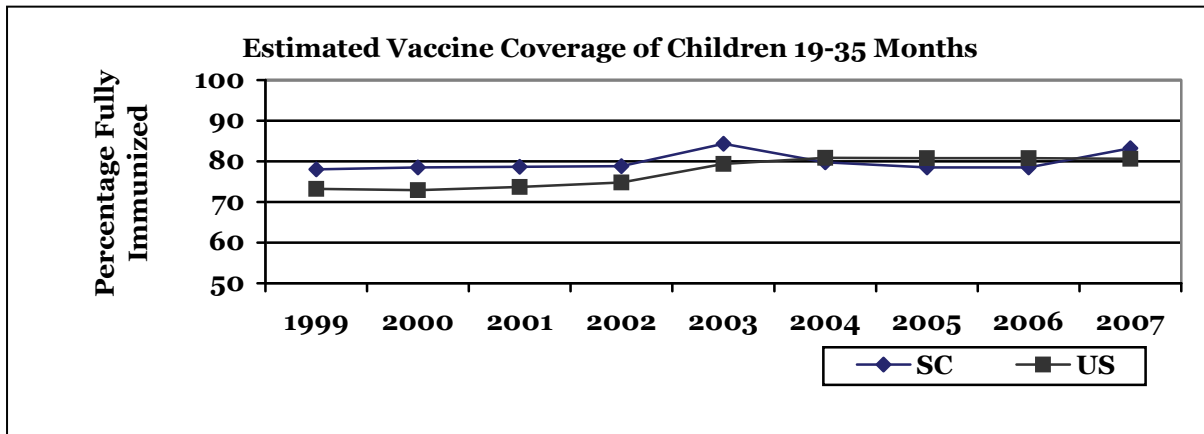
Lack of Health Insurance (Overall State Population)	
State	% Uninsured
Virginia	13.3
Alabama	15.2
U.S. Average	15.8
South Carolina	15.9
Georgia	17.7
North Carolina	17.9
Mississippi	20.8
Florida	21.2

Access to care. About 46 million Americans, nearly 15 percent of the population, are without health insurance. Although in the past year the rate of uninsured South Carolinians decreased by 8 percent, we still have significant room for improvement in the area of health care coverage. Overall, the uninsured rate in South Carolina (15.9 percent) sits above the national average. Individuals without health insurance frequently do not participate in preventive care programs and can add substantially to the cost of health care due to delayed care and emergency department treatment.

Increase the number of children living in a safe and stable environment. According to national standards, we should not have more than 9.9 percent of children entering foster care who had been returned home from a previous foster care placement, re-entering foster care within a 12-month period. In South Carolina for FY 2007-08, the percentage of children who re-entered care due to re-abuse was 7.25 percent, which is better than the national standard.

We are struggling with the stability of foster care placements. The national standard for stability is that of all the children who have been in foster care less than 12 months, 86.7 percent have two or less placement settings. As of July 2008, South Carolina was at 74 percent, still short of the national standard. There has been some progress in this area, however, as the overall length of time children spend in foster care has decreased by 27 percent since FY 2005-06 (from 3.3 years to 2.4 years).

Reduce preventable injury, illness, and death. Immunization against diseases is a cost effective strategy for improving the health of our citizens. South Carolina is currently 14th in the nation with 83.2 percent of South Carolina's children ages 19-35 months being immunized in 2007, which is higher than the national average of 80.6 percent.



The state Occupational Safety and Health Act requires employers to provide their employees with a safe and healthy worksite that is free of hazards that may cause injuries and illnesses to workers. In 2007, our state had 8.5 occupational fatalities (per 100,000 workers), an increase from 6.7 occupational fatalities (per 100,000 workers) in 2005.

Among children, accidents are the number one cause of death in South Carolina. Approximately 45 percent of unintentional injury deaths, according to the National Safety Council, occurred in and around the home. Unintentional home injury deaths to children are caused primarily by fire and burns, suffocation, drowning, firearms, falls, choking, and poisoning.

Increased awareness of and compliance with safety laws and standards, appropriate vaccinations for major diseases, and increased emphasis on curbing domestic violence are all potential ways to improve South Carolina's performance in this area.

Decrease health disparities. Disparities between races in health outcomes continue to be a significant problem in South Carolina. The National Institute of Health has defined health disparities as, "differences in the incidence, prevalence, mortality and burden of diseases and other adverse health conditions that exist among specific population groups in the United States."

The conditions that disproportionately affect minorities living in South Carolina include cancer, cardiovascular disease, diabetes, kidney disease, HIV/AIDS, lack of immunizations, and infant mortality. Large health disparities exist in our state in areas such as prenatal care, certain cancers, obesity, diabetes, stroke, and heart disease. While the state has made some progress in increasing awareness of preventive health strategies among African Americans, much more needs to be done to reduce health disparities.

Reduce poverty. Poverty rates remain direct indicators of economic well-being of children and adults, and are closely linked to physical well-being. Last year the percentage of children in poverty decreased from 19.4 in 2006 to 15.6 percent in 2007. The percentage of South Carolina seniors living below the poverty line is equal to the Southeastern average of 15 percent, but above the national average of 13 percent.

Purchasing Priorities

We developed this purchasing plan by taking proven and promising strategies and then prioritizing them in a way that will achieve the best results. The key strategies we identified are as follows:

Provide incentives to promote healthy lifestyles. Improved quality and length of life among South Carolinians begins with citizens making better choices about their own health. Engaging in unhealthy habits such as poor eating, leading a sedentary life, and smoking cigarettes result in significant health care costs to our state. For example, the prevalence of adult obesity in South Carolina costs \$1 billion in medical expenditures, with about half of the costs being funded by Medicare and Medicaid. Obesity-related expenditures represent more than five percent of South Carolina's annual health care bill. Smoking-related health care costs exceed \$1 billion annually.

Provide increased access to insurance and private payment for health care. Many South Carolinians are either underinsured or without insurance. Health insurance coverage increases the likelihood that people will receive the preventive care they need to stay healthy. A high rate of uninsured individuals puts a strain on emergency care and increases the likelihood that health issues will go unaddressed until they are at a critical point. It has been estimated that the national cost of un-insurance is up to \$130 billion dollars. The cost to South Carolina is \$2.7 billion annually.

Provide measures to increase the number of individuals with an identified primary care physician or medical home. People with a regular provider of health care are more likely than those without a usual source of care to receive a variety of preventive health care services. An estimated 15 percent of adults in the United States lack a usual source of care, and at least two in five residents in South Carolina have inadequate access to a doctor's office, clinic, or health center.

Provide disease prevention and disease management. Many of the health care and societal costs associated with physical and behavioral disorders can be reduced through improved disease management and prevention programs. Health outcomes in South Carolina clearly demonstrate that we fall short in preventing and managing disease. Cardiovascular disease, cancer, and diabetes are among the leading causes of death. On the national level, approximately 1 in every 10 health care dollars is attributed to diabetes. In South Carolina, the total cost of diabetes was \$2.6 billion in 2006. Indirect costs include increased factors such as absenteeism, reduced productivity, and lost productive capacity due to early mortality. Some of these costs could be reduced through improved blood sugar control, control of elevated blood pressure and high cholesterol, and other disease management techniques.

Provide adequate food and nutrition. A 2007 U.S. Department of Agriculture report reveals that 36.2 million Americans, including 12.4 million children, are "food insecure" which refers to the "ability of people to obtain sufficient food for their household." Additionally, South Carolina is listed as one of ten states with the highest "food insecurity rates." Undernutrition can have lasting negative effects upon the physical and cognitive development of children. The Food Stamp Program is the first line of defense in ensuring that low-income families receive adequate nutrition. Programs like the Summer Food Program, Child and Adult Care Food Program, and the Emergency Food Assistance Program help families provide nutritional meals. Providing adequate food and

nutrition through programs like Meals on Wheels supports independent living for home-bound adults.

Provide opportunities for employment and independence. To improve the economic well-being and self-sufficiency of our low-income population and our adults with disabilities, we must find ways to continue to increase opportunities for employment. For adults and seniors, adequate supports such as homemakers, personal care aides, Meals on Wheels, and transportation can prevent or delay nursing home institutionalization. Maximizing living choices for adults and seniors, especially if they choose to stay in their own homes or be cared for by family members, is a win-win cost saving strategy for state government and for South Carolina citizens.

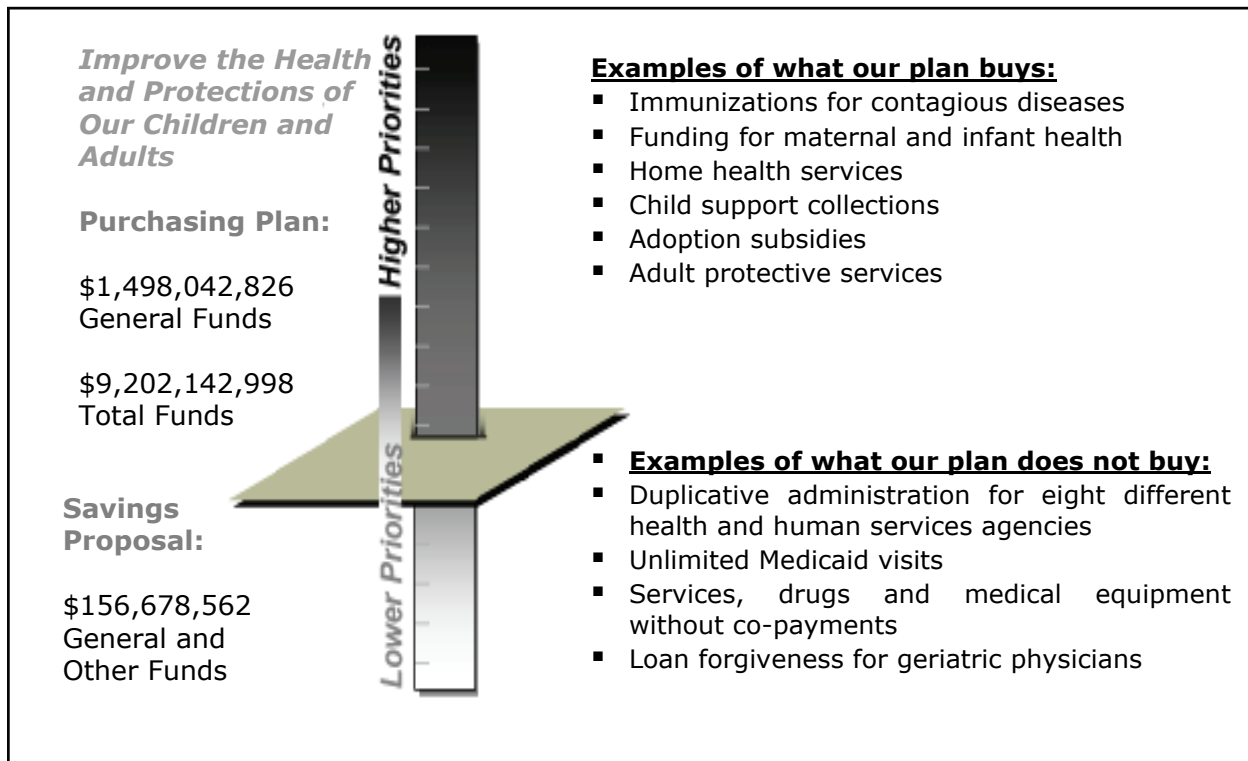
Provide child support collections. To reduce the rate of poverty of South Carolina's children, we must find ways to increase child support collections. According to the 2007 United States Department of Agriculture's report on Expenditures on Children for Families, a single parent home with a household income of \$50,000 will spend a little over an estimated \$140,000 on one child up to the age of 17. The year before high school graduation, that child costs about \$8,800. Children in poverty are more likely to suffer poor health, die in childhood, be developmentally delayed, repeat a grade, drop out of high school, become pregnant during adolescence, and be unemployed after high school.

Provide measures to reduce time for foster children to be adopted. By reducing the amount of time for South Carolina children to be adopted, we can increase the number of children in stable and safe environments and reduce the number of children in institutional settings. Another long-term consequence of children aging out of the foster care system with no permanent family is the high incidence of homelessness experienced by former foster youth. Across the nation, various studies indicate that as many as 27 percent of homeless persons have a history of being in foster care, a group home, or other institutional setting for part of their childhood.

Provide timely and effective interventions when safety is compromised in the home or family environment. Children who are abused and neglected are 25 percent more likely to experience delinquency, teen pregnancy, low academic achievement, drug use, and mental health problems. To reduce costs to society in the long term, children need to be protected from the effects of abuse and neglect. Psychological problems often manifest as high-risk behaviors, which, in turn, can lead to long-term health problems such as sexually transmitted diseases, cancer, and obesity. For adults and seniors, timely and effective intervention will help prevent recurring abuse and improve the quality of care for residents in long-term care facilities.

Governor's Purchasing Plan – Highlights

As we address our state's unprecedented financial problems, it is important to focus on purchasing only those services that deliver the greatest impact on improving the health and protections of our children and adults. In many cases, we have had to use cost savings methods to simply maintain current funding levels for high priority services. We do not purchase services that, while still considered valuable, have been identified as lower priority. The following table identifies key purchases within our executive budget's total state health care and social services spending plan as well as examples of what is not purchased. Detailed highlights of our purchasing plan are provided below the table.



Our Plan Buys:

Increased emphasis on prevention and promoting healthy lifestyles

Immunizations for polio, measles, and other contagious diseases. Many serious childhood diseases are preventable through routine childhood vaccination. Diseases such as polio, whooping cough, and measles are easily spread through communities. Individuals who are not immunized increase the risk that they and others in their community will contract a contagious disease. Also, the flu and pneumonia are among the leading causes of death in the senior population, and both are easily preventable through either an annual flu shot or a one-time pneumonia vaccine. To prevent disease,

disability, and death from preventable diseases and to avoid the exorbitant public health costs associated with these illnesses, we continue to **support recurring funding for these activities amounting to \$3,390,721 in general funds and \$7,936,357 in total funds.**

Funding for maternal and infant health. This funding seeks to improve the health and well-being of children in the state with an emphasis on eliminating health disparities. Activities include family support services, newborn screening and home visits, medical home partnerships, family planning, and nutrition education. These activities also further our goals of promoting healthy behaviors and improving access to comprehensive quality health care. We continue to **support current funding for this activity amounting to \$3,836,045 in general funds and \$130,846,126 in total funds.**

Access to insurance and private payment for health care

Further emphasis on verifying eligibility (including citizenship) for Medicaid benefits. To be faithful stewards of the taxpayers' dollars, we are working on making sure that Medicaid recipients are actually eligible for those benefits. To fund citizenship verification requirements and other related items mandated by the Federal Deficit Reduction Act, we propose to **maintain current funding for this activity, amounting to \$11,672,343 in general funds and \$47,883,939 in total funds.**

Options for Medicaid coverage for enrolled beneficiaries in South Carolina. The state reimburses the Managed Care Organizations a capitated reimbursement rate for enrolled members. These organizations generally provide a coordinated system of primary care aimed at establishing beneficiaries in a "medical home." Additionally, they provide other health services such as health education and home visits. For this service, we propose to **maintain current funding for this activity, amounting to \$101,367,187 in general funds and \$430,847,288 in total funds.**

Disease prevention and disease management

As we maintain funding for prevention-related activities, our state must still deal with the reality that we remain among the unhealthiest populations in the United States – a reality that costs us in terms of both dollars and lives.

Our budget proposes to continue purchasing many activities that manage illness. Because managing illness among the poor and disabled is so important to our state, this budget proposes to fund these activities so that continued health care cost increases can be absorbed without having to reduce services. Important activities include:

Inpatient and outpatient hospital care. Our prevention, pharmacy, medical professional, and clinic services seek to reduce Medicaid recipients' need for hospital care. Nevertheless, some circumstances require a more specialized setting. We propose to **maintain funding for Medicaid hospital services with \$189,360,286 million in recurring funds and \$5 million in nonrecurring funds – amounting to \$194,360,286 in general funds and \$1,166,953,601 in total funds –** to ensure that our fellow citizens who require this high-level care continue to receive the help they need.

Prescription drug availability for South Carolinians on Medicaid. Pharmaceutical services covered by Medicaid include the provision of most prescription and over-the-counter drugs. Pharmacy utilization levels are growing, but we can save on pharmaceutical costs by pooling our buying power with several other states in the National Medicaid Pooling Initiative. Therefore, we intend to **maintain funding for this activity, amounting to \$42,675,311 in general funds and \$457,197,602 in total funds.**

Clinical Services for South Carolinians

Acute Psychiatric Services for consumers whose conditions are temporarily severe enough that they cannot be treated in the community. Services are delivered in a hospital setting with the intention of improving the patient's ability to function and decreasing the number of patients who have to return to a hospital setting for treatment. We propose to **maintain recurring funding for this activity amounting to \$15,938,650 in general funds and \$27,824,606 in total funds.**

Long-term inpatient psychiatric services for adults whose conditions are of such severity that they are not able to be treated in the community. Services for these individuals are provided by a multidisciplinary team in a hospital setting. We propose to **support recurring funding for this activity, amounting to \$22,587,644 in general funds and \$39,000,927 in total funds.**

Chemical dependency community-based treatment services. The need for mental health and substance abuse treatment is closely linked as many individuals with mental illness abuse alcohol and other drugs. Services for individuals with chemical dependencies range from locally available outpatient treatment to specialized treatment such as detoxification, adolescent inpatient services, and residential services. First, this funding will go toward evidence-based prevention for adolescents to prevent alcohol use and alcohol dependency. Second, it will be used for treatment services within the community to reach individuals early in the dependency cycle to reduce the need for more expensive, episodic treatment in residential facilities and hospital emergency rooms. We propose to **maintain funding for this activity, amounting to \$7,188,225 in general funds and \$23,376,262 in total funds.**

Adequate food and nutrition

Food stamps and other food programs for South Carolinians. The food stamp program is a federal entitlement program. It is administered by the state to provide low-income families and individuals food stamps through the use of debit cards. For those who qualify, the Food Stamp program must provide work-related activities that will lead to employment and decrease dependency. The provision of funding to pay for food helps safeguard the health and well-being of the state's population. We propose to **maintain current funding for this activity amounting to \$11,165,815 in general funds and \$682,827,631 in total funds.**

Opportunities for employment and independence

Home health services for recipients. Home health services include part-time nursing aide services, therapies (i.e., physical, speech or occupational), and supplies. We propose to **maintain funding for this activity amounting to \$7,464,141 in general funds and \$26,349,638 in total funds.**

Child care vouchers for children in families transitioning off of welfare and for other low-income families. The vouchers allow eligible low-income families to become and remain employed with the help of available, affordable, high quality child care. This protects the children's well-being while their parents work or attend school or training. We propose to **maintain funding for this activity amounting to \$6,962,037 in general funds and \$119,963,154 in total funds.**

Vocational Rehabilitation Direct Client Services to persons with disabilities. This activity provides assessment, counseling, placement, academic training, transportation, and retention services to eligible adults with disabilities to prepare for employment. Successfully employed clients become contributing members of the workforce rather than relying on Social Security disability benefits, Medicaid, and other public assistance. The cost of their rehabilitation is repaid through their taxes in an average of 5.6 years. We propose using administrative savings derived from restructuring the Vocational Rehabilitation Department and the Commission for the Blind to **maintain recurring funding for this activity, amounting to \$10,289,248 in general funds and \$43,492,482 in total funds.**

Rehabilitation services for eligible blind and visually impaired individuals. Vocational rehabilitation services led 313 blind and visually impaired citizens to competitive job placements in FY 2007-08. We propose to **maintain current funding for this activity amounting to \$815,918 in general funds and \$6,494,970 in total funds.**

Community training homes for vulnerable South Carolina citizens. Community training homes offer the mentally challenged the opportunity to live in a home-like environment under the supervision of trained caregivers. We propose to **maintain current funding to help reduce the waiting list for the mentally challenged, amounting to \$4,637,820 in general funds and \$10,510,201 in total funds.**

Temporary Assistance to Needy Families. This program provides assistance to needy families with children and provides parents or caretaker relatives with job preparation, work experience, job placement, and support services to enable them to leave the program and become self-reliant. This activity assisted clients in finding more than 10,000 jobs last fiscal year. We propose to **maintain funding for this activity amounting to \$14,328,813 in general funds and \$147,207,405 in total funds.**

Child support collections

Child support enforcement for children receiving support from a non-custodial parent. Child Support Enforcement establishes paternity for children born out of wedlock, establishes and enforces orders for child support, and collects and distributes the support. Support collected from

non-custodial parents totaled \$254 million in FY 2006-07. In actual performance, for every \$1 spent in child support activities, it returns \$6.87. We propose to **maintain recurring funding for this activity, amounting to \$17,463,011 in general funds and \$82,659,280 in total funds.**

Measures to reduce time for foster children to be adopted

Foster care services for children who have been abused or neglected, are no longer able to safely stay with their families, and are taken into the custody of the state. Foster care is the temporary placement of a child with a licensed foster family or group home. Foster care workers monitor the children in the foster or group home and arrange needed medical, educational, vocational, social, treatment, and rehabilitative services. Foster care workers also identify needed services for the birth family if reunification is the plan. These services protect the child and provide a temporary home environment. We propose to **maintain recurring funding for this activity, amounting to \$11,700,718 in general funds and \$45,382,816 in total funds.**

Adoption services for children with a plan to find loving and stable families for foster children, which includes recruiting parents, performing or contracting for home studies, placing children with families, and stabilizing placements after the adoption. We propose to **maintain recurring funding for this activity, amounting to \$2,969,388 in general funds and \$11,814,478 in total funds.**

Adoption subsidies for special needs children. This program provides a monthly subsidy to adoptive parents based on the needs of the child up to the amount the child received in foster care. We propose to **maintain funding for this activity, amounting to \$9,866,719 in general funds and \$25,303,129 in total funds.**

Adoption incentives to families to cover part of the adoption costs. We restored this incentive in 2004 to help further our goal of finding permanent, stable homes for our state's 1,500 foster children with a plan for adoption. We propose to **maintain current funding at \$750,000 for this activity, amounting to \$1,500,000 in total funds.**

Timely and effective interventions when safety is compromised

Child protective services when child abuse or neglect is suspected. CPS workers investigated thousands of reports of child abuse and neglect last year. When abuse is confirmed, treatment services are provided to the family, allowing the child to remain in the home when possible. These services protect the children and prevent them from being removed from their families. We propose to **maintain current funding for this activity, amounting to \$7,437,391 in general funds and \$33,539,693 in total funds.**

Adult protective services for vulnerable adults living in a non-institutional setting. This service identifies and corrects conditions of actual or potential abuse, neglect, or exploitation of persons 18 years or older who are disabled or incapacitated. We propose to **maintain recurring funding for this activity, amounting to \$632,265 in general funds and \$7,759,775 in total funds.**

Our Plan Saves By:

Restructuring our health care agencies. We continue to support consolidating five health services agencies into two agencies, each more directly accountable to the Governor and to the citizens of South Carolina. We expect that creating an efficient health services delivery system will yield approximately **\$15.4 million in general fund savings in the first fiscal year.** The administrative savings are delineated as follows:

- Department of Health and Environmental Control: \$5,672,714
- Department of Mental Health: \$6,874,703
- Department of Disabilities and Special Needs: \$2,259,107
- Department of Alcohol and Other Drug Abuse Services: \$501,920
- Continuum of Care: \$152,315

Making our Human Services agency structure more efficient by merging the Vocational Rehabilitation Department and Commission for the Blind. In 2002, the Legislative Audit Council recommended that the General Assembly merge the Commission for the Blind and the Vocational Rehabilitation Department to realize increased efficiency and lower costs. The LAC report found that this could be done without adversely affecting the quality of services provided by either agency. The report further found that 1) both agencies' core missions are to place clients in competitive employment; 2) over 50 percent of the commission's budget is spent on competitive job placement; 3) South Carolina is one of only 12 states with a stand-alone commission; and 4) the rehabilitation rate for merged agencies is higher than the combined rates of stand-alone agencies. We propose merging these two agencies, **saving \$654,826 in the first year, and redirecting those savings to fund direct client services at the new agency.**

Capping the number of enrollees in the expanded Medicaid SCHIP program. The state budget shortfalls have presented a variety of challenges for our SCHIP program, and they have not been immune from making tough decisions. Our current program covers a significant number of children relative to other states. For instance, the South Carolina program covers approximately 40 percent of all children ages 0-18; only Arkansas, Louisiana, Mississippi, New Mexico, Vermont and the District of Columbia cover a higher percentage. Regionally, South Carolina covers a higher percentage of children than Georgia, Florida, or North Carolina. Expanding this system puts us even further toward the top.

Due to a lack of funds, and with more than 40 percent of the children in our state already receiving Medicaid benefits, we recommend an enrollment cap for the expanded SCHIP program starting July 1, 2009. An enrollment cap would allow us to establish a certain number of eligibility slots for children: as some children leave the program, new children are enrolled to take their place.

In June 2007 we vetoed this funding because, while well-intended, we had concerns about the long-term consequences on our ability to fund health care. In 2000, the Medicaid program comprised \$1 out of every \$7 in state funding; now the ratio is approximately \$1 out of every \$5. Even without this expansion in the State Child Health Insurance Program, projections showed that the state could spend as much as \$1 out of every \$3 in the state budget on an annual basis. Ultimately, our veto was

overridden and the change increased Medicaid eligibility from 150 percent of poverty to 200 percent of poverty.

With that in mind, we **propose capping the number of enrollees as of July 1, 2009, and saving \$14,275,806.**

Allowing Medicaid beneficiaries to participate in cost-sharing. A 2003 Legislative Audit Council report encourages the Department of Health and Human Services to take full advantage of federal options for cost-sharing by Medicaid recipients. A new federal rule provides parameters for what states may charge Medicaid beneficiaries for co-payments for physicians' services, hospital care, and prescriptions drugs. The rule allows states to implement a sliding scale for premiums and co-pays, the total of which cannot exceed five percent of a family's income, with the cost sharing adjusted for inflation each year. Under the new rule, states can enforce the collection of the cost sharing for services rendered, in certain cases.

One possible way to reduce Medicaid expenditures is to increase the co-payments that Medicaid beneficiaries must pay when receiving medical care. According to the Kaiser Commission on Medicaid and the Uninsured, there is a national trend to do so. In fact, four states raised Medicaid co-payments in 2002, seventeen states increased them in 2003, twenty states raised them in 2004, and nine states did so in 2005.

During the budget process in 2007, the House of Representatives included such a provision in the SCHIP stand alone program, which we supported, that required co-payments based on income for participants in the Medicaid system to make the cost of this expansion more affordable.

Given our current financial situation, we think it is reasonable to ask eligible beneficiaries to contribute a small portion toward their own health care. These co-payments allow the agency to offset reductions and ultimately provide services to more people. By requiring co-payments, **we save \$125,000.**

Eliminating the Office on Aging Geriatric Physician Program. Since this loan forgiveness program began, only 14 doctors who have agreed to practice geriatrics in South Carolina for at least five years have actually received loan forgiveness. While we believe this is a worthy goal, and recognize that South Carolina is the only state to give this type of incentive, we believe that the geriatric practice in South Carolina would benefit more from the National Health Service Corps Loan Repayment Program, which is supported by the American Geriatric Society. This national program recruits health professionals to provide primary health services in areas that lack adequate medical care. In return, the federal government offers loan forgiveness. Because of the availability of federal loan forgiveness, we propose eliminating the Geriatric Physician Program and **saving \$105,000.**

Making Tough Choices:

Given the state's finite amount of resources, we had to make some difficult choices regarding which activities to fund. During the last fiscal year, several health-related state agencies reduced administrative costs, eliminated agency staff, and implemented a mandatory furlough for all employees. However, it was also necessary to make substantive changes to services provided to beneficiaries.

For example, in December 2008, as a result of significant state revenue shortfalls, the Department of Health and Human Services notified providers that Medicaid was limiting hospice coverage to those eligible for Medicare, cutting the service by **\$1,500,000**. Home health visits were reduced from 75 to 50 visits per year, cutting the service by **\$700,000**. In addition, Medicaid no longer covers adult dental procedures (**\$2,000,000**), vision services (**\$500,000**), and podiatry services (**\$500,000**). Waiver beneficiaries are receiving a maximum of seven home-delivered meals per week, down from 14 meals a week (**\$787,000**).

The Department of Disabilities and Special Needs, which serves more than 20,000 South Carolinians with mental retardation and related disabilities, autism, traumatic brain injury, and spinal cord injury, also experienced harsh cuts. For example, child development centers (five around the state) serving 108 children with special needs have been closed, resulting in a reduction of **\$357,160** in state funds. Additionally, summer services providing specialized recreational/camp opportunities for children and adults, usually lasting one week, have been cut. This results in a reduction of **\$354,870**. The Department has also decreased early intervention service programs. These in-home programs instruct families how to work and play with disabled children, younger than six, to help stimulate and strengthen the child's development. After the age of six, the child is school age and similar therapy is provided in the school setting. This decrease reduces agency costs by **\$989,267**.

While the activity below has merit, when compared to other activities, we did not think its anticipated outcome would be effective in achieving our goal.

South Carolina State's Nutrition, Diet and Health program that is duplicative of DHEC's obesity awareness campaign. South Carolina State University's public service activity provides low-income families with nutrition education to promote healthy living and to deter obesity. Our administration has been very vocal in support for health and exercise programs and recognizes the important service this type of activity provides. However, we recommend eliminating this program, because not only does it fall outside the core mission of the educating students, it duplicates DHEC's obesity awareness campaign (SCCOPE), which fosters statewide efforts to promote healthy lifestyles. We propose **eliminating this program and saving \$270,362**.

Please see the Appendices for a complete listing of the Governor's Purchasing Plan for this goal area and for a detailed listing of what our plan saves and what our plan does not buy.

Improve the Quality of Our
Natural Resources

Improve the Quality of Natural Resources

The high quality of South Carolina's natural resources is directly correlated to our citizens' high quality of life. From our pristine beaches to the majestic Blue Ridge, South Carolina has a lot to offer in the way of natural beauty. To ensure future generations will enjoy an equally high quality of life, we must maintain the balance between economic development and environmental protection.

South Carolina's landscape is likely to change now more than ever as recent estimates suggest the state's population will increase by 1.1 million people by the year 2030. With such change comes a unique opportunity to shape our state's future – from preserving our natural resources to developing our towns and neighborhoods. Our state's natural beauty – our beaches and marshlands, mountains and rivers – will become increasingly endangered unless we protect our environment and manage land use development. We must always strike a balance between infrastructure needs and environmental protection – between new construction and God's creation. Finding this balance is the key to South Carolina's way of life.

Natural resources provide both an immediate economic benefit and a lasting quality of life to the citizens of South Carolina. For these reasons, our budget priorities will focus on activities that deliver positive outcomes and preserve South Carolina for future generations.

Administration's Goals for Improving the Quality of Our Natural Resources provide for:

- ✓ Managing state resources for public benefit.
- ✓ Minimizing the negative effects related to business and population growth, industrialization, and development.
- ✓ Regulating and enforcing quality standards.
- ✓ Producing outcome-driven solutions for citizen stewardship.

Developing Our Purchasing Priorities

To develop our purchasing priorities, we examined whether state government is currently reaching its goal of improving the quality of South Carolina's natural resources. South Carolina continues to make progress, but the accelerating pace of land development, the flagrant abuse of our environment by litterbugs and arsonists, and public indifference toward recycling and neighborhood conservation threatens the future of South Carolina's natural beauty.

Where We Are Succeeding

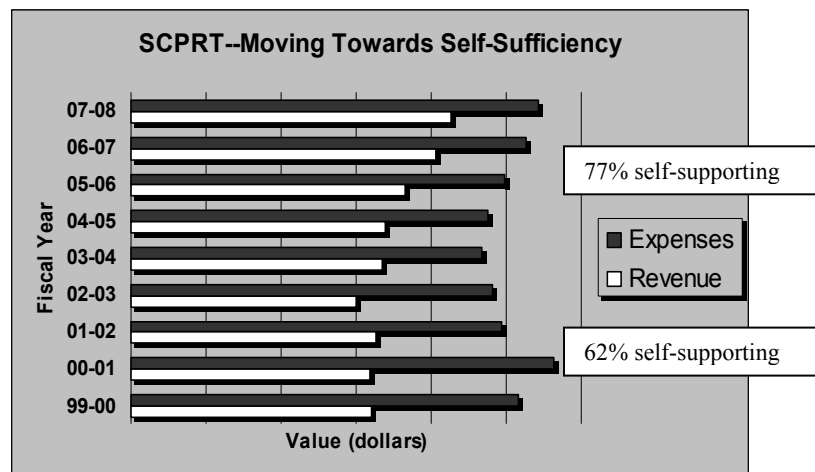
One of the state's most successful efforts in preserving our natural resources was the creation of the South Carolina Conservation Bank. The Bank works with private foundations, land trusts, and other government agencies to conserve natural resources in South Carolina by giving landowners incentives to create conservation easements on their property and by purchasing interests in land from willing sellers. The Bank decides to purchase land based on objective evaluations of the land's natural resource value, financial leverage, and relative benefit to the public. Since its creation, the

Bank has conserved a total of 43,468.89 acres of forest lands/wetlands, 268.59 acres of urban parks, 1,334.52 acres of farm lands, and 165.7 acres of historical lands. In its four years of funding, the Bank has conserved 152,720 acres of land – guarding the heritage that makes South Carolina such a special place. The Bank has become the main source of land conservation funding for statewide grants, and has funded conservation projects in 38 counties in South Carolina. 2007 was a very good year for the Bank – conserving an additional 45,237.7 acres at an average cost of \$446.03 per acre.

In 2008, the General Assembly cut the Conservation Bank's entire funding except for pending contractual obligations. While we understood the need to cut some funding due to budget shortfalls, we believe the Bank should not be zeroed out since preservation of our state's natural resources is important to ensuring the qualities that attract tourism, economic development, and retirees to South Carolina.

In addition to conservation of land, our state is also making progress in the area of energy conservation. In July 2008, the Public Service Commission approved regulations for net metering in South Carolina. Net metering refers to a system that allows homeowners or businesses that generate power, whether by solar fuel cells or wind turbines, to sell any excess energy to the utility provider. In other words, if your home runs on solar fuel cells and you use less power than you generate, you can sell the excess back to the power company. Currently, all power companies in this state (SCE&G, Duke Power, Santee Cooper, and Progress Energy) offer a net metering program. Because net metering is such a practical energy solution, we encourage net metering in South Carolina and hope our citizens will continue to find innovative ways to produce clean, renewable energy.

During this administration, the Department of Parks, Recreation, and Tourism's (SCPRT) State Park Service has made great strides in improving the way the state's parks are operated. As a result of five years of improving management, spurred by this administration's steady encouragement, South Carolina's state parks are now 77 percent self-supporting.



The recent developments surrounding the State Farmer's Market present new opportunities for agricultural commerce within our state. A public-private partnership to build a new market in Lexington County broke ground on the project in August 2008. While there have been many delays in finding the appropriate site for the market, we are hopeful that this public-private partnership will develop a successful market and save South Carolina taxpayer dollars. When it opens in April 2010, the new market will further the Department of Agriculture's mission of providing new opportunities for our state's farmers and enhancing agricultural commerce in the Palmetto State.

Because of the expected increase in land development, we will be presented with the task of balancing private property rights with South Carolinians' interest in protecting our state's natural

beauty. We are pleased that the General Assembly worked with us to address one such challenge by passing H.3575 to simplify the permitting process. When a regulatory agency considers whether to issue a land-use permit, the agency gives interested parties the opportunity to have input in the permitting process. Unfortunately, the previous public input process allowed for serious abuse, which some people exploited in an effort to hinder beneficial development. Among other things, H.3575 gives citizens input into an agency's decision of whether to grant a permit, yet avoids some of the unnecessary delays and costs that can harm developers. This law strikes a good balance between making the permitting process more efficient while also ensuring that the permitting outcomes are fair.

Opportunities for Improvement

An enterprise cannot be successful when its management lacks sufficient freedom to make smart decisions. While SCPRT's State Park Service has significantly improved its fiscal performance under this administration, the General Assembly refuses to give the agency the option to explore privatization of Hickory Knob or Cheraw state parks. Privatization is important because it would give the agency, through the efforts of private management, greater ability to attract tourists and provide public recreation to our citizens. Privatization would also allow the agency more freedom to manage state parks in ways that use state revenue more efficiently. We again urge the General Assembly to lift budget Proviso 39.7 and allow the agency to decide how to best manage state parks.

A recent multi-agency study by the Environmental Protection Agency gave our state's air quality the highest rating possible. However, our state's level of water pollution is a serious problem that affects the quality of life of all our citizens, not just those with waterfront property. As documented by several recent articles in *The State* newspaper, the South Carolina Department of Health and Environmental Control (DHEC) has not adequately carried out its mission of protecting our citizens from harmful pollutants – including failing to monitor pollutants coming from a coal-power plant in Georgetown, failing to protect the Little Pee Dee River from a hog farm in Dillon County, and failing to prevent sewage pollution from contaminating the Saluda River. DHEC's environmental oversight is compromised at times by its potentially conflicting objectives: weighing health and environmental protection against economic and industrial development. Unfortunately, DHEC's current structure does not give the governor direct control over the agency's policy decisions or execution, and the current structure insulates DHEC from real accountability. This is yet another example – seen all too often in state government – of when everyone is in charge, no one is in charge. We ask the General Assembly to consider restructuring DHEC in ways that make it directly accountable to the governor and focus its efforts to protect our environment.

The Governor's Climate, Energy, and Commerce Advisory Committee (CECAC) recently completed a comprehensive study of South Carolina's current level of green house gas emissions and recommended energy and economic policy objectives. For instance, CECAC recommended reducing emissions by state agencies, encouraging utilities to invest in energy-efficient practices, and supporting the expansion of nuclear power production. The problem of global warming threatens us just as much as our nation's current financial crisis, and we cannot afford to put off our responsibility any longer. The CECAC report is a tool that our state can use to form intelligent energy policy goals to meet our state's energy needs.

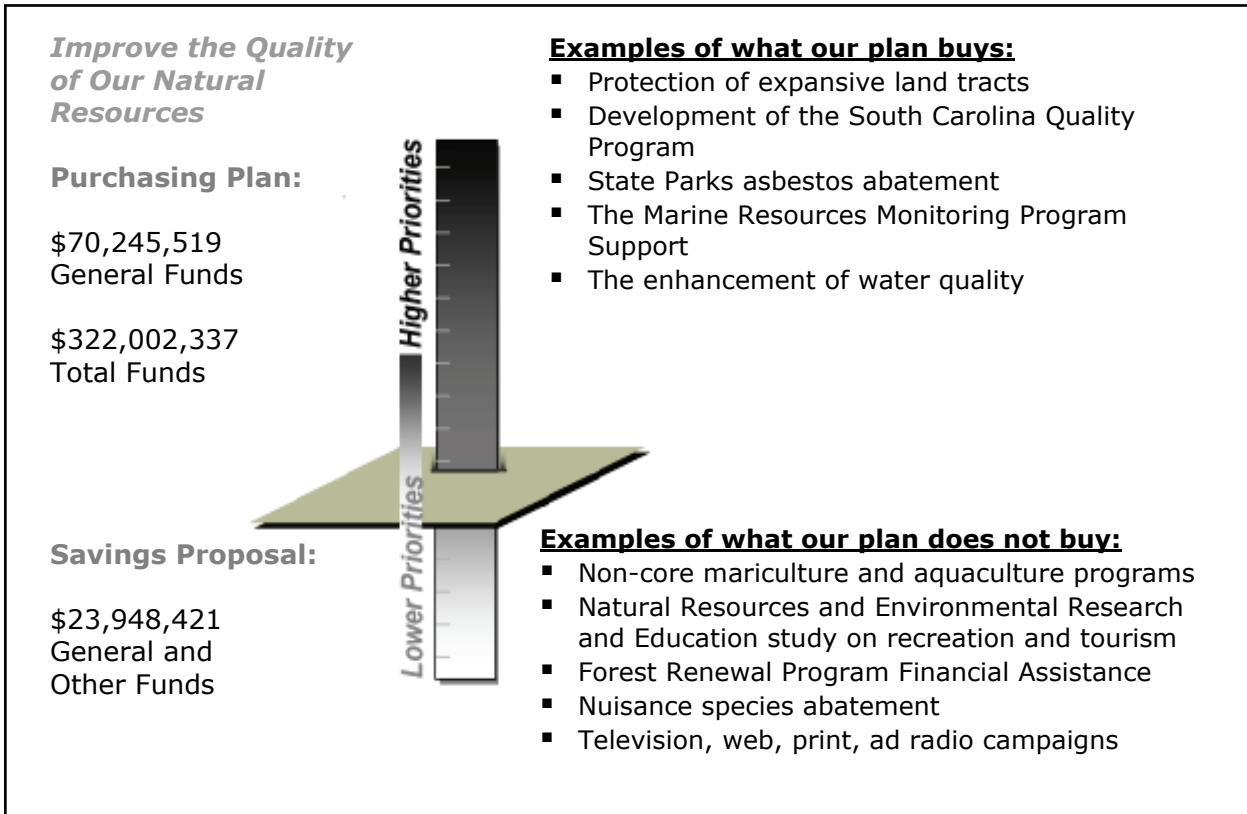
Purchasing Priorities

Having determined where we are succeeding and where opportunities for improvement exist, it is important to identify the strategies that dictate our spending priorities and will help us achieve our objectives.

1. Market and enhance the economic and social value of South Carolina's natural resources. Billions of dollars are contributed annually to South Carolina's economy from natural resource-related industries. To achieve our objectives, we must encourage the responsible use of South Carolina's agriculture, forestry, aquaculture, parks, and tourism-related resources. It is essential that we consider long-term economic goals and increase public access to natural resources for recreational and commercial use.
2. Create statewide policies, incentives, and programs aimed at ecological sustainability. Ecological sustainability demands programs that offer flexible, creative, and rapid responses to conservation and preservation issues; pursue beneficial partnerships between citizens, nonprofits, and the state; enable landowners to manage and pursue conservation opportunities; and support land use planning efforts that respect private property rights. In sum, natural resource conservation requires us to be dedicated to policies and practices that sustain our ecosystem but do not overburden landowners.
3. Minimize the negative effects of population growth, industrialization, and development on our natural resources. According to current estimates, South Carolina will have 916 square miles of new development by 2030. To put that figure in perspective, the U.S. Census Bureau estimates that Charleston County has a total area of 918.51 square miles. Such rapid development will demand that we pay close attention to land conversion rates, deforestation, and the potentially negative impact of uncontrolled growth. It is vital that we carefully consider the long-term effects of current development patterns and plan accordingly.
4. Create and enforce quality standards and the responsible use of natural resources. To maintain the high quality of our state's resources, we must create and enforce air and water quality standards through the use of permits, inspections, and other means.
5. Create and maintain programs aimed at citizen-level stewardship and education. By educating the public, we can significantly reduce the amount of state resources spent to maintain and repair public property. Educational opportunities should provide public information encouraging environmental stewardship, educate youth on South Carolina's natural resources, promote "best practices" in forestry and agriculture, and encourage the responsible use of our natural resources.
6. Prevent and respond to the irresponsible use of our natural resources. Mankind may very well be classified as "enemy number one" to natural resources. By creating measures that prevent or deter people from violating our state's environmental regulations, we can better preserve our natural resources.

Governor's Purchasing Plan – Highlights

As we address our state's unprecedented financial problems, it is important to focus on purchasing only those natural resource services most needed by our citizens. In many cases, we have had to use cost savings methods simply to maintain current funding levels for high priority services. We do not purchase services that, though valuable, are lower priorities. The following table identifies key purchases within our executive budget's total state natural resources spending plan as well as examples of what is not purchased. Detailed highlights of our purchasing plan are provided below the table.



Our Plan Buys:

Funding the Conservation Bank from a Portion of the Film Incentives Program. South Carolina's natural beauty has made it an attractive site for movie making, which is why our administration has long supported reasonable incentives to create a vibrant film market in our state. We recognize the important impact the film industry has on the quality of life in South Carolina and support the future existence of the film industry in our state. However, the Department of Commerce and a recent College of Charleston study confirm that the current film incentives program is not producing positive returns for the state. Rather, in many cases film producers have used the generous wage rebates offered under the current program to provide jobs to out-of-state film crews that temporarily locate to South Carolina during filming and then leave the state. The

South Carolina Senate also recognized flaws in the program and has created a study committee to determine whether it benefits the state's taxpayers.

Accordingly, while changes are being made to correct the flaws in the film incentives program, we recommend redirecting a portion of these funds to a program that can greatly benefit our citizens and future generations by securing the scenic landmarks that are so attractive to the film industry – the Conservation Bank. Now is an ideal time to buy land due to falling prices, and yet in the fall of 2008, the General Assembly cut the Bank's funding in its entirety, except for pending contractual obligations. For FY 2009-10 we propose **redirecting \$4.9 million** from the film incentives program to the Conservation Bank. Once the changes to the program have been implemented, we will revisit fully funding the film incentives program. Additionally, we propose maintaining current law which requires that deed recording fees go toward funding of the Conservation Bank.

Marine infrastructure and resources monitoring program support. This program strengthens marine infrastructure in South Carolina. Marine monitoring provides South Carolina with profitable tourism-related industries while promoting a sustainable ecosystem. We propose maintaining the current funding level of **\$801,470** to help preserve South Carolina's aquaculture.

Enhanced water quality. South Carolina has 29,794 miles of rivers, 407,505 acres of lakes, and 401 square miles of estuaries that would benefit from a large-scale monitoring network. Water is becoming a coveted resource – as shown by recent disputes with Georgia and North Carolina – and the monitoring and maintenance of water quality and quantity will only increase in importance. Therefore, we propose maintaining the current funding level of **\$1,155,000** for this program.

Our Plan Saves By:

Consolidating select DHEC functions, DNR, and the Forestry Commission into the newly formed Department of Environment and Natural Resources. Only 20 percent of DHEC's budget is allocated to environmental activities, and many of the Forestry Commission's responsibilities can be provided by DNR. This proposed consolidation will make our administrative system more efficient – freeing up **\$1,636,968** of general funds.

Continuing to encourage the golf course industry to fund turf-grass research. Because the industry derives such value from this service, we feel it should be responsible for funding the continued research, thereby eliminating the need for a state subsidy of **\$145,200**.

Making pesticide licensure programs self-sufficient. Nearly all of the South Carolina Department of Labor, Licensing, and Regulation's licensing regimes are self-sufficient. To further the effort of creating a self-sufficient pesticide licensure program, we have pushed to 1) enable LLR to provide more efficient online certificates and renewals, and 2) extend renewal cycles to two years. Our proposal would result in a cost savings of **\$280,345**.

Integrating PSA's forestry efforts with Forestry Commission programs. Clemson PSA provides "best management" forestry programs, but the Forestry Commission already provides similar sustainable forestry programs. We recommend integrating all forestry programs under the

Forestry Commission. Integration provides strength and efficiency for the program while conserving **\$1,620,778** of general funds.

Integrating our state's food-processing regulatory system is necessary to ensure that two or more agencies are not performing the same regulatory function. While testing and inspecting South Carolina's food-processing operations are important to the health of our state's citizens, we do not need different state agencies to duplicate each other's work. Currently, DHEC, the state Department of Agriculture, and the state Livestock-Poultry Health Commission each take part in administering our state's food inspection laws. Food-processing oversight should be DHEC's exclusive responsibility, thereby saving an estimated **\$592,443** of general funds.

Reducing the negative impact of animal agriculture on the environment by encouraging privately-funded research and educational programs for animal agriculture producers. Though it is imperative that we reduce the effects of animal waste on the environment, we think these activities should be funded by private organizations and individuals. By creating a fee-based system, we are able to save **\$100,000** of general funds.

Supplementing our current funding for wildland firefighting efforts with a fee-based system. Our proposal maintains the Forestry Commission's role in protecting our citizens and private and public property at a lower cost to South Carolinians. We think the current funding should be decreased by **\$1,000,000** and offset by charging private landowners who receive the state's services or by opening up this activity to private sector competition.

Eliminating duplicative programs currently being performed by Clemson PSA and the Department of Agriculture. The Department of Agriculture's "Certified South Carolina Grown" program and a similar program operated by Clemson PSA work to provide marketing services for South Carolina's agricultural industry. Because of the current budgetary needs, and because the department receives separate funding to support the State Farmers Markets, we believe funding two separate programs that render similar marketing services is not a wise use of state revenue. We recommend eliminating the funding for "Certified South Carolina Grown" because we don't think spending general funds on advertising is the most responsible way to spend the few dollars we have in this difficult budget year. Our proposal saves **\$2,758,807** of general funds.

Making Tough Choices:

Given the state's finite amount of resources, we have to make some difficult choices about the best ways to allocate state funds. While the following activities have merit, we do not think their anticipated outcomes are as effective in achieving our goals as the programs discussed previously – particularly in a difficult budget year.

Non-core mariculture and aquaculture programs. We propose limiting DNR's role in mariculture and aquaculture to issuing permits, ensuring regulatory compliance, and conducting relevant research. For instance, we believe research for species like red drum is important to a viable state industry, but such research should be performed by industries and other entities that profit from such research – allowing us to rededicate **\$611,930** of general funds to more critical needs in this tight budget year.

Natural Resources and Environmental Research and Education study funding on recreation and tourism from Clemson PSA. This program is a lower priority than other areas such as education and health care. Also, we believe individuals and private industry can perform this function. This proposal saves **\$1,406,613** of general funds.

Television, web, print, and radio campaigns. Our need to fund productions like “Making It Grow” is a lower priority than other areas, such as health care and law enforcement. We believe we should coordinate with the Department of Agriculture regarding the state’s media campaigns and that we should reevaluate PSA’s communications strategy. We propose to reduce funding for television, web, print, and radio by one-third – saving **\$421,299** of general funds.

Forest renewal program. Alternative financial assistance is available for private, non-industrial landowners. Critical needs in other budget areas take precedence over the state’s contribution of **\$200,000** for this landowner subsidy.

Please see the Appendices for a complete listing of the Governor’s Purchasing Plan for this goal area and for a detailed listing of what our plan saves and what our plan does not buy.

Improve the Safety of People
and Property

Improve the Safety of People and Property

From day one, our administration has made “quality of life” in South Carolina a priority. South Carolina provides a unique look and feel that most other states and countries cannot provide. It is important to continually work to not only maintain but also improve our state’s quality of life for many reasons including protecting citizens from dangers and disasters – a core responsibility of government. Quality of life is also important to companies that are considering where they want to invest resources and create jobs. Finally, maintaining a high quality of life is important to sustaining the state’s tourism industry – the foundation of South Carolina’s economy.

Many factors go into determining whether a place has a high quality of life – the natural beauty of the environment, quality education, and the ease with which citizens live their daily lives. At a fundamental level, however, no factor is as important when discussing quality of life than the ability of citizens to live free from crime and unnecessarily harsh results of natural or man-made disasters. Individuals should not be forced to live in fear because of excess crime, and when disaster strikes, citizens should be confident that the state and local government will effectively respond to and resolve the current crisis.

South Carolina once again ranked second in the nation in violent crimes per 100,000 people (trailing only Washington, D.C.), according to a recent Federal Bureau of Investigations (FBI) report. Many factors contribute to the struggles that South Carolina has experienced in this area including population density, concentration of youth, climate, economic conditions, strength of local law enforcement agencies, education levels, crime reporting practices of citizens, and family cohesiveness. However, lack of consistent support through the budgetary process has played a disproportionate role in continuing this discouraging trend. Nowhere has this lack of support been more evident than at the Department of Corrections and the Department of Probation, Parole and Pardon Services.

In addition to criminal activity, South Carolina is also vulnerable to natural and technological hazards. Not only is our coast vulnerable to hurricanes every year, but the state has also been heavily impacted by droughts for the past several years. Charleston’s port and the eight nuclear power facilities spread across the state are also vulnerable to terrorist activity.

Administration’s Goals for **Improving the Safety of People and Property** are to:

- ✓ Decrease personal injuries and property damage that result from natural and man-made disasters (non-criminal) and criminal activities.
- ✓ Increase the percentage of offenders managed successfully.
- ✓ Increase emergency response and recovery following natural and man-made disasters and criminal activities.
- ✓ Increase citizens’ confidence in their safety.

South Carolina continues to face challenges in the area of transportation safety in terms of automobile accidents. South Carolina has been cited as having the second most deadly roads in the nation and continues to rank high among states in the number of alcohol-related fatalities.

The tie that public safety has to our state's quality of life makes it a core government function and, therefore, a priority in our executive budget.

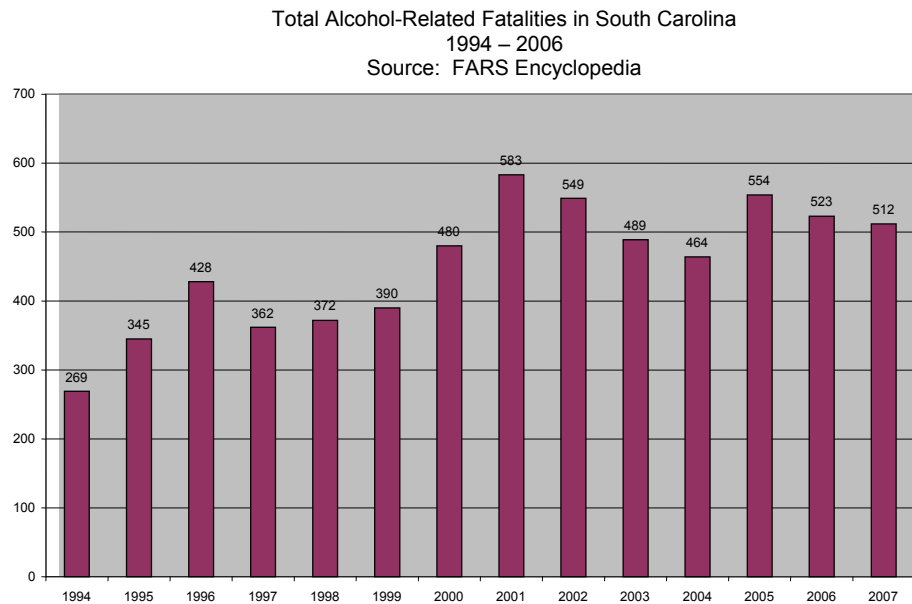
Developing Our Purchasing Priorities

To develop our purchasing priorities, we first established major indicators that will assist us in monitoring the annual progress of improving the safety of people and property in South Carolina. We found South Carolina is performing well in some areas; however, there are many opportunities for improvement.

Where We Are Succeeding

We commend the General Assembly for answering the call to pass legislation strengthening our state's DUI laws. We believe the enactment of H.3496 in 2008 will help reduce the number of alcohol-related highway fatalities in the state. We plan to improve enforcement of drunk driving laws by continuing to increase highway traffic enforcement through the funding of new officers for the fourth year in a row. This year, we propose maintaining the current level of funding for Highway Patrol officers, continuing our administration's attempt to reverse years of field officer declines at the Department of Public Safety. For example, the number of commissioned Highway Patrol officers was at an all-time low just five years ago, but if the General Assembly had followed our budget recommendations the last two years, the number of troopers would be at an all-time high.

The Department of Public Safety has reported that South Carolina once again decreased the number of alcohol-related highway fatalities. According to an annual NHTSA report, South Carolina showed a slight decrease in the number of alcohol-related fatalities, dropping from 523 in 2006 to 512 in 2007. While the state remains well above the national average for percentage of highway fatalities involving alcohol, we are making continued progress. We believe the legislation we signed this year will help continue this progress.



In 2007, we enacted a law stating that South Carolina would not participate in the implementation of the federal REAL ID Act. This unfunded mandate by the federal government would force every state to issue licenses in a uniform format and contain uniform information. Implementation of the program would increase DMV workloads by 132 percent and push wait times to over an hour, while costing the taxpayers of South Carolina \$25 million in startup costs and \$11 million on an annual basis.

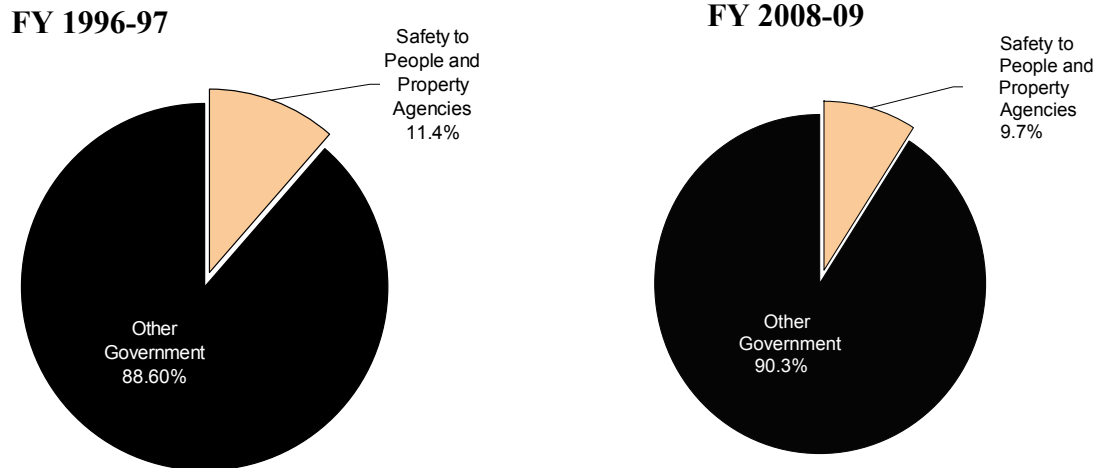
In March, the Department of Homeland Security attempted to force every state to comply with REAL ID by threatening to not accept a state's driver's license for identification purposes to enter a federal building or board an airplane unless the license was REAL ID compliant. We resisted this tactic, and our citizens can still use their driver's license as a valid form of identification for federal purposes. We encourage the General Assembly to continue to resist REAL ID and every state to join South Carolina in opposing this top-down federal mandate.

Last year in the State of the State address, we called for the General Assembly to pass strong immigration reform. While the federal government has failed to tackle this problem, states have been forced to take what action they can to combat illegal immigration. In May, after much debate, the General Assembly finally passed a bill that included what our administration had called for all along – strong worker verification requirements. South Carolina became only the third state to require employers to use E-Verify, a free program run by the Department of Homeland Security, to check the legal status of their employees. We commend the Legislature for taking this action.

Our administration has been very vocal about our belief that South Carolina must reduce the number of domestic violence incidents. To assist in this effort, our administration signed a bill allowing courts to recognize domestic violence convictions in other states when judges are sentencing offenders in South Carolina.

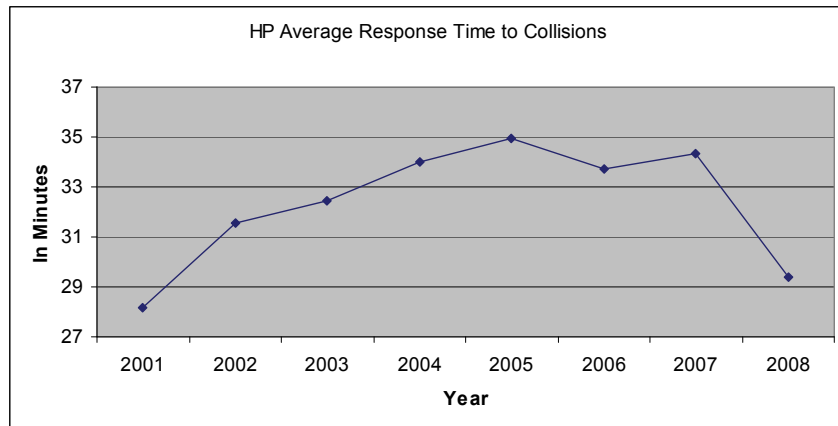
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From FY 1996-97 to FY 2008-09, the major law enforcement and correctional agencies (SLED, SCDC, PPP, DJJ, DMV, DPS, and DNR) saw their budgets – as a percentage of the overall state budget – decline by 2.63 percent.

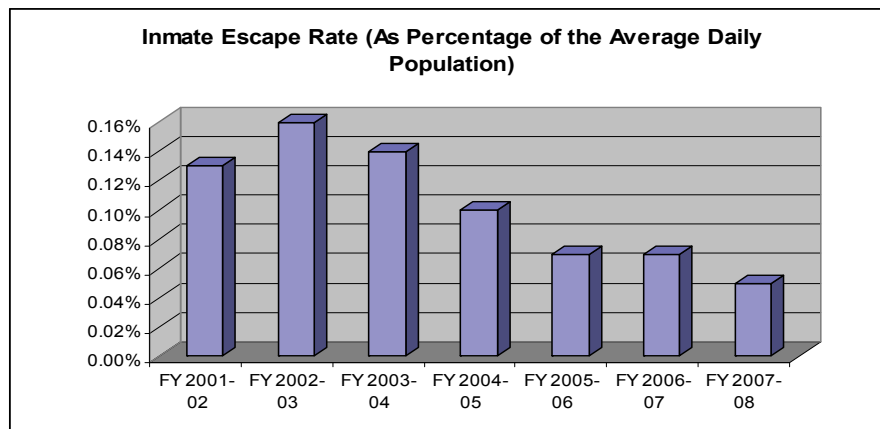


This reduced percentage of the overall budget resulted mainly from a “crowding out” of funds available to the major law enforcement and correctional agencies due to significant growth in the state’s other core areas – primarily health care and education. The impact of this reduction is a decrease in the ability of law enforcement agencies to retain staff and the inability to replace older, broken-down equipment.

Despite receiving a smaller portion of the state’s budget, South Carolina continues to make progress in several of the established indicators to improve the safety of people and property. For example, decreases in the average response time to collisions, the mileage death rate, and the drunk driving fatality rate indicate continued progress in the administration’s goals to *decrease preventable injury and loss, increase emergency response and recovery, and increase citizens’ confidence in their safety*. The state made additional improvements in *increasing citizens’ confidence* regarding forensic casework management, vehicle crime property recovered, and fugitives arrested.



South Carolina is also making incremental gains in terms of *managing offenders* based on decreases in the state's inmate escape rates. These gains come even though South Carolina has a sizable prisoner incarceration rate of 526 prisoners per 100,000 population. The state's prisoner incarceration rate ranked 8th in the nation and 7th in the Southern region. Due to managerial and policy changes, the state's inmate escape rate at the Department of Corrections has declined from 0.16 percent in 2002 to 0.05 percent in 2007.



Department of Juvenile Justice (DJJ) reports that its Broad River Road Complex, which houses the state's most serious long-term committed juvenile offenders, has been escape-free for nearly five years.

The Department of Corrections recently executed a contract for energy savings at five of its institutions with a private company. The department will reap the benefit of \$6 million in new, energy efficient equipment at no cost to the taxpayers. After 12 years, the state will benefit from an

FY 2009-10 Executive Budget

estimated annual savings of well over \$1 million in reduced energy costs. The estimated total net savings to the taxpayers will be \$11 million over the next 20 years in reduced energy costs.

The combined assault rate at the Department of Corrections – the number of inmate assaults on fellow inmates, inmate assaults on guards, and inmate assaults on other persons – has decreased from 4.3 percent in FY 2004-05 to 3.7 percent in FY 2007-08.

Additional offender management success is reflected in DJJ's School District receiving an "excellent" rating for the fifth consecutive year, as well as an "excellent" improvement rating for the fourth time in the last five years. With these ratings, DJJ received a Palmetto Gold Award for the sixth consecutive year.

Within its school district, DJJ emphasizes academics and basic literacy to increase youth capacity for future productivity. The number of youth earning their GED Certificates has improved dramatically since school year 2003. The 170 GEDs earned by DJJ students in FY 2007-08 represents a five-year high, up from 104 in 2003. The DJJ average for completing the GED is 64 percent compared to the state average of 59 percent.

DJJ measures to alleviate overcrowding and meet minimal constitutional standards to ensure the safety of juveniles within its facilities have resulted in a significant decrease in the number of lawsuits brought against the department. In 2003, DJJ had 31 pending lawsuits brought by inmates in its care, and 12 additional lawsuits were brought by inmates in FY 2004-05. Currently, there are no pending lawsuits against the agency.

DJJ's community division now has 35 Teen After-School Centers (TASC) in 26 counties sponsored by churches, non-profits, a law enforcement agency, a municipal government agency, and a public school. The centers provide safe places for recreation, tutoring, mentoring, and cultural enrichment during hours when youth are most at risk to engage in delinquent behavior. TASCs served 506 youth in FY 2007-08. DJJ's partnerships with the African Methodist Episcopal (AME) Church, the Women's Missionary Union of the South Carolina Baptist Convention, and Brookland Baptist Church in West Columbia have brought to the agency a host of resources including donations, volunteers, auxiliary probation officers, and donated space/sponsorship for employment program sites and teen after-school centers.

DJJ is also succeeding in preventing juvenile recidivism while serving probation or parole or completing arbitration programs. DJJ reports that 86 percent of juveniles in community programs did not re-offend while under DJJ supervision.

The South Carolina Department of Natural Resources (DNR) plays a vital role in ensuring citizens are safe as they enjoy the outdoors of our state. In FY 2007-08, DNR's Law Enforcement Division identified and resolved 34,772 safety violations. DNR's management accountability initiative and the recent increase in field officers have greatly improved DNR's ability to effectively protect our state's resources. The increased number of field officers has also provided over 12,000 man-hours of support to law enforcement agencies that prosecute public safety violations and conduct search-

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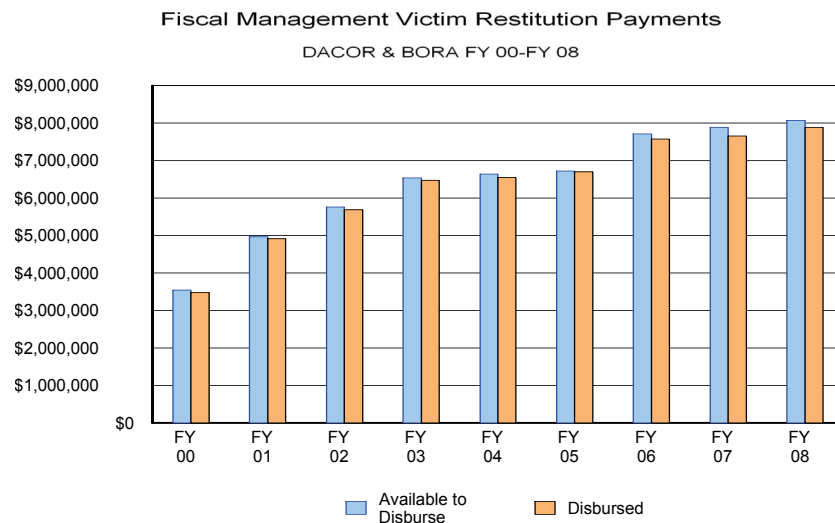
and-rescue operations. Finally, DNR's hunting and boating safety classes, which drew over 18,000 students last year, exhibit DNR's proactive approach to public safety.

SLED has also made progress in *increasing citizens' confidence in their safety*, based upon several achievements realized at the South Carolina Law Enforcement Division's Forensic Laboratory, the Vehicle Crime Unit, and the Fugitive Task Force. During FY 2007-08, case backlogs were reduced in seven of the forensic laboratory units, and forensic laboratory personnel were able to complete over 19 percent more cases compared to the number of cases completed the previous year.

SLED has steadily increased the number of criminal DNA profiles that it maintains from 63,300 in FY 2005-06 to 87,163 in FY 2006-07, to 125,206 in FY 2007-08 – a 43 percent increase from the previous year. Due to this increase, over the same period of time, the number of offender hits increased from 258 in FY 2005-06 to 406 in FY 2006-07 to 709 in 2007-08 – a 74 percent increase from the previous year.

During FY 2007-08, the Vehicle Crime Unit at SLED conducted 492 investigations, made 153 arrests, and recouped approximately \$5.3 million in stolen property. The Fugitive Task Force investigated 362 cases, which resulted in the arrest of 346 fugitives.

Another example of success is the victims' restitution program managed by the Department of Probation, Parole, and Pardon Services (PPP). PPP has steadily increased the total dollar amount of restitution payments collected and disbursed to victims. Last year PPP collected and disbursed \$7,887,339 to victims. Since July 1, 1998, PPP has collected and disbursed \$58,169,525 to victims.



Opportunities for Improvement

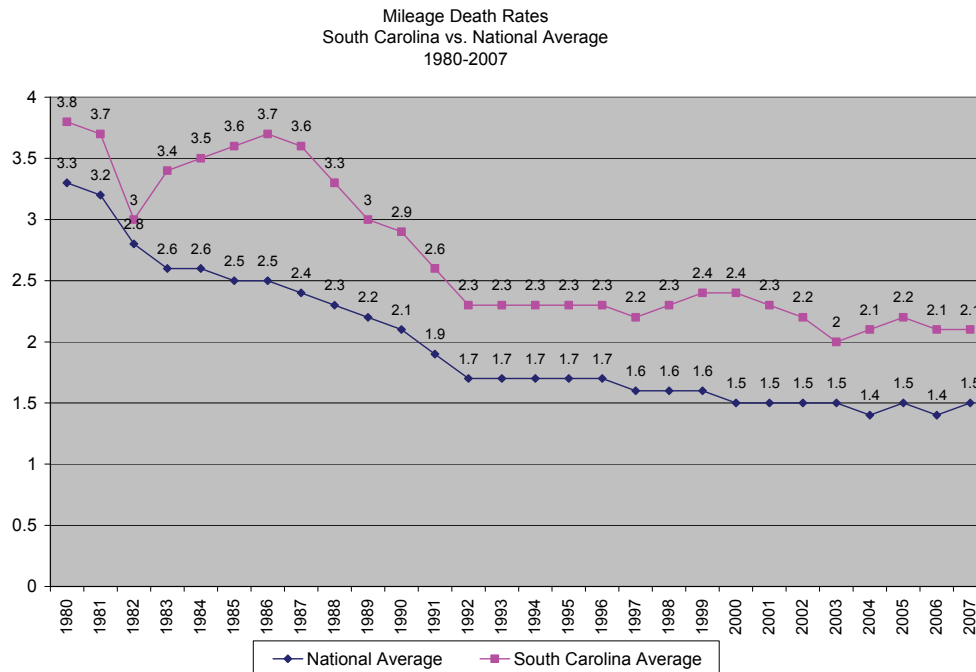
South Carolina must still improve in a number of critical areas to achieve our goals for public safety. As previously mentioned, the FBI recently ranked South Carolina as the state having the highest

violent crime rate in the nation – trailing only Washington, D.C. According to the FBI, during 2007, the nation’s violent crime rate per 100,000 population dropped by approximately 1.4 percent, while South Carolina’s violent crime rate per 100,000 population increased by 3 percent. This statistic decreases *citizens’ confidence* in the public safety of their state.

With regard to *preventable injury and loss, emergency response and recovery* and *citizens’ confidence*, the number of alcohol-related fatalities has fallen over the past several years, but the state is still experiencing a spike that began in the late 1990s. South Carolina’s ratio of alcohol-related fatalities to overall fatalities is among the highest in the nation. As such, we remain committed to greater reduction in alcohol-related traffic deaths and have taken steps toward reducing such deaths by promoting tougher DUI laws in our state.

South Carolina’s mileage death rate (MDR), defined as the number of traffic fatalities per 100 million vehicle miles of travel, continues to be higher than the national average. While there was a reduction of highway deaths in 2006, there was an increase of 33 fatalities in 2007 – leaving the state’s MDR at 2.1 for the second consecutive year.

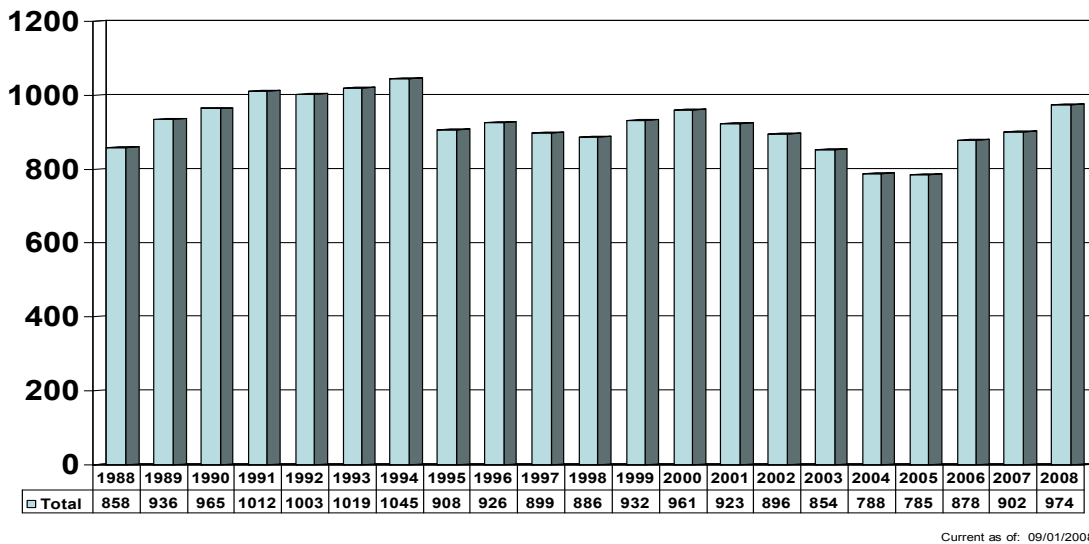
MILEAGE DEATH RATE South Carolina vs. National Average



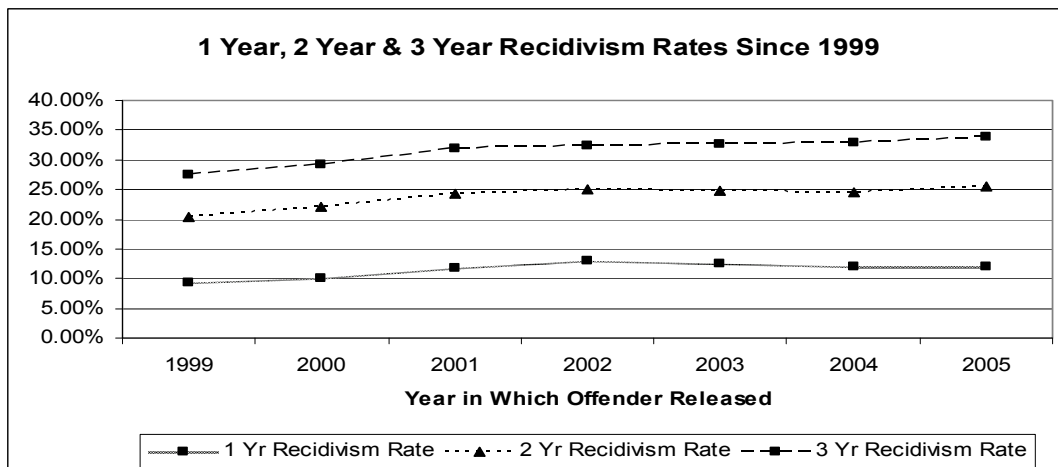
Highway officers currently patrol over 66,248 miles of state roadways, enforce traffic laws, investigate collisions, assist motorists, and provide a safe motoring environment for the public. An

increase in troopers will help combat the state's high drunk driving rate as well as improve the response time to collisions.

Highway Patrol Commissioned Officer Manpower



Improvements are also needed in South Carolina's adult recidivism rates. The percentage of re-offenders from those who have spent time in the state's correctional system has risen steadily since 1999. While the state's recidivism rate of 33.9 percent is close to the national rate of 33.8 percent, it remains too high, particularly when compared with recidivism statistics from previous years.

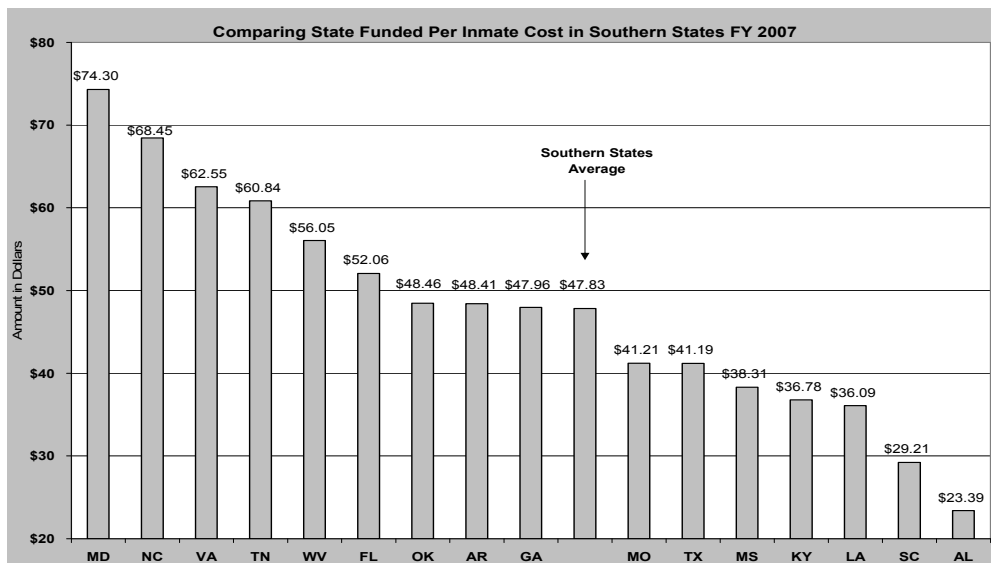


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With an incarceration rate that ranks 8th in the nation, we once again encourage legislators and corrections officials to explore alternative sentencing in our criminal system. The cost of maintaining prison facilities continues to rise, leaving our state with two options: increase funding to construct and staff new prisons or find different methods of punishing and rehabilitating criminals. To help explore the sentencing structure of our criminal system, the Legislature created an independent commission to study sentencing guidelines, the parole system, and alternative sentencing procedures for nonviolent offenders. We commend them for taking this action and are hopeful this committee will produce legislation that will bring much needed reform to our sentencing system.

While the Legislature recognizes the need to reform our sentencing procedures, it has failed to recognize the importance of adequately funding our prison and probation system. Despite continued underfunding, the agency has accomplished remarkable efficiencies – from a workforce that is 20 percent smaller, to producing its own eggs and grits, to leveraging the buying power of the State Health Plan and HHS to reduce medical costs. In fact, it is telling that critics of the agency have been unable to point to a single prison system across the 50 states that does more with less in any functional area. The Department of Corrections has gone beyond mere efficiency, reducing escapes and assaults and setting new records for GED completions. However, for too long, the state budget process has punished the good performance of this agency. As we did last year, our request this year would end that practice, fund corrections as a core function of government, and avoid another year of deficit spending.

South Carolina ranks second to last in the Southeast in funding per inmate per day at \$29.21 (Southeastern average is \$47.83) – a trend that must end.



Likewise, the Department of Probation, Parole and Pardon Services has seen the portion of its budget that is composed of general funds decline from 59 percent in FY 2000 to 38 percent in FY 2009. This forces PPP to rely upon the collection of fees to run the agency – an unreliable source of revenue. Fees are particularly difficult to collect from offenders during difficult economic times. We believe PPP needs to be funded by a more reliable revenue source – a higher percentage of general funds.

Purchasing Priorities

The major funding priorities are those that we feel best achieve our goals. The four key purchasing strategies, as determined by the FY 2009-10 Safety to People and Property results team, are defined as follows:

Prepare for and prevent criminal activities and natural and/or man-made events. To ensure that an agency is prepared to prevent or manage criminal activity and natural or man-made disasters, it must be adequately staffed, equipped, trained, and have a proven, executable plan in place to deliver its services.

Effectively manage the state's offender population. The goal of effectively managing offenders is the same as the crime prevention goal – reduce the risk of harm to people and property that are either associated with, or come in contact with, criminals.

To provide for the enforcement of state laws. The primary focus of this strategy is to ensure that agencies possess the tools necessary to enforce the laws of South Carolina. For example, additional law enforcement officers can prevent crime, resulting in greater compliance with state laws. The State Law Enforcement Division recognizes the need to address violent crime in our state. SLED will continuously reprioritize mission capabilities during these difficult economic times in an effort to address this substantial need. An example of this strategy includes embracing the formation of collaborative interagency law enforcement teams (local, state and federal) to better deal with violent crime in our state.

To provide for response and recovery activities following criminal activities and natural or man-made events. Once an event occurs, be it a criminal activity or a disaster, the state must be prepared to quickly execute a response and recovery plan. A recovery and response plan may include activities such as criminal investigations, responses to traffic accidents, and disaster cleanups. An effective plan will increase the public's confidence in its safety.

Governor's Purchasing Plan – Highlights

As we address our state's unprecedented financial problems, it is important to focus on purchasing only those public safety services most needed by our citizens. In many cases, we have had to use cost savings methods to simply maintain current funding levels for high priority services. We do not purchase services that, while still considered valuable, have been identified as lower priority. The following table identifies key purchases within our executive budget's total state public safety spending plan as well as examples of what is not purchased. Detailed highlights of our purchasing plan are provided below the table.

<p><i>Improve the Safety of People and Property</i></p>	<p><u>Examples of what our plan buys:</u></p>
<p>Purchasing Plan:</p>	<ul style="list-style-type: none"> ▪ Highway patrol troopers that will assist nearly 100,000 motorists and enforce commercial motor vehicle laws ▪ Resources for incarceration of 23,958 adult criminals ▪ Supervision of 47,797 adult jurisdictional offenders upon orders of the courts or Parole Board ▪ Increased funding for drug testing of offenders ▪ Funding for a Domestic Violence Fatality Review Project pilot program ▪ \$45 million to pay down the deficit at the Department of Corrections in FY 2009-10 ▪ Funding for implementation of Ignition Interlock and Alcohol Enforcement Teams aimed at reducing underage drinking
<p>\$593,458,301 General Funds</p>	
<p>\$1,059,351,519 Total Funds</p>	
<p>Savings Proposal:</p>	<p><u>Examples of what our plan does not buy:</u></p>
<p>\$42,423,090 General Funds</p>	<ul style="list-style-type: none"> ▪ Reduced food service expenses at the Department of Corrections associated with the implementation of the Egg-Laying/Pullet House, the Freezer Warehouse, and the Dairy Operations projects ▪ Duplicative parole boards for youths and adults

Our Plan Buys:

Funding to pay down the deficit at the Department of Corrections in FY 2009-10. Due to a lack of funding by the General Assembly, the Department of Corrections was forced to run a \$45 million deficit in FY 2009-10. We propose including **\$45 million** to pay down this deficit.

Troopers and state transport police officers to patrol over 66,248 miles of state highways and enforce traffic laws, investigate collisions, assist motorists, and provide a safe motoring environment for the public. During FY 2007-08, these troopers assisted 86,174 motorists, issued 9,671 DUI tickets, and investigated 77,726 collisions. Enforcement of commercial vehicle laws by State Transport Police (STP) resulted in driver violations totaling 41,196 with 1,882 drivers placed out-of-service, and vehicle violations totaling 48,862, with 5,595 vehicles placed out-of-service. We propose to **maintain recurring general funding of \$68.8 million** for this activity. The troopers will continue to help combat the state's high drunk driving rates as well as lower the Highway Patrol response time to collisions.

Funding for a Domestic Violence Fatality Review Project pilot program. In January 2006, the South Carolina Domestic Violence Fatality Review Task Force issued its report which recommended establishing the Domestic Violence Fatality Review Project. This program, which has been successful in other states, aims to formulate recommendations for collaboration on domestic violence investigation, intervention and prevention by coordinating with locally based review panels. Once again, we propose **providing non-recurring funding in the amount of \$100,000** to establish this pilot program.

Funding for incarceration of 23,958 adult offenders at the state's seven high-security, eight medium-security, eleven minimum-security, and three female institutions. These services provide for the proper housing, care, treatment, feeding, clothing, and supervision of inmates within a controlled and structured environment. We propose **maintaining general funding of \$342.7 million** for this activity.

Community Supervision of 47,797 adult jurisdictional offenders. These services include the regular supervision of adult jurisdictional offenders upon the orders of the courts or the PPP's Parole Board. In order to protect the safety of our agents in performing their duties, it is essential that the proper safety and equipment be provided. We propose to **increase recurring funding** for this activity by providing **\$150,000 in general funds** during FY 2009-10. This funding will replace safety items such as flashlights, holsters, and firearms. By replacing the department's weapons, we can provide agents with reliable weapons and reduce the costs of repair and upkeep.

Offender Drug Testing Programs. Probation, Parole and Pardon Services is required, by court order in some cases, to administer regular drug tests to offenders. However, lack of funding has made it difficult to perform this function, forcing funds to be taken from other activities. In FY 2007-08 PPP conducted 105,833 drug tests, with the cost being paid out of "other funds." We propose **increasing recurring funding** for this activity by **\$150,000** so all drug testing is completed to ensure that offenders are rehabilitated before completing probation.

Implementation of Ignition Interlock. On June 15, 2007, we signed into law the Prevention of Underage Drinking and Access to Alcohol Act. The Act establishes Alcohol Enforcement Teams aimed at reducing the incidents of underage drinking. Also included in the Act are provisions requiring the use of ignition interlock devices for second and subsequent DUI offenses. Offenders are required to have their device inspected every sixty days and the data from this inspection sent to PPP. The revenue collected from the participants can be deposited into the Ignition Interlock Fund, thereby allowing the Fund to generate a cash balance that can be used to cover program expenditures for future years.

Our Plan Saves By:

Charging for traffic control services. The Department of Public Safety provides traffic control services at various events throughout the year – most notably football games. Proviso 49.1 restricts the department from charging for these services. We recommend removing this proviso and allowing the department to charge for providing traffic control services in FY 2009-10. This change will lead to **cost savings of \$983,133 annually** in general funds.

Reducing expenses associated with food services at the Department of Corrections. In the FY 2004-05 Appropriations Act, the General Assembly included a proviso that allowed the Department of Corrections to secure private funding to build three egg-laying houses so that the Department could become self-sufficient with its egg-based needs. While the initial goal was self-sufficiency, early estimates pointed to a project that would generate excess cash which could then be used to reduce the general fund needs of the agency. In addition to the egg-laying operation, the agency has sought to achieve self-sufficiency in its dairy operations. In the FY 2005-06 Appropriations Act, the General Assembly included a proviso that allowed the Department to secure private funding to construct and maintain a dairy operation. Noting these initiatives, our budget proposes a two-year phase out of the general fund needs for agricultural operations at the Department. When factoring in the projected annual cost of production and estimated debt service for these projects, the agency should be able to **save \$100,000 annually** in general funds.

Combining Parole Boards at DJJ and PPP. Currently, the state has separate boards at PPP and DJJ. The parole board at PPP has seven members and a budget of \$699,350, while the DJJ board has a budget of \$806,862 with ten members. Despite having a larger budget, the DJJ board hears far fewer cases per year. Because these two parole boards have very similar missions, we feel this presents an opportunity to gain efficiencies and savings by merging them. Combining the two boards will **save \$425,000 annually** in general funds.

Making Tough Choices:

Given the state's finite amount of resources, we had to make some difficult choices regarding which activities to fund or not fund. While the activities listed below may well have merit, when comparing them with other activities, we did not think their anticipated outcome would be as effective in achieving our goal. Due to the budget cuts that the public safety agencies have already sustained, and the core function of state government that public safety represents, we are not proposing additional cuts to these agencies. However, the following is one example of a difficult choice:

Seeking alternative funding for the Adjutant General's Operations and Training and Public Information activities will result in a **reduction** of **\$125,288** in recurring general funds. We encourage those maintaining this unit to seek other funding in order that this service may continue. Crowd control is part of the core mission of the National Guard. We recommend that funding for this activity come from its base appropriations.

Please see the Appendices for a complete listing of the Governor's Purchasing Plan for this goal area and for a detailed listing of what our plan saves and what our plan does not buy.

Improve the Efficiencies and
Effectiveness of Central State
Government Support and Other
Governmental Services

Improve the Efficiencies and Effectiveness of Central State Government Support and Other Governmental Services

State government's antiquated structure prevents it from providing the most efficient and effective services to taxpayers. Our administration thinks it is past time to release government from the shackles of the past by changing the policies and structures of specific agencies as well as government statewide.

Examples of this antiquated system of state government include an executive branch structure where only 15 of more than 70 executive agencies report directly to the governor; more than 2,000 different, uncoordinated computer servers spread across state agencies; a multitude of separate accounting systems used by each member of the cabinet, non-cabinet, "quasi-legislative" Budget and Control Board, and higher ed agencies that take additional technologies to communicate effectively; and a Chief Information Officer (CIO) who reports to a board of five different elected officials and has little authority to effectively manage information systems in this state.

Government should be most accountable to those who pay for it – the taxpayers. This administration continues to push for policies that will provide an efficient and effective government that maximizes value to taxpayers. A good first step in this process would be creating a Department of Administration within the governor's cabinet, which would perform the administrative functions currently performed by the Budget and Control Board. In this section of the budget, we propose ways to improve the structures and policies of central state government and other governmental services that will make them operate more efficiently and effectively.

Developing Our Purchasing Priorities

To develop our purchasing priorities, we first determined major indicators of success related to the goal of improving the structures and policies of central state government. These indicators measure whether state government is currently reaching its goal of operating efficiently and effectively. We found South Carolina is performing well in some areas; however, there are many opportunities for improvement.

Administration's Goals for Improving the Efficiencies and Effectiveness of Central State Government Support and Other Governmental Services are to:

- ✓ Reduce fractured lines of responsibility in the executive branch of government.
- ✓ Modernize state information technology regulations to improve cost efficiency to state agencies.
- ✓ Manage state-owned assets more cost effectively.
- ✓ Centralize state accounting systems to improve productivity.
- ✓ Fix our retirement system so it can meet its obligations.

IMPROVE THE EFFICIENCIES AND EFFECTIVENESS OF CENTRAL STATE GOVERNMENT SUPPORT AND OTHER GOVERNMENTAL SERVICES

Where We Are Succeeding

The South Carolina Department of Revenue (DOR) continues to be a national leader in the percentage of individual income tax returns that are filed by electronic/non-paper methods. In June 2008, the Federation of Tax Administrators reported that 71 percent of all South Carolina taxpayers filed their tax returns electronically over the last year. That means that more than 1.3 million South Carolina taxpayers are filing by computer, which is an increase of 152,410 over last year. South Carolina's high percentage of electronic filing keeps South Carolina as one of the top ten states for electronic filing.

The increase in electronic filing in the last year is partly due to DOR's efforts to provide free filing for all South Carolina taxpayers who earn \$30,000 or less, who are 65 years of age or older, and who are students. DOR was able to provide this benefit by joining the Free File Alliance, which is a group of 20 states that have partnered with private software companies to provide free tax filing services. DOR estimates that approximately 45,000 taxpayers were able to take advantage of the free file program in 2008.

As a result of DOR's efforts on this front over the last several years, many South Carolinians have begun filing their tax returns earlier in the year. DOR reached the one-million-electronic-filer milestone on March 24th in 2008, whereas it did not reach this mark until April 4th in 2007. Filing earlier allows taxpayers to get their tax refunds earlier. In sum, DOR's efforts have saved significant cost and time for the agency, the state, and the taxpayer.

In addition, DOR, working with the Department of Commerce and other key agencies, has done an outstanding job in implementing and being the primary operator of South Carolina One Stop for Business (SCBOS). It goes without saying that bringing new industries into the state leads to new jobs, and many of these jobs are created by the very backbone of our economy – small businesses. Over 97 percent of all businesses in South Carolina are small businesses. They stimulate economic activity, attract capital investment, and, most importantly, create new jobs. This focus on small businesses and providing an environment for them to succeed is important for our state to remain competitive.

In each of the four years prior to this administration, more businesses closed than were created – with over 3,500 total businesses shutting their doors. But in each of the past four years, more businesses have been created than lost – with over 3,000 total businesses opening their doors. This administration realizes the need to equip the small business community with the necessary tools to succeed in this global economy. Specifically, SCBOS guides potential new business owners through the process of starting a business while making it easier for existing business owners to file and pay for business licenses.

Opportunities for Improvement

On February 26, 2007, Governor Sanford issued an executive order creating the nine-member Government Efficiency and Accountability Review (GEAR) Committee. The committee was instructed to “analyze the systems and services within and provided by the South Carolina Budget and Control Board in an effort to propose changes which will reduce costs, increase accountability, improve services, consolidate similar functions, return functions to the private sector and help South Carolina become more competitive in a world economy.” The committee’s report examined how the Budget and Control Board and other areas of state government could streamline their operations and save the taxpayers over **\$500 million**. To date, the Budget and Control Board and the General Assembly have either implemented or are in the process of implementing 16 of the committee’s 61 recommendations to improve central state government. We commend the Board and the General Assembly for taking these steps; however, the rest of the recommendations need to be implemented to better serve the taxpayers of South Carolina.

In 2008 the General Assembly came close to passing legislation that would have placed purely administrative state government functions under a cabinet-level Department of Administration. While the House passed this bill unanimously, the bill died on the Senate floor in the closing days of the session. We once again call on the General Assembly to pass this meaningful legislation that will help modernize state government.

There are many areas in government where we can be better stewards of the taxpayers’ money by providing services in a more efficient and effective manner. One of the primary areas that should be looked at is state travel. The Legislative Audit Council (LAC) report on state travel, released in July 2007, reveals numerous areas where we are not being cost efficient. The LAC report noted, “There is no centralized office that is responsible for managing travel by South Carolina state agencies to ensure that travel expenditures are efficient and cost effective.” The report states that a centralized office could “use its volume of travel to reduce costs, improve communication and training about travel policies, and develop expertise in travel practices.” For example, a centralized state travel office could negotiate and purchase bulk travel from hotels, conference centers, and airlines. The LAC report estimates that the annual cost savings to the taxpayers would be **\$1.6 million** if the state used its bulk purchasing power to obtain contracts with airlines.

The administration continues to push for more flexibility in the human resources policies of state government. Currently, our managers do not have the tools needed to run agencies effectively. Outdated regulations tie the hands of directors, preventing them from getting the most out of their employees. In fact, we have a system that makes it virtually impossible to remove that employee from the state payroll after a standard probationary period. This has created a government with only two percent of employees being “at-will,” which is almost unheard of in the private sector.

The number of state employees in South Carolina is higher than the regional and national averages partly because of inefficient human resources policies. A recent *Governing* magazine comparison of state employees showed that South Carolina has 234 employees per 10,000 in population, which is 35 percent more than the national average of 174 state employees per 10,000 in population. By

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comparison, North Carolina had 229, Georgia 179, Texas 157, and Florida only had 120 employees per 10,000 in population – almost half that of South Carolina. We suggest updated human resource regulations and more efficient administrative policies are needed to put us in line with the rest of the nation.

One policy that is vital to reducing the number of employees to a more efficient level is to address the rehiring of prior employees who enroll in the Teacher and Employee Retention Incentive (TERI) program. Agencies have an opportunity to demonstrate fiscal prudence with the taxpayers' money by rehiring TERI employees only in extreme cases. By the end of FY 2007-08, almost 800 state employees will be set to leave the TERI system. However, current law allows an agency to rehire the former TERI employee if he or she is separated from the agency for only one day. This scenario forces the taxpayer to pay an employee's salary in addition to an employee's retirement package. For this reason, we are recommending that agency directors evaluate former TERI employee job duties to determine if they may be distributed among others in the agency, while also looking to hire qualified individuals that may be trained for the long run. According to numbers from the Human Resource Office in the Budget and Control Board, if each agency's budget were reduced by taking the difference between the average TERI employee salary and the average salary for that agency, an annual cost savings of **\$17,180,713** in general and other fund dollars would be provided.

Over the last year, we made some progress in improving the way we fund health care for state employees. Upon our initiative, the Budget and Control Board adopted an incentive that provides employees with a twenty-five dollar premium discount if they do not use tobacco, which we believe will reduce health care costs in the long term by discouraging smoking. Also, upon the GEAR Committee's recommendation, we signed into law the creation of a trust fund for health care benefits for future retirees. This fund will allow the state to invest current funds to help fund future health care costs. Nevertheless, the state currently has an **\$8.5 billion** unfunded liability for future retiree health care. This is a situation that we need to improve, and our budget contains costs savings for the State Health Plan that will save approximately **\$21.1 million** annually.

Purchasing Priorities

Having determined where we are succeeding and where opportunities for improvement exist, we next identified some proven or promising strategies to determine our purchasing priorities and best achieve our goals. The key strategies we identified are as follows:

Provide effective and efficient central state human resources support. Managers and employees need more flexibility to provide effective service to citizens in the 21st century. Our proposed changes to human resources regulations and staffing will save taxpayers money and increase managers' ability to change their agencies' staffing plans as changing circumstances require. We would push to modernize state human resources regulations to improve efficiency.

Provide effective and efficient central state information technology support. Many agencies across the state are not using the most efficient means in maintaining their websites and other technological

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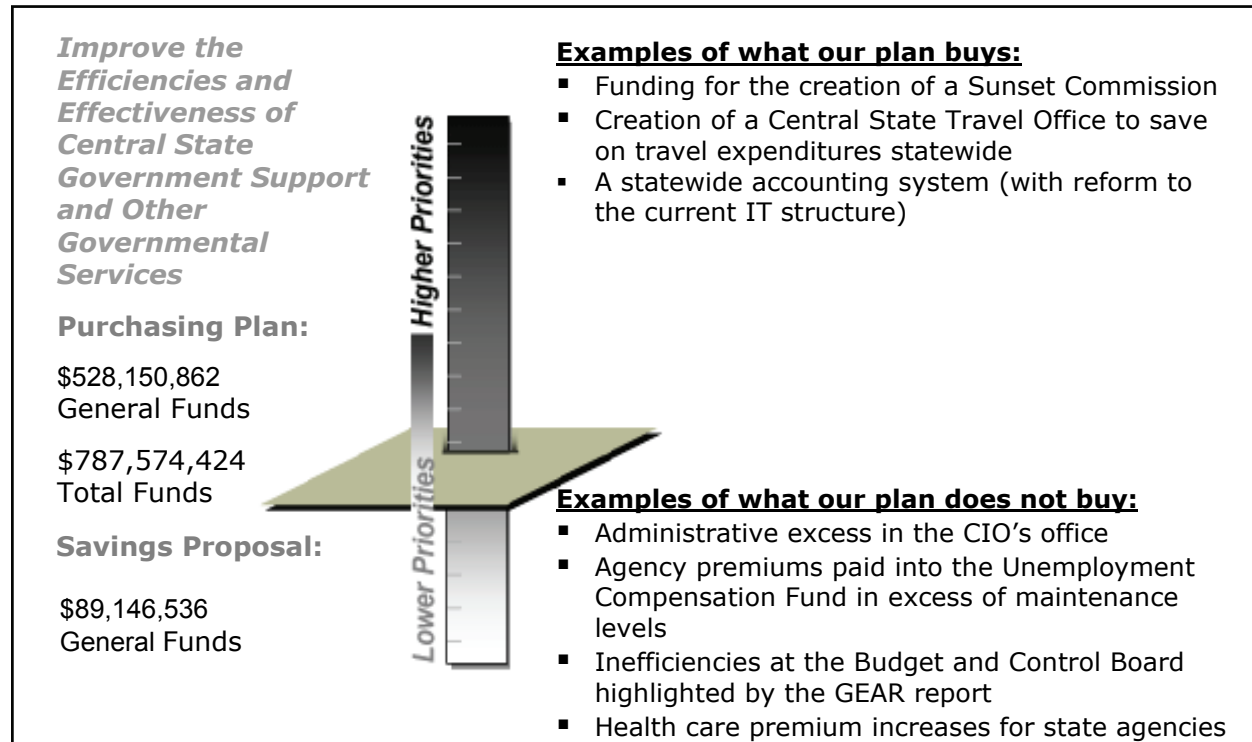
operations. With the recent contractual agreement between South Carolina Interactive and the state, it is essential that South Carolina Interactive effectively market the benefits of online services that will save the state and taxpayers money. We would push to reduce technology costs that all state agencies are forced to pay.

Provide effective and efficient central state administrative support. By disposing of excess property and co-locating state agencies that deal directly with the public, citizens can take care of state business without having to search through a myriad of locations. We will continue to push for a more cost-efficient method to operate our fleet of vehicles across the state – including cost savings from recommendations in the recent vehicle study. We will also push to create a system that is more efficient regarding state-owned assets.

Provide accountability to the citizens of South Carolina in all state government services. We need to pass restructuring legislation to make the executive branch more accountable to taxpayers. Our restructuring proposal is a step in the right direction toward making key functions of state government, primarily health care, education, and administration, answerable to the Governor's Office and thus to voters. It is imperative that we reduce the fractured lines of responsibility in the executive branch of government.

Governor's Purchasing Plan – Highlights

As we address our state's unprecedented financial problems, it is important to focus on purchasing only those central state administrative functions most needed by our agencies. In many cases, we have had to use cost savings methods to simply maintain current funding levels for high priority services. We do not purchase services that, while still considered valuable, have been identified as lower priority. The following table identifies key purchases within our executive budget's total state administrative services spending plan as well as examples of what is not purchased. Detailed highlights of our purchasing plan are provided below the table.



Our Plan Buys:

Establishment of a Sunset Commission to evaluate whether government programs should be continued. In the past, the House of Representatives has adopted a measure which would have created a Sunset Commission as described earlier in our "Modernize Government" section. In 2008, the Senate appeared ready to adopt a legislatively-controlled version of a Sunset Commission, which we supported. We hope the General Assembly will reconsider this much-needed commission especially in light of our current fiscal crisis. Our budget provides **new funding of \$585,000** for the creation of a Sunset Commission.

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Tax collections, compliance, and processing. In recent years, our cost to collect taxes has been reduced to \$.00678 per dollar. At the same time, enforced collections now exceed \$300 million, with total collections exceeding \$6 billion. Noting this, we propose to **maintain funding at \$6,134,587** in general funds for tax collections, compliance, and processing during FY 2009-10.

Taxpayer assistance. Taxpayer assistance includes the Contact Center as well as regional and satellite offices that provide statutory compliance with registration, licenses, and explanation of correspondence and forms. Taxpayers need a clear, trustworthy channel of communication to answer questions about their taxes. We propose to **maintain funding at \$3,680,753** in general funds for taxpayer assistance during FY 2009-10.

Statewide budget development analysis and implementation. The Budget and Control Board's Office of State Budget (OSB) assists the governor and General Assembly in the preparation and implementation of the annual state budget. We propose to **maintain funding at \$2,527,542** in general funds for the OSB during FY 2009-10.

A Central State Travel Office. The LAC recently reported that inefficiencies in managing state travel are a result of our state not having a centralized office responsible for ensuring that agency travel expenditures are cost effective. This type of office will use the state's high volume of travel to reduce costs and oversee each agency's travel practices. Specifically, the newly created Central State Travel Office within the Comptroller General's Office, in conjunction with the Office of Procurement, will establish strict guidelines to ensure that each agency adheres to the contractual agreements established with airlines and hotels. We feel that the creation of this office will be consistent with the idea of utilizing taxpayer dollars in the most efficient manner for state travel needs. It will also be the responsibility of this new office to generate savings by negotiating bulk airline and hotel/motel purchases.

Other states, such as Louisiana and Mississippi, and the federal government have a central office that handles travel. Currently, Mississippi's central travel office consists of one employee. It is time for South Carolina to fall in line with the travel practices of other states and the federal government – as a centralized travel office will produce more efficient agency travel and save taxpayer money. Our budget provides **new funding of \$50,000** for the creation of a Central State Travel Office.

An integrated financial reporting and management system for the state, which is essential to standard and meaningful multi-year technology planning. In previous years, we have indicated our concerns with implementing the South Carolina Enterprise Information System (SCEIS) without reforming the structure of the Division of State Information Technology (DSIT) office and the responsibility of the state's Chief Information Officer (CIO). A CIO in our proposed Department of Administration would lead to innovation in technology, strategy, and oversight. A strengthened CIO could ensure cost-effective, reliable delivery of technology infrastructure and services, as well as governance that involves all stakeholders in technology decision-making in state government. A CIO accountable to one person rather than a board is also critical to successful implementation of the SCEIS project.

While this project offers a potential of up to \$120 million dollars in annual work process savings after five years of implementation, it also brings the potential for significant cost overruns and failure if not managed properly. Under the current structure, the CIO answers to the Director of the Budget and Control Board, who answers to five separately elected officials. In a report assessing the state's management of IT, the Gardner Group finds South Carolina to be the only state in the Southeast or the Middle Atlantic that has a CIO position with narrow influence and with structurally deficient depth of support.

If a restructuring plan to make the CIO more accountable to the governor is adopted by the General Assembly next legislative session, we will support **maintaining funding** in the amount of **\$5,689,821** for the continuation of completing the five-year SCEIS project. We believe this is a significant opportunity to reform South Carolina's government and make it more efficient.

Our Plan Saves By:

Moving to night-time cleaning services for most state offices. The Facilities Management Office of the General Services Division currently provides daytime custodial services five days a week for most buildings they manage. The Facilities Management Office reports that it would be more efficient to clean offices at night when they are not occupied. In fact, most government, as well as private sector offices, receive janitorial services at night. State agencies that lease property from the private sector – including the many divisions within the Budget and Control Board with offices in the Capitol Center Building – receive standard nightly cleaning service with no reported problems. This simple and logical change would save the taxpayers approximately **\$1,000,000** annually.

Moving health plan members to generic drugs. For 2006, pharmacy costs were just over \$300 million and accounted for approximately 30 percent of the total State Health Plan expenditures. Currently, there are eight therapeutic classes that represent nearly 24 percent of Plan cost and 21 percent of claims utilization. As the state discovered through its 2003 creation of a Preferred Drug List, moving certain preferred drugs to equally effective, lower-priced drugs can lead to significant savings for the state. A logical continuation of that process involves adding these classes of drugs to the equation, and it is our understanding that the board has already taken steps to implement this plan. This would create a **cost savings of \$16,400,000**, which could be passed on to state agencies in the form of lower insurance contribution rates.

Establishing a Network Management Approach and Capping Benefits for Chiropractic Care. The State Health Plan currently offers unlimited chiropractic services without any medical or utilization management specifics for that benefit. Partially as a result, chiropractic is now the leading professional specialty in terms of claims payout, costing over \$23 million last year. From 2004 to 2006, growth in chiropractic expense per person has increased by an average annual rate of 16.8 percent, compared with 5.8 percent a year for the overall plan. Twenty-five percent of the plan's participants had expenses over \$1,000 a year, 126 patients (out of 350,000) spent over \$10,000 last year, fourteen patients exceeded \$20,000 last year, and three patients cost the State Health Plan over

\$30,000 each last year. In order to provide more accountability in the system, the State Health Plan is currently adopting a network management approach for chiropractic care as the GEAR report suggests. This option implements a plan for chiropractors to join the State Health Plan network and follow a specific set of guidelines in order to receive state business. The cost savings resulting from this change would be **\$4,700,000**, which could also be passed on to state agencies in the form of lower insurance contribution rates. Additionally, we propose limiting chiropractic care benefits to \$1,000 per participant, which will save an additional **\$8.3 million**, for a total savings of **\$13 million**.

Further reducing DSIT charges. All financial information included in the reimbursement system should be made available to anyone with a legitimate interest in access to the information. In addition, a detailed audit of the past five years' activities in the DSIT reimbursement system and the DSIT operations should be conducted with the goal of reducing charges to agencies to reflect their actual costs. In its FY 2007-08 activity-based budget report, the DSIT's office shows a total of \$49.6 million in revenue for telecommunication and data services. The DSIT's office has also provided information from a consultant they hired which reports that the agency only spent \$16.7 million for telecomm and data services. The result is a significant \$33.3 million gap between the DSIT's office anticipated receipts and what they say they will spend for what seems to be the same services. All or part of this gap appears to be primarily in charges to DSIT customers and pays for other functions within the office. It also helps explain the huge cash balances that the DSIT's office carries forward annually. The Board agreed to reduce the charges effective July 1, 2007. The Board only half implemented this recommendation. While a savings of \$1,900,000 annually is a step in the right direction, we **propose fully implementing this proposal and realizing a full cost savings of \$4,000,000 annually.**

Eliminating costly, inefficient DSIT services. As a result of the GEAR Committee recommendation that the DSIT allow DHEC to directly contract with an outside vendor for IBM DB2 database management services, which was previously provided by DSIT for approximately \$1.7 million annually, DHEC has now contracted with an outside contractor for DB2 services. Going forward, DHEC will purchase DB2 services for approximately \$100,000. This measure will save the agency **\$1.6 million**. DHEC's budget has already been reduced by \$600,000 because of these changes; therefore, we propose reducing DHEC's budget by an additional **\$1 million** to realize the full savings of this measure.

Restructuring for a more accountable executive branch. Many services throughout state government are being duplicated. This is not only inefficient but it also costs the taxpayers. LAC, members of the MAP Commission, the GEAR Committee and participants of the budget hearings all agree that restructuring is needed. The bottom line is our state government can function better and more efficiently. Restructuring will produce this by holding agencies more accountable and, in turn, provide better results at a lower cost. Specifically, the primary elements of our restructuring proposal are (1) reducing the number of elected constitutional officers, (2) consolidating agencies that deliver health care services into one cabinet-level agency, (3) restructuring the Department of Transportation further, and (4) moving administrative functions of the Budget and Control Board into a cabinet-level Department of Administration, like all other states in the country. The total

dollar **savings for one year – \$21,362,375 in state funds** – from adopting our restructuring proposals are recognized in the separate budget goal areas that would be impacted.

Reducing lottery commissions to approximately the national average is an idea that we have proposed in our last three budgets to provide significant new dollars for education in our state. Data from lotteries across the country show there is no correlation between a higher retail commission and higher lottery sales. In fact, a study shows the top ten lotteries across the nation in sales had average per capita sales of \$581 compared to South Carolina's \$229 per capita sales. However, the data shows the top-selling states had a retail commission that was one full percentage point less than ours and one-tenth lower than the national average of six percent.

When the Education Lottery was established, retail commissions were set at a minimum of seven percent. Had sales for the lottery's first year been \$500 million as predicted, retailers would have shared in commissions of approximately \$35 million. As lottery sales are now over \$900 million annually, commissions are over \$66 million. In other words, retailers signed up for a program that projected average annual commissions of \$10,000. But they have been rewarded with average annual commissions of over \$19,000 per retailer. A reduction of retailers' commissions from seven percent to the approximate national average of six percent will still leave retailers making an average of over \$16,000 per store – 60 percent more than the initial projections. More importantly, paying retailers a six percent commission will free up an estimated **\$9,519,064 annually** that can be used for education in our state.

Creating a central state travel office and instituting travel guidelines. A recent LAC report on state travel shows that our state can better manage its travel. This is why we recommended in our past two budgets, and continue to do so, the creation of a Central State Travel Office. With no current centralized travel agency, we currently have over 70 agencies making travel decisions with no standard regulations – resulting in a very inefficient system. Several reports in recent years have found numerous examples of excessive spending of finite state resources. Even though our state spends tens of millions of dollars annually in travel-related costs and we have countless examples of employees staying in hotel rooms costing hundreds of dollars per night, South Carolina government has no maximum rate to limit an employee's hotel expenditures. The LAC discussed inefficiencies when it comes to agency airline purchases. Currently, each airline transaction is bought at the individual agency level and results in a more expensive ticket. This additional cost to the taxpayer can be avoided by taking advantage of bulk purchasing. According to the LAC report, other states and the federal government utilize pre-negotiated contracts with airlines for discount prices. We propose joining the federal government and other states by utilizing bulk purchases with airlines. The LAC estimates each agency will reduce airline expenditures by 25 percent if purchased through this mechanism.

We also propose that members of the Workers' Compensation Commission, the Employment Security Commission, and the Public Service Commission be covered by the same guidelines as other state employees when traveling 50 or more miles from their homes. The newly created Central State Travel Office within the Comptroller General's Office in conjunction with the Office of Procurement will ensure that each agency adheres to the state's travel provisions. This

management, coupled with savings from bulk airline purchases, will provide an annual **savings of \$831,218** during FY 2009-10.

In addition, when looking at travel expenditures across all agencies, it is clear that some have not used taxpayer dollars in the most efficient manner during the past years. Specifically, total state travel expenditures have grown by almost 20 percent in just two years. Some agencies have done a good job in spending travel dollars, while others have not had the taxpayer's best interest in mind. For this reason, we are recommending all agencies reduce travel expenditures back to FY 2004-05 levels for a total cost **savings of \$10.4 million**.

Savings from TERI employees leaving state government. In many instances, the Teacher and Employee Retention Incentive (TERI) program has accomplished its goal – retaining experienced teachers and good workers in critical positions of government. However, in many other instances, it has prevented qualified individuals from entering the state's workforce at lower rates of pay. The TERI program has, in essence, been unfair to the taxpayers of the state because it asks them to contribute more tax dollars to high-salaried managers simply because they were able to take advantage of a system. In fact, TERI employees are paid \$17,000 more than the average non-TERI state employee.

The first class of TERI participants has hit the five-year mark. We recommend that agencies rehire these employees only in extreme circumstances. Agencies should disburse job duties among remaining employees and concurrently look to hire and train qualified new hires so that the agency will be better prepared for the long term. This type of management will not only reduce duplication and create a more efficient office, but it will also create a savings for all agencies with TERI employees leaving. According to numbers from the Human Resource Office in the Budget and Control Board, if each agency's budget were reduced by taking the difference between the average TERI employee salary and the average salary for that agency, an annual cost savings of **\$17,180,713** in general and other fund dollars would be provided. We want to make it clear that this proposal is not about terminating any current employees but instead represents the natural process of replacing most positions with less tenured individuals at lower pay.

Eliminating vendor preferences in the procurement code. South Carolina's state procurement code provides vendors in South Carolina a seven percent preference when they bid for certain state government contracts. While these preferences give resident vendors a competitive advantage over vendors in other states that bid for state contracts, they add a significant expense to the state agencies' cost of doing business. Audit reports from the Materials Management Office in the Budget and Control Board show that these preferences have cost South Carolina state agencies more than **\$1.3 million** over the past ten years. Moreover, these preferences have cost our state in ways that cannot be counted by discouraging out-of-state vendors from competing for South Carolina government contracts and by penalizing South Carolina vendors who encounter retaliatory preferences in other states. Accordingly, we seek to save South Carolina state agencies money and to make South Carolina vendors more competitive in other states by eliminating the vendor preferences from the procurement code. This measure will save the state approximately **\$115,000** annually.

**IMPROVE THE EFFICIENCIES AND EFFECTIVENESS OF CENTRAL
STATE GOVERNMENT SUPPORT AND OTHER GOVERNMENTAL
SERVICES**

Implementing efficient cell phone, pager, and satellite phone policies. In June 2008, the LAC issued its audit report of state agency usage of cell phones and other wireless communication devices. The report found that South Carolina state agencies spent over \$7 million on cell phones, \$790,000 on pagers, and \$68,000 on satellite phones in FY 2005-06. Unfortunately, many agencies waste thousands of dollars a year on cell phones and other devices because their policies are inefficient or because they fail to adequately monitor their employees' usage. To remedy these wasteful practices, the LAC made several recommendations that will reduce the state's total expenditures on cell phones and other devices. These recommendations include for all agencies to review their cell phone plans and choose the most cost-effective plan suitable to their needs, improve procedures for preventing overcharges, comply with IRS regulations regarding personal use of state-issued cell phones, and prohibit state employees from making directory assistance calls. We believe that the LAC recommendations will help eliminate government waste, and, therefore, we include them in our executive budget, which will result in cost savings of over **\$777,743** if implemented, according to the LAC.

Reducing insurance premiums paid to the Insurance Reserve Fund. On November 7, 2007, the Budget and Control Board implemented the GEAR Committee's recommendation that the Insurance Reserve Fund (IRF) competitively bid the property reinsurance broker contract for the first time in nineteen years. This recommendation realized an immediate savings of approximately \$2.1 million, and the broker who was awarded the contract saved the state an additional \$1.7 million by purchasing reinsurance on the secondary market. By implementing the GEAR Committee's recommendation on bidding the reinsurance program, the state saved a total of **\$3.8 million**. We propose that the IRF pass these savings along to the state agencies in the form of insurance premium reductions, which will allow for a corresponding cut in all agencies' general fund appropriations.

Making Tough Choices:

Given the state's finite amount of resources and an anticipated revenue reduction for FY 2009-10, we had to make some difficult choices regarding which activities to fund or not fund. While the activities listed below may well have merit, when comparing them with other activities, we did not think their anticipated outcome would be as effective in achieving our goal of making central government as efficient as possible. The following reflects some of those difficult choices:

Requiring all state employees to choose two holidays without pay. In an effort to find cost savings during a tight budget year, we propose requiring all state employees to choose two state holidays that they would like to take unpaid during FY2009-10. State employees currently have 12 paid holidays during the calendar year in addition to Christmas Eve, which has been annually granted by this administration through an Executive Order.

According to the U.S. Bureau of Labor Statistics, the average number of paid holidays for state and local government employees nationwide is 11 days a year. The average private-sector employee

receives eight paid holidays. Therefore, reducing our total number of paid holidays from 13 to 11 would be keeping in line with the national average and still place us above the private-sector holiday average. Other states, including Utah, Maryland, California, and New Jersey, have also taken a similar approach. In addition, several private corporations have begun imposing unpaid holidays. This proposal will save more money than a voluntary furlough because state offices would already be closed on holidays, which saves operational and utility expenses. Implementing this proposal for FY 2009-10 for nearly 65,000 state employees will result in a **cost savings of \$10 million.**

Delaying supplemental, non-essential pension payments for retired National Guardsmen. On June 11, 2008, we vetoed House Bill 4339, which allows National Guard members who joined after June 30, 1993, and have reached the age of 60 and have 20 years of service to receive a supplemental monthly pension of \$50. As we explained in the veto message, we have the deepest admiration for Guardsmen and the jobs they do, but we thought it was the wrong time to create new liabilities for the state in the face of tough budget times. In our view, it made no sense to create non-essential supplemental pension obligations when it was clear that we would be making serious cuts to existing health care and education spending. Unfortunately, our warning about the state's impending fiscal downturn was ignored, and the General Assembly enacted this measure anyway. Accordingly, we believe it is wise to revisit this newly granted obligation and delay funding the expansion of the National Guard Pension Plan until the state is on more solid financial footing. Delaying funding of this plan would save the state approximately **\$926,000.**

Making ancillary human resources functions self-sufficient. The Budget and Control Board provides a number of human resources services such as training and development, temporary employment services, and recruiting services to various state agencies. The Board charges agencies a fee for these services. In addition to the fees they collect, these services also receive a general fund appropriation. We propose removing the general fund appropriation for these ancillary services and require the Board to justify their expenditures entirely in terms of services provided to agencies. Removing the general fund supplement for Training and Development Services, Temporary Employment Services, Recruitment Services, Workforce Planning, and Executive Education Training will save a total of **\$568,746** next fiscal year.

Please see the Appendices for a complete listing of the Governor's Purchase Plan for this goal area and for a detailed listing of what our plan saves and what our plan does not buy.

APPENDICES