

The Executive Budget

Fiscal Year 2010-11



January 7, 2010

Submitted by
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Governor
State of South Carolina

to the
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Second Session



State of South Carolina

Office of the Governor

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

I present to you this Administration's FY 2010-11 Executive Budget. Before going into some of the points included in the document, I would once again like to express my thanks to all who gave time, talents and focus to this effort.

Unfortunately, I must begin this letter the same way I did last year and point out the obvious – our state is facing very significant financial challenges due to the national and international economic slow down. As the revenue projections become bleaker, the task of crafting a budget that adequately funds core functions of state government becomes correspondingly more and more difficult. In many ways these challenges are exacerbated by the fact that federal stimulus dollars, used this year to plug state budget holes here in South Carolina and nationwide, are fast drying up. Amidst these challenges, our goal this year, as it has been the past six years, is to offer a balanced budget without raising taxes that provides essential services to the citizens of South Carolina in the priority areas of education, health care, social services, economic development, public safety, and natural resources.

Although the \$1.58 billion in state budget cuts over the last two years have garnered much attention, what is important to remember is that the total state government budget this coming year will top \$21 billion. This \$21 billion includes federal funds and state fees and is the highest total budget in South Carolina history. It is seven percent higher than last year's total budget and projected to increase another 7.5 percent going into FY 2010-11. Over the course of this Administration, the total state budget will have jumped from around \$15.5 billion in 2003 to a projected \$22.8 billion in 2011 – an increase of almost 47 percent, or 5.23% annually, which outpaces by an average one percent annually the estimated growth in "population plus inflation" over that time.

We've said year after year that this spending growth is unsustainable, and the budget choices necessitated in this year's budget reinforce this.

More funds than ever are being sent to and spent by state government, but there are still mounting challenges to be addressed.

First, South Carolina stands to lose roughly one billion stimulus dollars after FY 2011 that are currently filling gaps in the state's general fund budget. Our Administration argued repeatedly during the stimulus debate last year that you can't spend money you don't have, and that solving a problem created by too much debt by indeed issuing more debt seemed misguided. We strongly believed that using future generations' tax dollars from Washington D.C. to supplement today's state budget in Columbia, S.C., would have dangerous consequences – unsustainable spending, mounting debt, and taxpayers footing the inevitable bill. A *Washington Post* article from January 5, 2010, agreed:

What many state governments want is a federal bailout, which would free them of the consequences of overspending. It's a classic case of what economists call 'moral hazard' – in that the bailouts would allow the irresponsible behavior to continue, rather than forcing a halt.

South Carolina was not alone in falling prey to the stimulus' fiscal consequences. A January 2, 2010, *Wall Street Journal* editorial pointed out that “in most state capitals the stimulus enticed state lawmakers to spend on new programs rather than adjusting in lean times. They added health and welfare benefits and child care programs. Now they have to pay for those additions with their own state's money.”

For example, this year South Carolina was given a full year of enhanced match money for Medicaid by the federal government, also known as Federal Medical Assistance Percentages (FMAP). Next fiscal year, Washington D.C. will only provide half a year of enhanced FMAP, and the year after that none at all. This tapering-off effect of all federal stimulus funds will create an additional hole of \$733 million by FY 2011-12 in the state budget – and this does not even take into account any of the certain financial costs that will come to South Carolina with the massive change contemplated by Congress in health care.

Second, we already begin this Executive Budget \$462 million in the hole. Revenue numbers lagged this year, and the Office of State Budget sees this downward trend continuing over the next three years. They project another drop of \$560.9 million in FY 2010-11, a \$1.34 billion drop in FY 2011-12 and a \$1.44 billion drop in FY 2012-13. The Budget Office's report also assumes a two percent annual growth rate in sales and income tax revenues – which some would argue is most hopeful.

Third, there are nearly \$1 billion in existing liabilities – including a \$98 million deficit from last year – that must be funded in the budget before even addressing core services like education and law enforcement. In all, our Executive Budget starts not from ground zero financially, but short some \$1.44 billion in revenue, meaning that difficult decisions must be made with regard to cutting programs or finding new sources of revenue.

We have ruled out the second option because raising the overall tax burden of South Carolinians is not something we'd ever support. On that front we'd applaud the General Assembly for what they did last year in resisting the path of raising taxes as several other states did. We hope the tax increase option remains off the table as raising taxes will do more to deepen and prolong this global recession's impact on our state. We believe government should not be shielded from making the same hard decisions on costs, and cuts, that the businesses and individuals who pay for government have to make. These decisions are tough – and in many cases less than ideal – but, in this kind of economic climate, necessary.

With these challenges in mind, the following pages lay out this Administration's spending and policy initiatives. From a spending perspective, the FY 2010-11 Executive Budget prioritizes \$5.84 billion in spending by breaking down each activity in government, ranking them to adequately fund our most critical and effective services, and identifying \$254 million cost savings measures. In funding priorities and making cuts, our budgeting approach is focused on the relative performance and results of each agency.

Our budget this year also looks longer term in preparing for what we believe may be several difficult years as state revenue growth idles, or increases only incrementally. For this reason, we cannot hold certain areas of the budget harmless from cuts that we ordinarily by and large would – such as K-12 Education, Higher Education, and Health. These three pieces of the state budget pie make up over 80 percent of the current budget, rendering it nearly impossible to make all of the cuts necessary to put forth a balanced budget out of the remaining 20 percent. To do so would be detrimental to other core government functions such as Public Safety.

Specifically, our budget serves students of all ages, providing more than \$218 million to college scholarships and grants, \$34 million to First Steps and \$3.3 million to charter schools. On health care, we fully fund the state employee health plan and the state's Medicaid Maintenance of Effort, and support Medicaid-fraud enforcement because every dollar we spend on enforcement we recoup seven dollars in Medicaid costs. To improve public safety, we restore funding to Corrections and keep Juvenile Justice out from under federal court order, as well as send \$40 million to DPS for increased highway traffic enforcement. We're also putting \$4 million in Commerce's closing fund to help encourage investment and job growth in South Carolina, and we're setting aside \$40 million to pay the interest on federal unemployment benefit loans taken out by the ESC. Finally, we are making sure the Conservation Bank doesn't have to shutter its doors, and also again funding a Sunset Commission in order to eliminate archaic and oftentimes expensive laws that no longer serve their original purpose.

From a policy perspective, we are focused this legislative session on three primary objectives: spending caps, real reform at the Employment Security Commission (ESC), and state government restructuring.

One, we continue to believe it is important we not allow government spending to grow faster than the underlying economy. Prior to mid-year reductions, South Carolina state government grew by over 40 percent from 2004 to 2008, leading the Southeast in year-to-year government growth. Over the last 18 months, that same budget has been cut by 27 percent. This spending roller coaster brings with it harmful consequences, and given the current economic climate, we believe it is critical that spending caps finally be adopted.

Capping government spending growth at population-plus-inflation would help on two fronts: first, it would protect the neediest of the needy for cuts past muscle and right into bone when times are bad; and second, when times are good it protects taxpayers from the excesses in spending that usually accompany large amounts of money coming into any state Capital.

Two, we believe reforming the ESC is vital to bettering the unemployment issue in our state. Given the continued lack of meaningful reform at the ESC, an Unemployment Insurance Fund deficit fast approaching \$1 billion, and the potential of counterproductive tax increases on the state's businesses, we'd urge legislators to pass substantive ESC reform as soon as possible this session. In

our Executive Budget, we set aside \$40 million to pay the interest on the federal loans South Carolina has been forced to borrow. These loans will likely total \$1.4 billion by next fiscal year. Instilling accountability and efficiency into the ESC will help prevent this deficit run-up from happening again, and more importantly, it will help the agency fulfill its core mission of connecting willing workers with open jobs across the state.

Three, restructuring South Carolina's fractured state government would make it more efficient and effective. We have proposed three small, but meaningful, measures that would go a long way to making our government work better for the people of this state. According to *Governing* magazine, South Carolina government has 234 state employees per 10,000 residents – 35 percent higher than the U.S. average of 174. The duplication in state services these numbers suggest has much to do with why government costs South Carolinians 40 percent more than the national average.

I look forward to working with the General Assembly to look for ways to weather these tough economic times and ensure a more prosperous South Carolina in the future.

Mark Sanford

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Executive Summary

Executive Summary

As everyone knows, our state is facing monumental financial challenges. As the revenue projections become bleaker, the task of crafting a budget that adequately funds core functions of state government becomes more and more difficult. Even as the revenue available becomes smaller, our goal in preparing this document, which has remained consistent for the past six years, is to present to the General Assembly a balanced state budget that, without raising taxes, prioritizes spending to fund the core functions of state government.

It is important to point out up front, that while the \$1.58 billion in state budget cuts over the last two years have garnered much attention, it is also important to remember that the total state government budget this coming year will top \$21 billion. This \$21 billion includes federal funds and state fees, and is the highest total budget in South Carolina history. It is seven percent higher than last year's total budget, and projected to increase another 7.5 percent going into FY 2010-11. Over the course of this Administration, the total state budget will have jumped from around \$15.5 billion in 2003 to a projected \$22.8 billion in 2011 – an increase of almost 47 percent, or 5.23% annually.

Objectives

The current economic situation at both a national and state level presents us with the difficult task of meeting the increased demand for government services with ever-decreasing state revenue. Our first goal is to present to the General Assembly a balanced state budget that does not raise taxes and 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 changes we intend to achieve this coming year.

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

Administration Goals

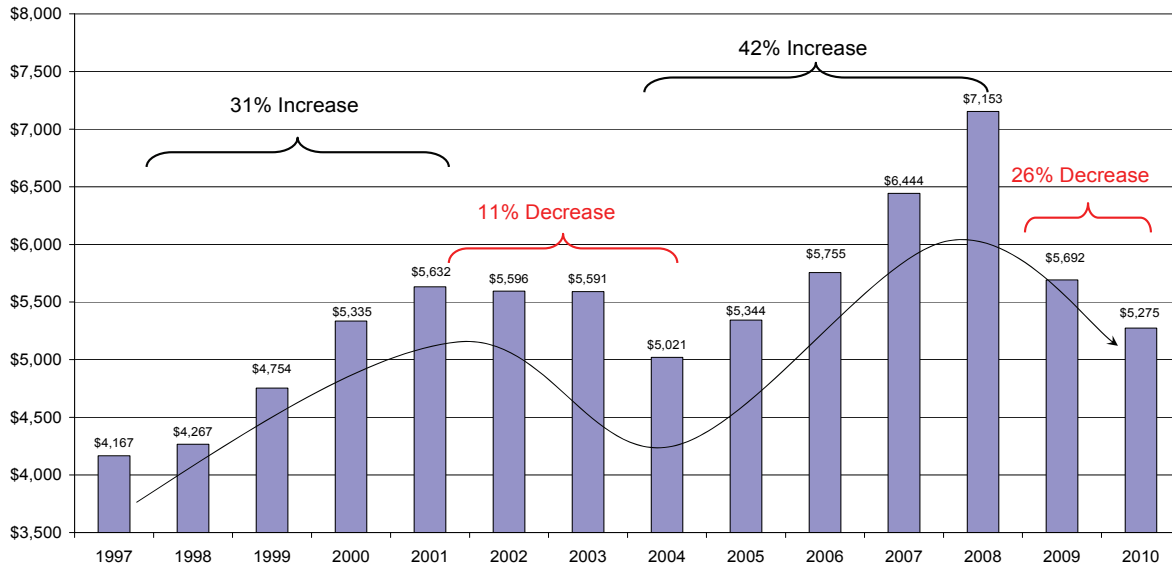
To improve South Carolina's competitive advantage globally and ensure that government spending does not grow at an unsustainable level, the administration has laid out seven major budget goals for the FY 2010-11 Executive Budget. Adhering to these goals, we have prioritized and funded the state's critical 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 2010-11 Executive Budget are as follows:

1. **Limit the annual growth of general fund spending by not exceeding population growth plus the rate of inflation.** 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 over 40 percent over the previous seven years. As evidenced by the painful spending cuts we are now making, it should be very clear that we cannot grow government faster than people's ability to pay for it. To that end, we are calling for legislation to limit spending increases to the growth in population plus inflation. Representative Garry Smith has filed a bill that would do just that, and we hope the full General Assembly will pass this legislation.

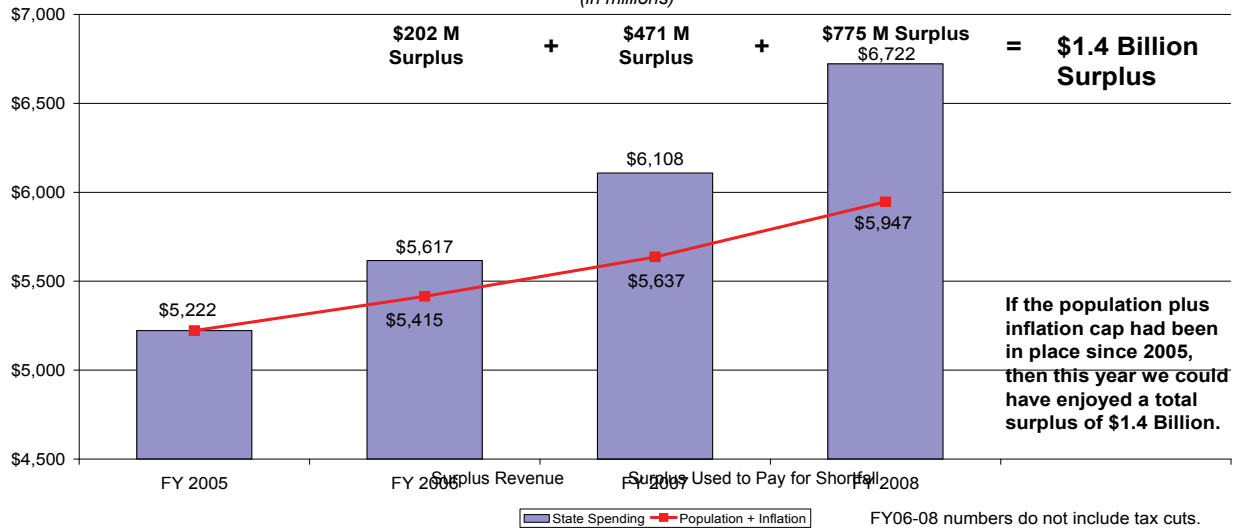
Peaks and Valleys Approach to State Spending

(recurring and non-recurring dollars, in millions)



It is important to point out that, in the years leading up to the downturn of the economy, there were excess funds over the population-plus-inflation cap. While some cuts might have been necessary over the last two years, they would not have been as pronounced as the cuts that state agencies have experienced. As the following chart demonstrates, had a population plus inflation spending cap been implemented in FY 2005, over \$1.4 billion potentially could have been saved for the current tough budget years, and prevented some difficult cuts.

**State Government Growth
Under Population Plus Inflation Spending Cap
FY2005 - FY2008**
(in millions)

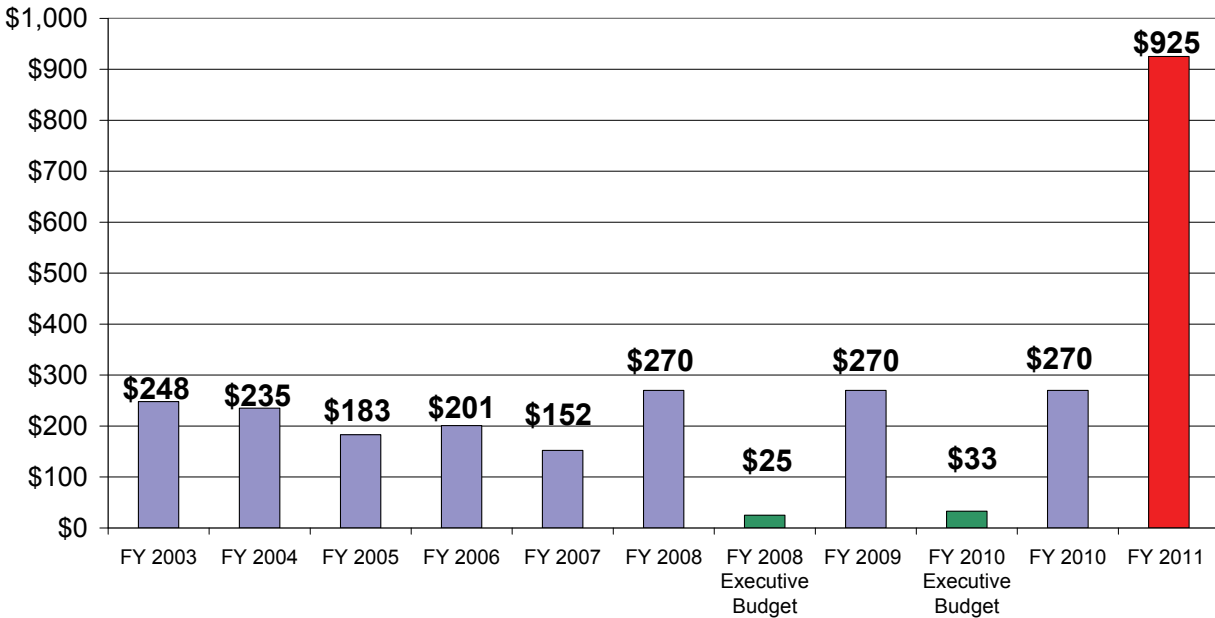


We believe that a spending cap that allows for budget growth that does not exceed population growth plus the rate of inflation will help prevent the roller coast budgeting that has occurred over the last decade in South Carolina from occurring in the future. In years in which there are surpluses over the cap, these excess funds should go into a long-term rainy day fund, toward paying down the state's unfunded liabilities, or sent directly back to the taxpayers.

2. **Annualizations.** To put our state's fiscal house in order, we must stop the practice of annualizations – using one-time money to fund recurring needs. Over the course of our administration we have pointed out the need to not allow annualizations to exceed one percent of total estimated revenue for a fiscal year. Each of our previous Executive Budget have met this goal and we will continue to support this practice in the future.

Unfortunately, given the sum of stimulus dollars included in the FY 2010-11 budget, this year's annualization total will be \$925 million. Going forward this is going to make crafting balanced budget that adequately fund core functions of state government very difficult.

South Carolina Annualizations Since FY 2001-02
in millions



3. **Provide tax cuts for individuals and businesses to spur investment and job creation.** There has never been a more important time to discuss how best to grow our state's economy. We believe staying competitive amid today's challenges requires two things. First, a lower income tax would represent a significant step toward making our state more attractive to businesses. Second, we have to get away from our piecemeal approach to economic development that selectively provides tax incentives to some businesses but not to others. We believe a better approach is 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. Our proposal avoids the unintended consequence that comes with much of today's incentives system, wherein we create incentives for businesses coming into our state, but have no incentives for small and mid-size businesses already in our state.

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

- First, create an optional income tax of a flat 3.65 percent – cutting the current rate of 7 percent nearly in half. 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.

4. **Appropriate funds based on a rational assessment, from the citizen's perspective, of the relative importance of the government's activities.** 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.

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 **\$254.8 million in specific general fund savings** to the taxpayers through operational efficiencies realized by state agencies and by not purchasing lower priority activities.

We also recommend purchasing higher priority activities in the areas of education, health care and social services, economic development, public safety, and natural resources as follows.

a) **K-12 Education – \$2.1 Billion General Funds/\$3.46 Billion Total Funds –**

To provide for the state's K-12 needs during FY 2010-11, 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 \$2,044. However, we once again propose that teachers' salaries should reflect classroom results or teachers' willingness to teach core subjects in critical needs areas – not simply on teachers' seniority. In this budget, K-12 represents 36.1 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: \$2,044
- 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: \$27.27 million
- Funding Student Health and Fitness Act obligations: \$28.66 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. We agree with the Education Oversight Committee's previous recommendation that students in 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: \$3.34 million
- Funding for 4K Child Development Education Pilot Program: \$17.3 million
- Funding school bus operations: \$41.66 million

- b) **Higher Education and Cultural Resources – \$690 Million General Funds / \$4.42 Billion Total Funds** – Our primary goal for higher education is to provide a high 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. Our current economic downturn has added to these challenges, as recognized by our low college-affordability ranking 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 providing funding for our various scholarship programs as follows:

- **Needs-based scholarships** for total funding of \$12.2 million
- **LIFE Scholarships** for total funding of \$158.1 million
- **HOPE Scholarships** for total funding of \$7.2 million
- **Palmetto Fellows Scholarships** for total funding of \$41 million

- c) **Health Care and Protections of Children and Adults – \$1.44 Billion General Funds / \$10.43 Billion Total Funds** – Nationally, the costs associated with health care continue to increase faster than the rate of inflation. Medical expenses, according to the 2008 “State of the States” report, account for 16 percent of the country’s gross domestic product, compared to 7.2 percent in 1970. In preparing this budget, one of the biggest challenges we face is dealing with the rising cost of all aspects of health care as it greatly impacts the quality of life. Overall, health care costs account for more than a third of the state budget. In fact, our state’s largest health care expenditure is our state’s Medicaid program – which has an enrollment of about 775,000 citizens. If nothing changes, Medicaid enrollment is projected to grow to more than 830,000 people by 2013. However, the reform bills being debated in Washington, D.C. will add a new group of people eligible for Medicaid – an estimated 543,000 adults with no children – to the state’s Medicaid rolls.

In other words, both the House and Senate proposal will result in 1.3 million South Carolinians being enrolled in Medicaid by 2019 – meaning approximately 30 percent of South Carolina’s total population will be enrolled in the Medicaid program in the next ten years. Without even taking into account any other growth in later years, the two bills being debated are estimated to either add \$687 million or \$1.17 billion to the amount that our state must annually pay by 2019. This legislation has the potential to more than double the percentage of the state budget dedicated to the Medicaid program. Like most states, South Carolina has seen a significant amount of its budget disappear over the last year and a half – over 25 percent, in fact. If ever there was an appropriate time to force an unfunded mandate our state, now is not that time.

The national health care debate notwithstanding, one of our primary goals is to meet Medicaid’s maintenance of effort requirements for core health benefits to our most vulnerable citizens. We also need to continue preventing and treating substance abuse. Because of the prevalence of smoking in our state--23 percent of South Carolinians smoke – 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 2008, 16 percent of our population lacked health insurance. With such serious health concerns, during FY 2010-11, we propose health care spending as a percentage of the total budget at 43.2 percent. Specifically, to provide support for the state’s health care and protections of children and adults during FY 2010-11, we propose:

- Meeting Medicaid's maintenance of effort requirements for core health care benefits for the poor, elderly, and persons with disabilities through the Department of Health and Human Services: \$348 million
- Continuing our focus on chronic disease prevention at the Department of Health and Environmental Control: \$1.35 million for chronic disease prevention
- Continuing development of the Child Support Enforcement System: \$9.56 million

d) **Economic Development – \$77.6 Million General Funds / \$1.92 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. Our administration and the Department of Commerce have already laid much of this groundwork. As a case in point, Commerce has completed 839 economic development projects, which created over 83,000 jobs and \$17.76 billion in new capital investment over the last seven years. Nevertheless, with a rapidly changing world, there is always room for improvement. Specifically, to assist with the state's economic development during FY 2010-11, we propose:

- Several ideas we have for tax reform, including lowering the personal income tax to as low as 2 percent, eliminating the corporate income tax, and cutting the sales tax from 6 percent to 4.5 percent.
- Funding \$40 million in interest owed on the federal loans for unemployment compensation benefits requested for the Employment Security Commission.
- Funding Local Workforce Investment: \$79.5 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.
- Funding the Closing Fund at the Department of Commerce with \$4 million.

e) **Public Safety – \$601 Million General Funds / \$1.09 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 such committed personnel working in its public safety agencies. Despite these efforts, South Carolina continues to face many challenges in the area of public safety, demonstrated by higher crime and accident rates than most of its Southeastern neighbors.

Specifically, to assist with the state's public safety needs during FY 2010-11, 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: \$11.7 million**
- **Funding the Department of Public Safety, allowing Highway Patrol officers to provide greater highway traffic enforcement and to further reduce the response times to collisions: \$61.3 million**
- **Maintaining funding for the state's seven high-security, eight medium-security, eleven minimum-security, and three female institutions: \$255.8 million**
- **Maintaining funding for community supervision of almost 50,000 adult jurisdictional offenders: \$41.3 million**
- **Funding enforcement for the South Carolina Illegal Immigration Reform Act with \$2 million recurring general funds.**

- f) **Natural Resources – \$53.4 Million General Funds / \$267.1 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 2010-11, we recommend funding for the following activities:

- **Funding to keep the Conservation Land Bank open: \$200,000**
- **Monitoring and preserving South Carolina's marine resources: \$19.8 million**
- **Protecting and managing water resources: \$10.95 million**

- g) **Improve Central State Government Support – \$650 Million General Funds/\$938 million Total Funds** – 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 which 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 \$988,357**
- **Incentivizing health plan participants to use clinically equivalent generic or plan-preferred drugs – savings of \$4.9 million**
- **Creating a Central State Travel Division within the Comptroller General's Office to manage and monitor agency travel – savings of \$6,573,666**

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 \$777,253**
- **Reducing insurance premiums paid to the Insurance Reserve Fund – savings of \$3.79 million**
- **Eliminating vendor preferences in the procurement code – savings of \$150,000**

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 Governor Carroll Campbell's legacy 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 that citizens are 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. Two different reports – 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 – have highlighted the areas for improvement. 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.

In previous years, some legislators have supported the creation of a Department of Administration. Although a bill that would create such a department has not been filed yet this year, we believe passage of this kind of 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 advance the restructuring proposals in our executive budget including streamlining health care agencies. This bill has been filed in both the House and the Senate again this session, with the House having already passed it again.

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 nearly \$17 million during FY 2010-11.**

6. **Honor the promises and obligations of prior years.** Our retirement system's last reported unfunded liability in mid-2009 was over \$11 billion. However, this number is only a part of the picture because it does not include \$9 billion of unfunded Other Post Employment Benefits (OPEB) costs for retirees' health care. The combined \$20 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.

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, 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 2010, retirees' total health cost is projected to be near \$380 million, which means that taxpayers will be paying over \$266 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 \$65 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 pay a maximum of only \$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 two percent annual cost of living increase for retirees. Unfortunately South Carolina is still a relatively poor state, ranking 47th in per-capita personal income, according to the U.S. Census Bureau. How can relatively low-income taxpayers afford to pay top-level benefits to public retirees? 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 its website, the President of the South Carolina State Employees Association wrote the following about how their benefits have been obtained (emphasis added):

[D]emonstrations 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

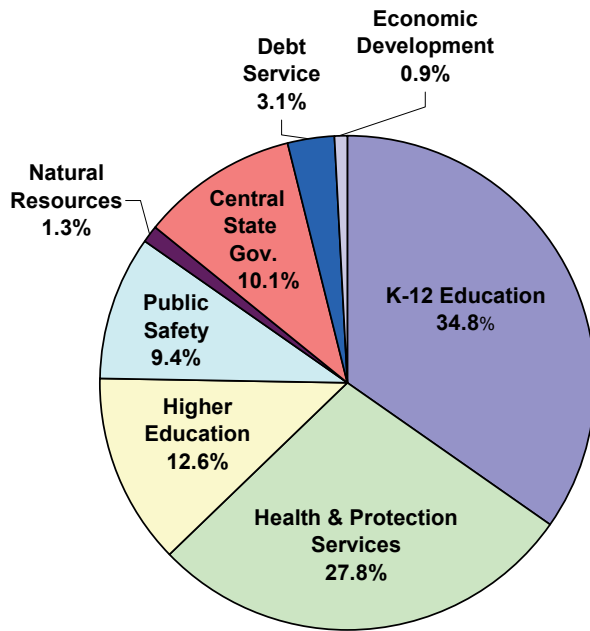
future benefits – political promises that have been made but not funded – will either have to come from our children and grandchildren or the entire system will collapse under the weight of its debt. Most taxpayers in South Carolina cannot afford retirement benefits “second to none” for themselves much less for hundreds of thousands of public retirees.

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. Three 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 \$99 million for FY 2010-11 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.

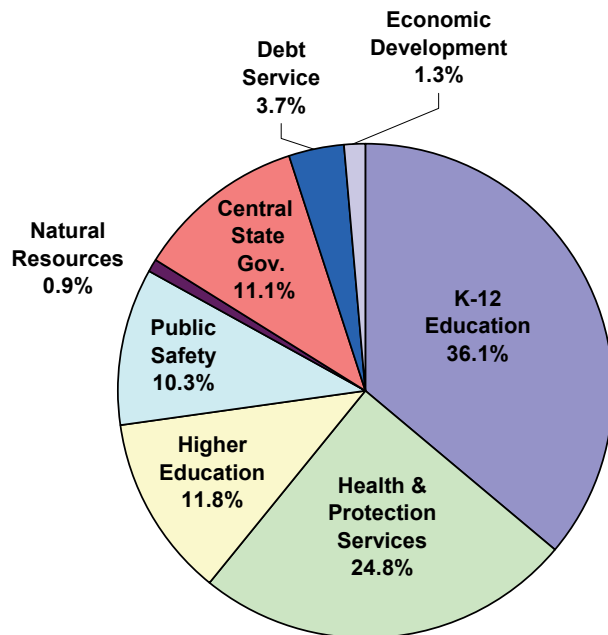
Summary Comparison of General Fund Expenditures

Current Budget – FY 2009-10 General Fund Expenditures



Category	Dollars in Millions
- K-12 Education	2,150.1
- Health & Protection Services	1,717.4
- Higher Ed. & Cultural Resources	776.0
- Central State Government / Other Governmental Services	626.4
- Public Safety	577.5
- Debt Service	190.5
- Natural Resources	81.1
- Economic Development	53.3
TOTAL	6,172

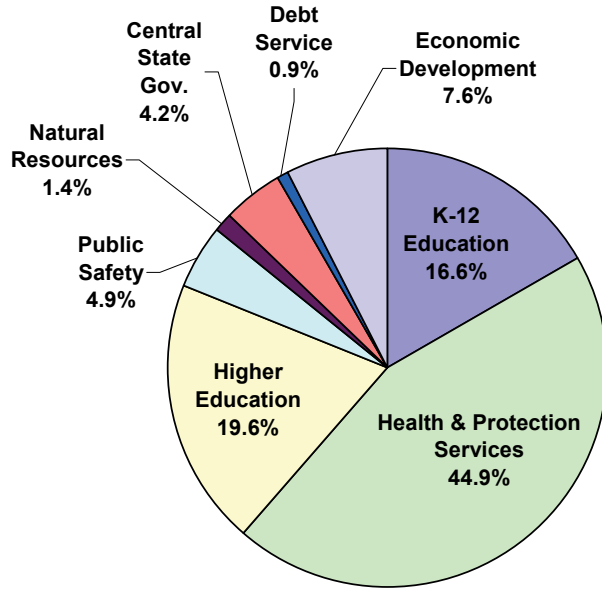
Governor's Purchase Plan – FY 2010-11 General Fund Expenditures



Category	Dollars In Millions
- K-12 Education	2,108.1
- Health & Protection Services	1447.0
- Higher Ed. & Cultural Resources	690.2
- Central State Government / Other Governmental Services	650.5
- Public Safety	601.7
- Debt Service	213.6
- Natural Resources	53.4
- Economic Development	77.6
TOTAL	5,842

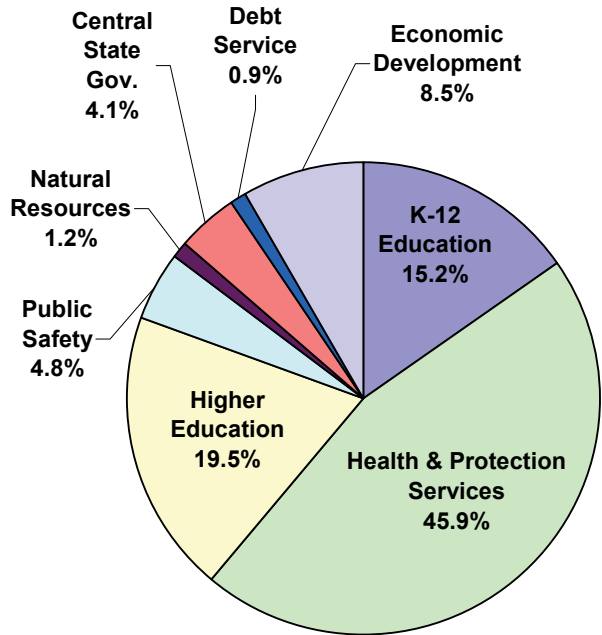
Summary Comparison of Total Fund Expenditures

Current Budget – FY 2009-10 Total Fund Expenditures



Category	Dollars in Millions
- Health & Protection Services	9,492.9
- Higher Ed. & Cultural Resources	4,140.1
- K-12 Education	3,500.8
- Economic Development	1,601.0
- Public Safety	1,046.4
- Central State Government /Other Governmental Services	882.9
- Natural Resources	297.8
- Debt Service	190.5
TOTAL	2,152

Governor's Purchase Plan – FY 2010-11 Total Fund Expenditures



Category	Dollars in Millions
- Health & Protection Services	10,433.9
- K-12 Education	3,461
- Higher Ed. & Cultural Resources	4,428.3
- Economic Development	1,924.3
- Public Safety	1,090.9
- Central State Government /Other Governmental Services	938.7
- Natural Resources	267.1
- Debt Service	213.6
TOTAL	22,758

\$22.75 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:

\$98 million	Covered the FY 2008-09 deficit
\$40 million	Interest on UI loan from federal gov't
\$17.3 million	Pre-K Pilot Program
\$10.48 billion	Health care and protection for nearly a million children and adults
\$4.42 billion	Higher education for over 222,000 students & funding for cultural resources
\$3.46 billion	K-12 education for more than 700,000 students
\$2 million	Recurring funding for S.C. Illegal Immigration Reform Act enforcement
\$1.92 billion	Economic development
\$1.09 billion	Public safety
\$938 million	Central state government/other governmental services
\$275.9 million	Constitutional/statutory funding requirements
\$267.1 million	Protection of our natural resources
\$213 million	Debt service for General Obligation Bonds
\$11.7 million	Funding for deficit at Department of Corrections
\$500,000	Sunset Commission

\$22.75 billion TOTAL

Examples of what our plan does not buy:

\$37 million	A fragmented system at the state's higher education institutions
\$17 million	Poorly coordinated executive structure
\$13 million	Unnecessarily high number of local school districts
\$6.57 million	Excess Agency Travel
\$5.69 million	TERI employees leaving state government
\$2.78 million	State-funded lobbyists
\$1.37 million	Piecemeal approach to economic development
\$988,300	Daily custodial services
\$983,133	Free DPS traffic control at special events
\$360,000	Excess vehicle maintenance facilities in the Columbia area

\$254.8 million TOTAL

\$254.7 Million General Funds

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 106. 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 sixth 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, who 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 toward bringing about positive short- and long-term consequences. In effect, the purpose of BFR and our executive budget for FY 2010-11 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.

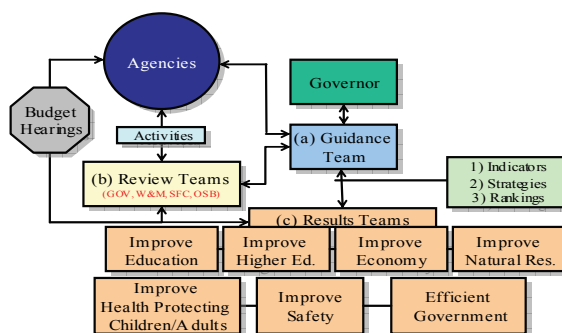
The Budgeting for Results Organizational Structure

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.

Each RT then 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 2010-11 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.

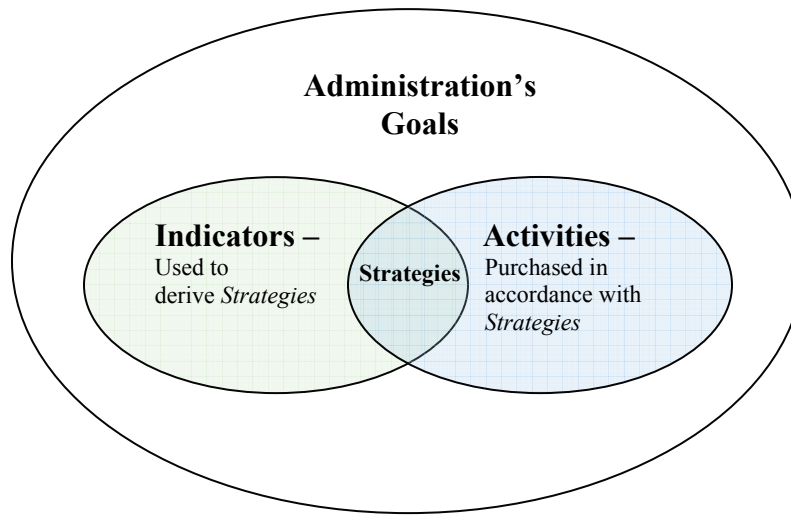
Additionally, it should be emphasized once again that BFR is a budgeting approach that places emphasis on logic, order, and proven cause-and-effect relationships. Utilizing the highest degree of objectivity and data analysis, this approach involves not only the setting of broad goals, but also

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 RTs 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?"
- 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. 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?

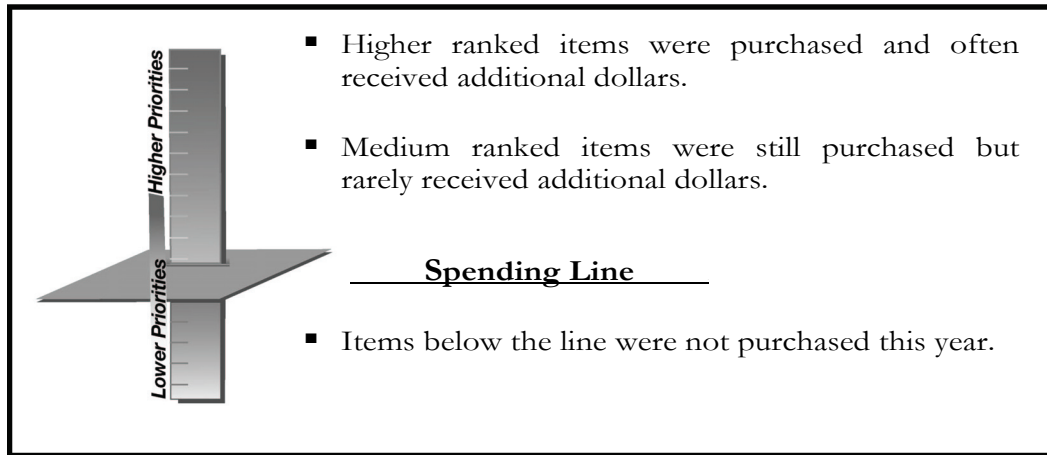
Step #6 – Distributing resources among goal areas, i.e., finalizing the purchase plans by result areas. The heart of Step 6 was the methodical and careful review by our administration of the preliminary purchase plans submitted by the RTs and the finalization of a completed purchase plan reflecting our philosophy and policies. Ultimately, this final purchase plan took the form and substance of this FY 2010-11 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 2010-11 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 2010-11 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

There are four ways in which you can spend money. You can spend your own money on yourself. When you do that, why then you really watch out what you're doing, and you try to get the most for your money. Then you can spend your own money on somebody else. For example, I buy a birthday present for someone. Well, then I'm not so careful about the content of the present, but I'm very careful about the cost. Then, I can spend somebody else's money on myself. And if I spend somebody else's money on myself, then I'm sure going to have a good lunch! Finally, I can spend somebody else's money on somebody else. And if I spend somebody else's money on somebody else, I'm not concerned about how much it is, and I'm not concerned about what I get. And that's government.

- Milton Friedman, winner of the Nobel Prize in economics

Continued Economic Recession

Continuing a trend that began in 2008, dozens of states are continuing to see their state budgets decline. According to the National Conference of State Legislatures, at least 36 states are still facing budget gaps totaling \$28.2 billion in the current fiscal year. This is on top of the \$145.9 billion that states reduced from their respective budgets earlier this year, and in stark contrast to the relatively small number of states that had to reduce their enacted budgets in fiscal 2008 and fiscal 2007. Most states, including South Carolina, will continue to be impacted by the weakening national economy, which means FY 2010-11 could prove to be even more challenging than FY 2009-10.

By the end of 2009, South Carolina's general fund has been reduced by over \$1.58 billion since June 2008 – including \$566 million reductions halfway through FY 2009-10. Unfortunately, there is a possibility of more reductions in FY 2010 due to a further economic decline and poor budgeting practices.

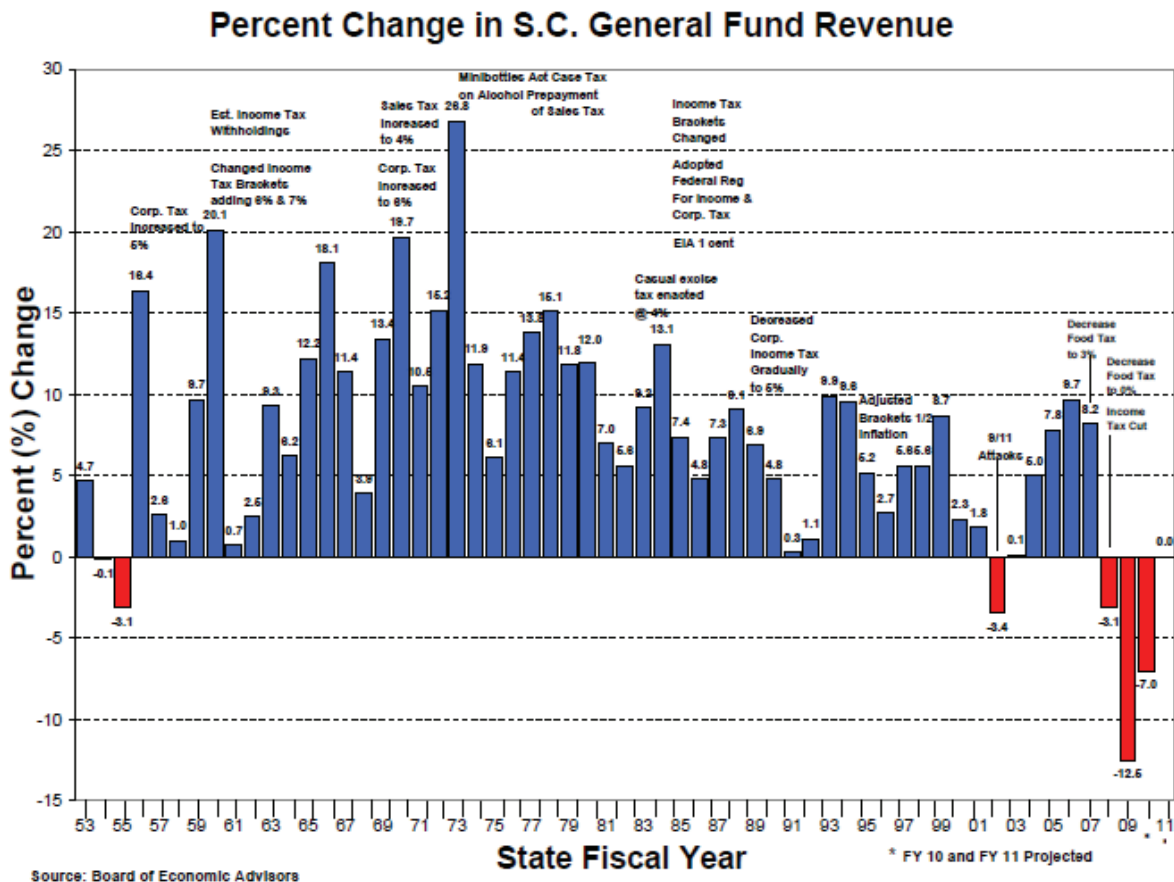
We could highlight many factors that have contributed to our current economic situation. First, the financial troubles caused by sub-prime lending practices have led major financial institutions to make a host of risky investments. A number of these institutions have either become insolvent or have had to write-down billions of dollars in losses – ultimately turning to the federal government for help.

Second, a weak housing market has made credit problems worse because of mortgage securitization. Mortgage-backed securities' success depends on high housing prices. Unfortunately, housing prices fell dramatically – bringing a decline in housing construction and home values, losses in personal wealth, and negatively impacting consumer spending. So far, there is little indication that this trend will reverse any time soon.

Despite our nation's desperate position, our federal leaders continue to advocate for new or expanded government programs. For example, the bailout/stimulus bills passed last year in Washington, and the health care reform legislation currently being debated, will add trillions to the national debt. In federal fiscal year 2009 alone, the Congressional Budget Office (CBO) reported that the federal deficit reached \$1.4 trillion – the highest on record and the largest as a percentage of the economy since the end of World War II. The CBO projects a \$1.38 trillion federal deficit for fiscal year 2010.

In previous budgets, this administration has highlighted the fact that the Board of Economic Advisors' (BEA) revenue projects are frequently far too optimistic. For instance, revenue projections from FY 2000-01 to FY 2002-03 were of \$1.185 billion higher than actual revenues. 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 make forecasting more accurate and realistic.

Currently, the BEA is forecasting that revenue will continue to decline in 2011. For FY 2010-11, the BEA estimated general fund revenue to be \$5.621 billion – roughly the same amount as seven years ago. Accordingly, we must prioritize state programs and fulfill only our citizens' most urgent needs.



Increases to General Fund Revenue

In our past budgets, we took an in-depth look at the benefit of the Job Development Fees that are dedicated for the Redevelopment Authorities (RDA) of Charleston, Myrtle Beach, and the Savannah River Site. These funds have been dedicated since 1994 for the purpose of redeveloping military bases that have closed. Even though the RDAs have fulfilled their original mission, the state is nevertheless forced to remit to the RDAs a portion of their individual income tax withholding. We believe it is time the taxpayers stop supplementing a project that has been completed. Specifically, we recommend suspending these RDAs for FY 2010-11, which will lead to **an increase of \$4.32 million in recurring general fund revenue next year.**

During the late 1990s, the four largest cigarette manufacturers reached an agreement with 46 states, known as the Tobacco Master Settlement Agreement (MSA), to settle state lawsuits 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 2010-11.

The GEAR report found several cost savings opportunities at the Budget and Control Board that would generate nonrecurring revenue for the next fiscal year. We have identified two that can easily generate millions to pay for nonrecurring budget priorities. First, the Board could sell the Tempo program's building if the Board uses a statewide contract for temporary staffing services – saving approximately **\$2 million** in one-time revenue. Second, the Board should operate as a “break-even” agency rather than a profit center, and we believe the Board's carry-forward dollars should be used for other, more vital services. These two recommendations from the GEAR report will generate a total of **\$40,000,000** in nonrecurring revenue.

The lean budget years that we are experiencing forces us, now more than ever, to make tough choices that we otherwise would not make. In 2005, the General Assembly passed legislation that transferred revenue from the General Fund to the South Carolina Department of Transportation (SCDOT) for maintenance on non-federal highways. The BEA estimated that eventually \$85 million a year would be diverted from the General Fund to the SCDOT budget. We vetoed this legislation for a few reasons. One being that the legislation didn't address how to decrease other areas of the state budget that would ordinarily be funded with this revenue. Last year, nearly \$80 million went to the SCDOT under this statute, and the same amount is expected to go to the SCDOT in FY 2011. About half of the \$80 million goes to the State Infrastructure Bank (SIB) and has been obligated for the foreseeable future, while the other half has been directed to non-federal highway road maintenance projects. The SCDOT will receive over \$460 million in stimulus dollars over the next year, including \$150 million for local projects. For FY 2011 *only*, we propose keeping **\$39 million** of the revenue that would typically go to SCDOT in the General Fund. The SCDOT is funded primarily through the state gasoline tax, and has seen some decline in this revenue source over the last couple of years. However, the agency has not had to endure the cuts – reaching 50 percent in some agencies – that other agencies in state government have been forced to confront.

In the FY 2009-10 budget, the General Assembly tasked the Department of Revenue (DOR) with generating \$48 million by utilizing its enforced-collections efforts. While we do not approve of balancing budgets using hypothetical revenue, the DOR reports that halfway through FY 2009-10 it has collected \$31.9 million of \$48 million goal and is on pace to collect between \$55 million and \$69

million. Additionally, the DOR reports that much of the new revenue is from people who otherwise do not file their taxes. The major advantage to finding and collecting from non-filers is that taxpayers are added to the tax rolls causing the revenue base to increase for future years. For this reason, and because the revenue is no longer hypothetical, we have added **\$31 million** to the revenue in the FY 2010-11 budget to pay down the interest on the loan from the federal government to pay unemployment benefits to our state's citizens.

FY 2010-11 Executive Budget

We have identified some remaining revenue generators in the “Nonrecurring Revenue” section of the following chart.

Recurring Revenue	
FY 2009-10 BEA Estimate Gross General Fund Revenue (Nov. 10, 2009)	5,621,810,481
Less: Tax Relief Trust Fund	(545,880,212)
Plus: Tax Relief Trust Fund Carryforward	-0-
Net General Fund Revenue Estimate FY 2008-09	5,075,930,269
Revenue Adjustments:	
Taxes and Fees Redirected from RDA's to General Fund	4,324,492
Transfer of Cash from DMV (10-Year License)	773,000
Transfer of Cash from DMV (Notices/Correspondence)	325,000
License Plate Replacement	400,000
Education Broadband Spectrum Lease (12 months of lease in FY 2011)	3,090,000
Adjusted General Fund Revenue Estimate	5,897,924,480
Less: FY 2009-10 Base Appropriations	5,275,343,200
“New” Recurring Revenue	622,581,280
Cost Savings:	
Agency “Savings”	170,889,036
Below-the-Line “Savings”	83,982,304
Subtotal, Cost Savings	254,871,340
TOTAL “NEW” FUNDS	877,452,620
Incremental Statewide Items:	
General Reserve Fund (1% of FY2008-09 actual revenues) (paid with nonrecurring dollars)	55,441,728
Capital Reserve Fund	(16,964,433)
Local Government Fund	(27,613,180)
Debt Service	23,172,760
Homestead Exemption Fund – BEA Est. Shortfall (Nov. 10, 2009)	99,085,991
FY 2008-09 General Fund Deficit – Repay General Deposit Account	98,216,617
Employee Health Plan	28,110,000
Total Statewide Items	259,449,483
“New” Funds Less Statewide Items	618,003,137
Nonrecurring Revenue Sources	
B&C Board – Sale of Property (Elimination of Tempo Program)	2,000,000
Transfer of Excess Cash from B&C Board	40,000,000
Transfer Cash – DHEC Waste Funds	2,700,000
Drug Lawsuit Settlement (Medicaid)	31,334,485
Taxes Redirected from SCDOT to General Fund	39,000,000
Remittance to General Fund for 2-day Furlough for “Other Funded Positions”	11,992,316
Transfer of Cash from Department of Agriculture	2,500,000
Transfer of Cash from Film Incentives to General Fund	5,000,000
Increased Tax Enforcements (to pay interest on UI loan)	31,000,000
Transfer of Cash from Employment Security Commission from reduced admin. (pay interest on UI loan)	3,000,000
Educational Broadband Spectrum Lease (Revenue from FY 2009-10)	8,545,000
Diversion of South Carolina Launch Funds	6,000,000
Anticipated FY 2009-10 Surplus (to pay down FY 2008-09 deficit)	89,247,697
Total Nonrecurring Sources	71,628,974
Other Funds	
A.R.R.A. Stabilization Funds	346,056,109
Health Care Maintenance of Effort Fund	184,706,112
FMAP Increase for FY 2011 (retained by HHS)	168,000,000
FMAP Increase (retained by other agencies)	34,188,524
Tobacco Deallocation	10,000,000

Education Lottery Revenues

Because our lottery competes with lotteries in other states, it is more important than ever that we run our lottery as efficiently as possible to maximize the amount of money going towards education. Recently we have seen the commencement of the North Carolina lottery cause South Carolina lottery to decrease. 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 recommend 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	2,600,000	2,500,000
Unclaimed Prizes	8,400,000	8,400,000
Surplus Cash	4,922,729	
Limit Retailer Commissions to 6 Percent of Sales		9,530,934
Limit Advertising Budget		4,183,870
Education Lottery Revenue	255,000,000	268,614,804

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

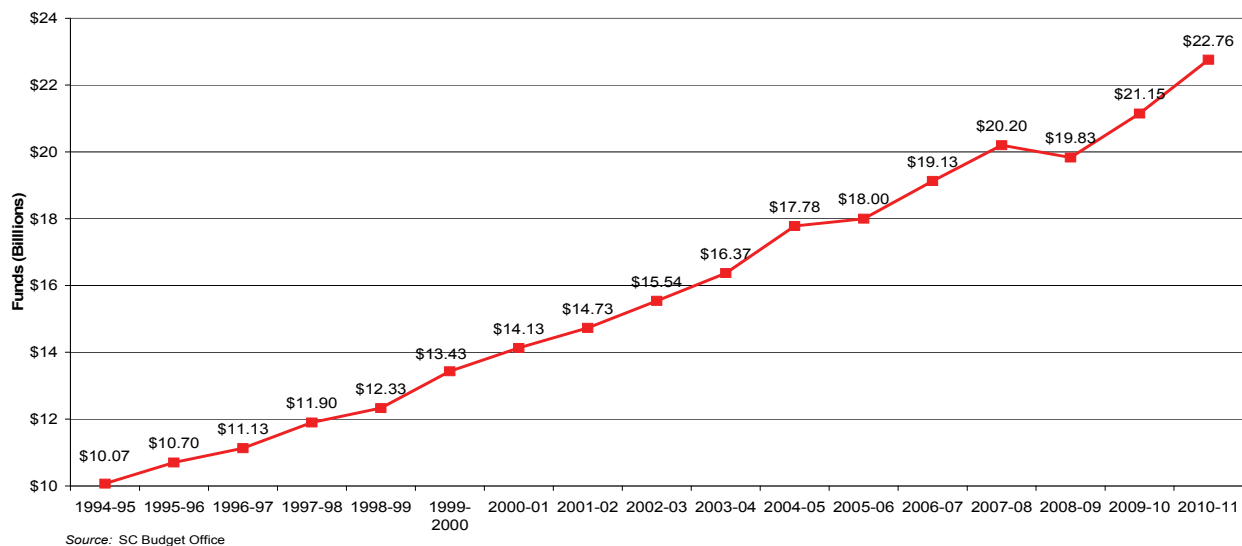
For the past six years, our administration has produced executive budgets with the overarching goal of eliminating spending that we believe is inconsistent with our state's priorities, because we adhere to the fundamental belief that excessive increases in government spending are not sustainable in the long run. In these challenging economic times in which we find ourselves, it is more important than ever that every tax dollar be directed toward the absolute core functions of state government.

We have consistently said that we need a wholesale change in the state's budgeting process that requires legislators to take a longer-term approach to spending and stop growing government faster than the underlying economy. Previous legislative budgets simply spent all of the money coming to Columbia without much consideration of a possible economic downturn. In short, during our state's prosperous times, we failed to restrain spending and, as a result, we are now forced to cut many important programs.

Planning for the Future

Although the \$1.58 billion in state budget cuts over the last two years have garnered a lot of attention, what is not commonly known is that the state's total budget has actually increased by 7 percent since FY 2008-09 and is projected to increase another 7.5 percent in FY 2010-11.

Total State Spending



Much of this increase is due to the large amount of stimulus dollars that the federal government has sent to our state. While we are not attempting to refight old battles, it is important to point out that when the federal stimulus money disappears after FY 2011, the state will have seen about \$1 billion evaporate from its budget over two years.

The Office of State Budget recently released its annual “Three-Year General Fund Financial Outlook” for FY 2010-11 to FY 2012-13. Even with the assumed two percent growth rate in sales tax and individual income tax collections – which some argue is unlikely – the state is on track to be down \$561 million from the current budget in FY 2010-11, \$1.34 billion in FY 2011-12 and \$1.44 billion in FY 2012-13.

With this in mind, it is important that when crafting the FY 2010-11 budget, strong consideration be given toward how the state will cope with the loss of another \$1 billion as it plans for FY 2011-12 and beyond. This forces us to make cuts to areas of the budget that are ordinarily, more or less, held harmless. However, with K-12 Education, Higher Education, and Health currently comprising over 80 percent of the state general fund budget, these areas can no longer be “off limits.” It would be impossible to find the necessary cuts in the remaining 20 percent of the budget and adequately fund other core functions of state government, such as Public Safety.

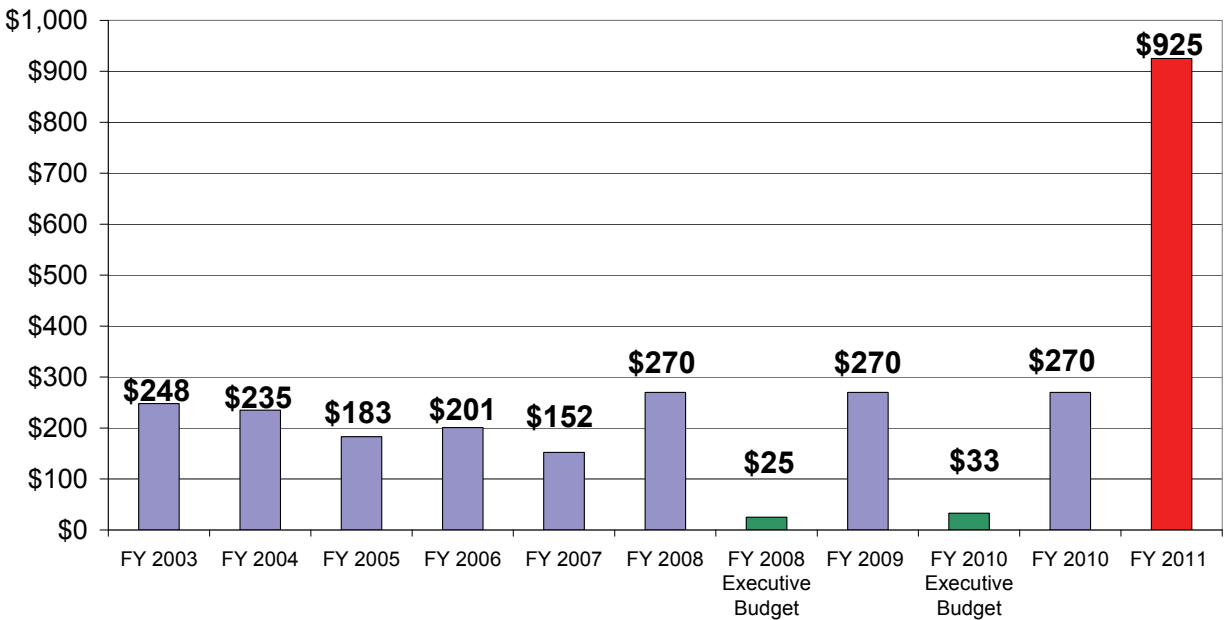
Annualizations on the Rise

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 serve only to delay tough decisions for another year. The frequency with which the General Assembly uses annualizations is evidenced by the fact that annualizations nearly doubled in the two years preceding the current budget year. With the passage of the FY 2009-10 Appropriations Act, which included roughly \$1 billion in federal stimulus dollars, the annualizations reached \$920 million – an unprecedented level. Whether we like it or not, we will be facing a \$920 deficit in FY 2011-12.

What is most troubling about our current circumstances is that much of the spending on core functions of state government – education, public safety and health – is now coming from one-time funds. For instance, in the FY 2009-10 budget, K-12 education is receiving \$180 million in federal money that will not exist in two years. The state will have to find this money somewhere in FY 2011-12, or education will be cut another \$180 million. The Department of Corrections, the Department of Public Safety, and the Department of Health and Human Services also have a significant portion of their respective budgets coming from one-time funds.

We believe there needs to be a limit on annualization spending, which is why, in the future, we believe that annualizations should not exceed one percent of total estimated revenue for a fiscal year. Each of our previous Executive Budgets has met this benchmark; however, we understand that that is not possible this year because of the massive amount of stimulus funds that are included in the budget.

South Carolina Annualizations Since FY 2001-02
in millions



Unfunded Liabilities

State and local “governments used rosy investment earnings projections, typically 8 percent a year, to make their promises appear more affordable than they really were.”

Never truly a sustainable strategy...the current financial crisis has thoroughly exposed the folly of it...the path to solvency, if there is one, runs through the hard business of restructuring – i.e., trimming – benefits. This will take political courage...the truth is that state and local public employees often enjoy far more generous pensions and medical benefits than the taxpayers who fund them...

This is a ticking financial time bomb, and the time to disarm it is now.”

- “State and local pensions plans are on a path to failure.” Editorial Board, *The Washington Post*, January 2, 2010

Our retirement system’s unfunded liability was over \$11 billion as most recently reported in mid-2008. While these numbers have likely worsened given last year’s financial crisis, this \$11 billion obligation is only a part of the problem. We unfortunately have another \$9 billion in unfunded costs

related to health care for public retirees that are commonly referred to as Other Post Employment Benefits (OPEB) costs.

The combined \$20 billion in unpaid political promises were the key reason this administration fought against the 2008 efforts to double the guaranteed cost-of-living increase for retirees – a move that cost our retirement system over \$2.5 billion it could ill afford.

The legislation which passed over our veto purported to offset these billions in new costs by assuming that our investment returns would increase from 7.25 to 8 percent. We pointed out at the time that even the retirement system's own actuary reported that our optimistic assumptions were 11 percent higher than the national assumed rate of return for public funds and 33 to 43 percent higher than the assumed returns for the retirement systems in our neighboring states of Georgia and North Carolina.

Our veto message related to this legislation raised the following concerns:

This bill artificially and arbitrarily raises the projected rate of return for the retirement fund so that more spending can take place now – though we have already accumulated over \$20 billion of unpaid for political promises. We have absolutely no plan for addressing the existing liability – which would put you in jail if you did this with private pension fund assets – and yet we are going to add to spending commitments.

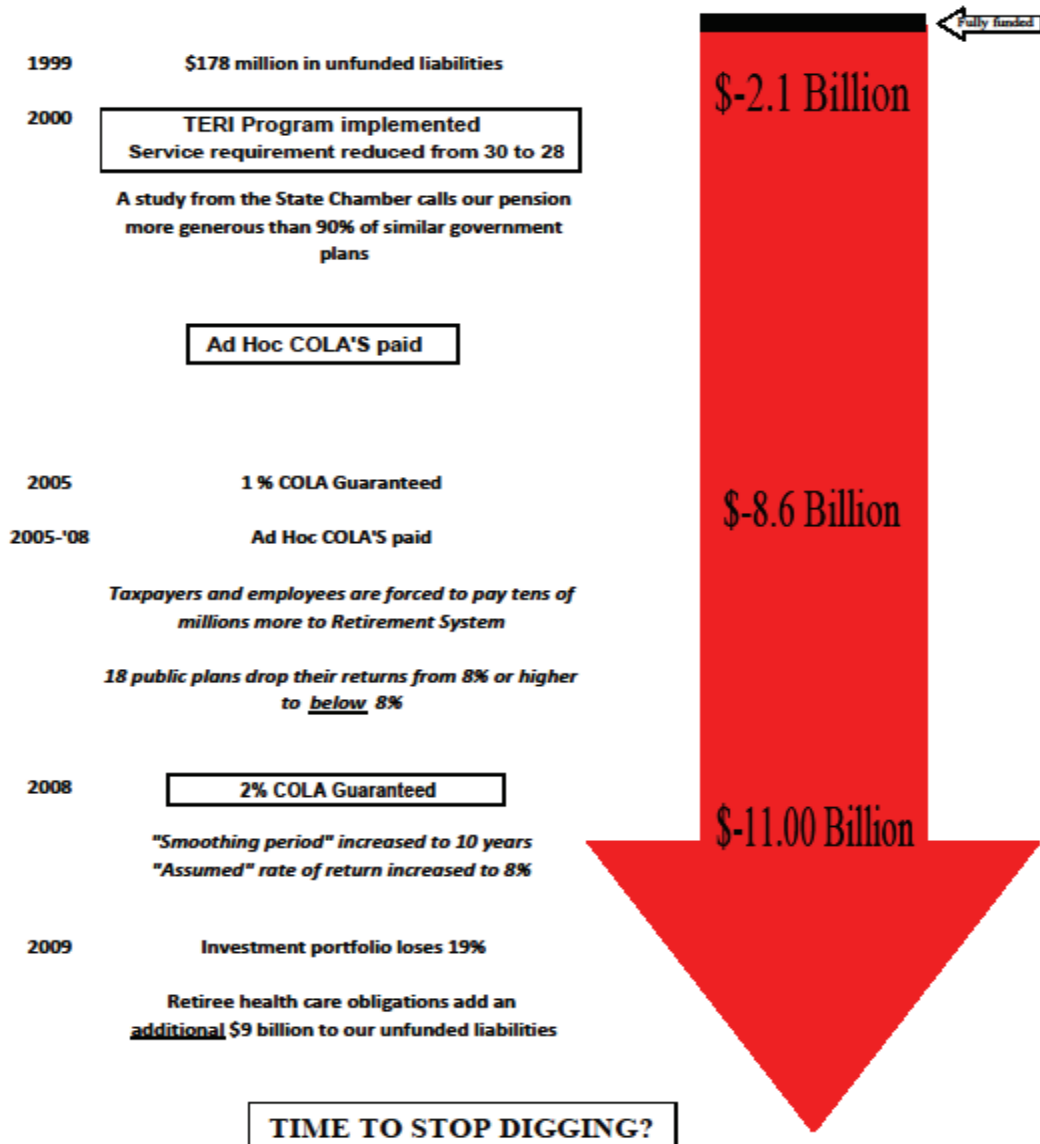
For the sake of our residents and retirees we would have been glad to have been proven wrong or merely overly cautious. However, our concerns about these overly optimistic investment projections unfortunately proved to be accurate sooner than we would have thought. Instead of achieving the projected 8 percent gain last year, the Retirement System's investment portfolio lost over 19 percent – performance that was a full 27 percentage below projections.

Largely as a result, the system's net assets dropped over 23 percent last year, equating to a cash outflow of \$6 billion over a twelve month period. We understand that the state is a long-term investor so we can't rely on the results from just one year. However our historic performance shows an annualized three year return of negative 3.6 percent, an essentially flat performance over a five year time horizon, and an annualized positive return of 2.6 percent over ten years. It will take much more than a change in our investment strategy to get us out of this deep financial hole we have dug for ourselves.

Even if these optimistic assumptions of annualized 8 percent returns somehow come true, our fiscal situation is still quite dire as that would still leave South Carolina taxpayers on the hook for at least \$20 billion in unfunded liabilities. This equates to over \$10,000 in hidden debt obligations for every taxpayer in our state. If we continue to ignore these problems, our obligations will likely to grow exponentially worse as has been predicted by leading financial experts like Warren Buffet.

As shown below, generous increases in benefits over the past decade have largely been responsible for the huge financial burden we are placing on future generations.

A DECADE OF DIGGING A HOLE OF RETIREMENT DEBT



Continuing to ignore these challenges is not a responsible option as it essentially leads to what former US Comptroller General David Walker refers to as “fiscal child abuse.” Governing Magazine’s Girard Miller further reported last January that public pension reforms “are virtually unavoidable, especially in light of the impact that the market meltdown has had on the taxpayers who contribute a majority of the funds that pay for these benefits. As one reader wrote me last week, ‘a public pension system cannot be sustainable if its retirees live far better off than the taxpayers who support them.’ That’s like welfare in reverse.”

In order to maintain our system’s solvency, we must make long overdue changes now to lessen the potential pain for both future retirees and taxpayers. In 2007, the Government Efficiency and Accountability Review (GEAR) Committee made the following common-sense recommendations for non-vested employees to begin shoring up the 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.
- Completely 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 a decade ago.

Unfortunately the implementation of these reforms has languished while the retiree benefits package has grown more generous. While action on these proposals is desperately needed to improve the financial condition of our retirement plan, we must do much more to maintain the solvency of the system and protect our state’s credit rating.

Governing Magazine’s Miller pointed to one important fix last January in writing that “those employers who permit 40- or 50-year-old retirees to receive full medical benefits at taxpayer expense, the plans are likely to be unsustainable going forward without significant restructuring....cost caps need to be installed in order to prevent runaway medical inflation from hitting future taxpayers.”

In South Carolina, state agencies (and the taxpayers who fund them) have traditionally paid the same percentage of health care costs for retirees as they do for active state employees. Over the past ten years, that has meant taxpayers have typically picked up between 67 to 82 percent of the health care costs for retirees and their families. As represented by our growing \$9 billion health care liability, this is simply not sustainable. If we are going to begin seriously addressing our unfunded health care benefits, we must ask retirees and their families to help by paying a greater portion of the cost of this benefit.

Our retirees' total health care cost is projected to be approximately \$380 million this year, which leaves taxpayers paying over \$260 million for this benefit. This burden has dramatically increased

from less than two percent of an agency's payroll a decade ago to 3.5 percent in the current budget year - over an 80 percent increase.

If the state were to drop this retiree health care surcharge back down to 2.65 percent of payroll costs, that would free up about \$65 million in recurring revenue that we could and should allocate towards the underfunded trust fund established for OPEB costs. The benefits would be approximately a \$2 billion reduction in our \$9 billion OPEB liability – a 10% reduction of our total \$20 billion in unfunded liabilities. While this would still leave us with significant financial challenges, it would be an important first step towards improving the financial health of our retiree's health care system while reducing the fiscal burdens we impose on future generations.

Allocating these funds towards the OPEB Trust Fund would require retirees to start paying approximately 46 percent of the insurance cost not already covered by Medicare. This is a reasonable amount that is similar to plans offered by other states. Taxpayers in South Carolina currently pay a very generous \$4200 in average annual health care cost for a state retiree. By comparison, taxpayers in Florida pay a maximum of \$1800 a year in health care costs for a state retiree. Our proposed change to the plan would still leave South Carolinians paying for more of our retirees' health care than our neighbors in Florida do for their retirees.

We believe it is both irresponsible to make tens of billions of dollars in political promises without having the means to pay for them. This is not fair to our state employees and retirees who are counting on benefits that we may not be able to deliver given other core services that government must provide. This is not fair to our residents who depend on core government services such as education, public safety, and health care as their budgets are under more and more pressure as finite resources go to pay for these retirement benefits. And it is certainly fiscal child abuse to burden our children and grandchildren with this legacy of debt that is promised and spent before many of them are even born.

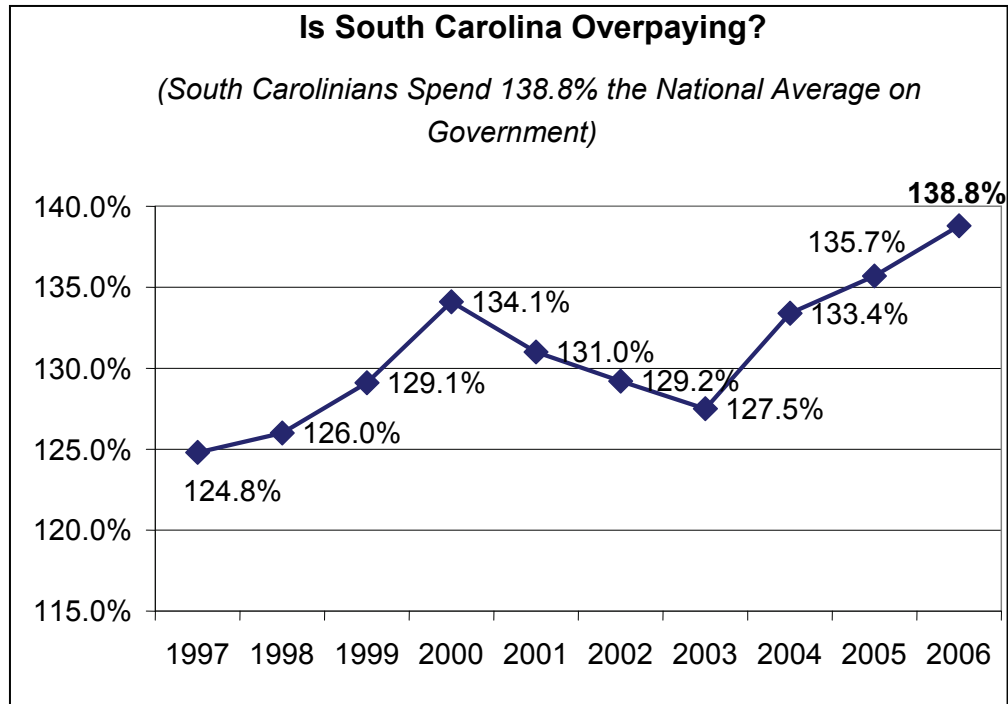
Three years ago in his letter to Berkshire Hathaway shareholders, America's most renowned investor Warren Buffett talked about "woefully inadequate" funding for public pensions as a "time bomb." Similarly The Washington Post on January 2nd, 2010, opined that, "this is a ticking financial time bomb and the time to disarm it is now." Our time is running short. We are eager to work with the General Assembly this session to implement our proposals or any that they may have to begin to address this looming crisis before it is too late.

Outspending the Competition

It is important that South Carolina remains competitive in this ever-changing global marketplace, and to do this, state government must be held accountable for every tax dollar it spends. In FY 2007 and FY 2008, South Carolina's government spending grew at the second fastest rate among Southeastern states. In fact, government spending increased by over 30 percent during this time period, according to the National Association of State Budget Officers.

Compared to the rest of the nation, up until the recent economic downturn, government in South Carolina cost almost 140 percent the United States average. This figure is cause for concern as we

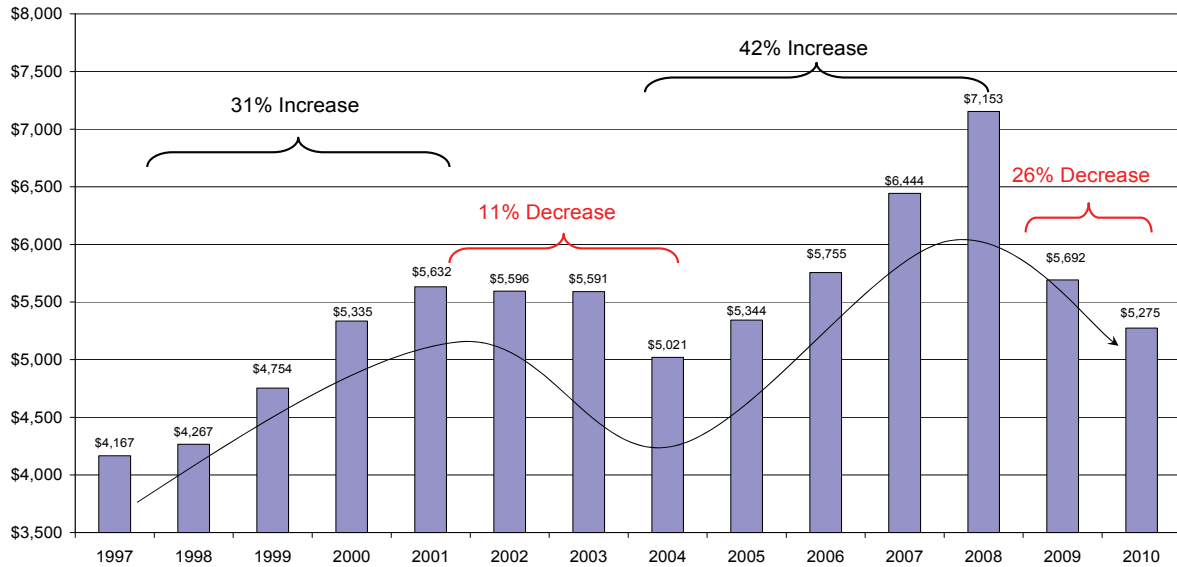
strive to compete against other states and attempt to invest valuable tax dollars back into the private sector.



Population Plus Inflation

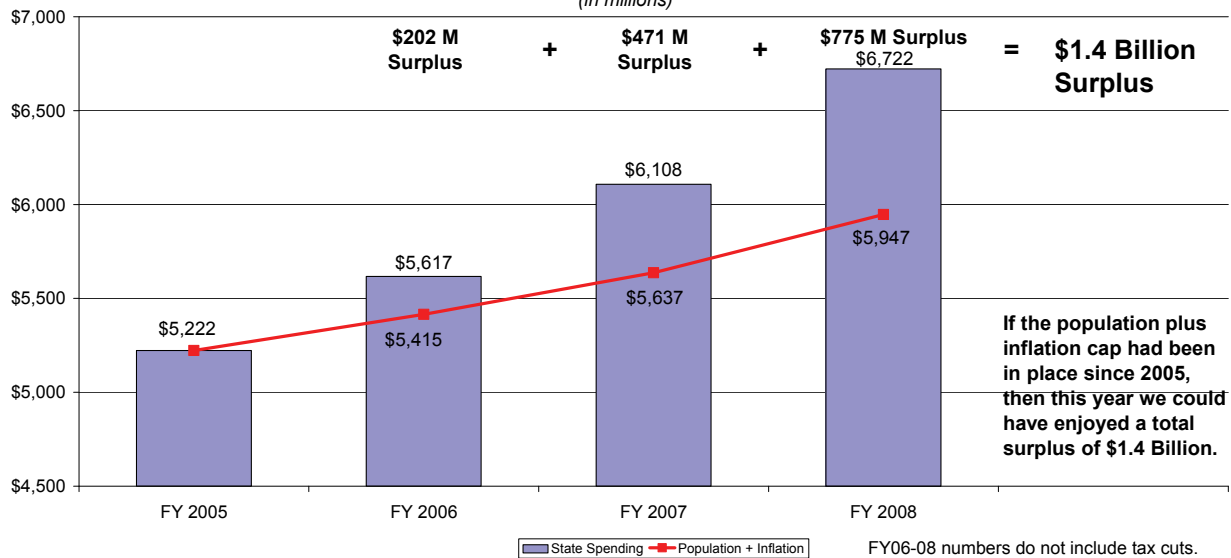
South Carolina has historically been on a constant budgetary roller coaster ride. When revenues are up, spending dramatically increases. When revenues are down, budgets are slashed to the bone – jeopardizing the state’s ability to deliver core government services to its citizens. The chart below reflects the dramatic ups and downs in the state budget over the last 14 years.

Peaks and Valleys Approach to State Spending (recurring and non-recurring dollars, in millions)



In past years, we have made our case for limiting government growth 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 four budgets where it was needed the most.

State Government Growth Under Population Plus Inflation Spending Cap FY2005 - FY2008 (in millions)



While it is true that some cuts would still have been necessary over the last year, it is also true that the cuts would not have been as deep as the ones we are currently experiencing. Likewise, citizens would not have become dependent on these services, only to have them disappear a couple of years later. Furthermore, had the state saved some of the money that was spent above the population plus inflation threshold, or paid off some of the unfunded liabilities discussed above, the state would find it in a much better fiscal position to emerge from the global recession. As the following chart demonstrates, had a population plus inflation spending cap been implemented in FY 2005, over \$1.4 billion potentially could have been saved for the current tough budget years, and prevented some difficult cuts.

We believe that when economic times are good, budget writers must resist the temptation excessively to spend tax dollars on new programs that cannot be sustained during challenging financial times. Recognizing that in the current political system in which we operate it is not realistic to expect the entire General Assembly to agree to save a dollar instead of spending a dollar, the only way for the state to prevent ending up in the same position that we are in today is to constitutionally limit the rate at which state government can grow.

We'd thank the House and the Senate for taking action last year by debating several pieces of legislation that would positively impact the boom-bust cycle so harmful to our state's budget practices, including Speaker Harrell's proposal to increase the General Reserve Fund by two percent in addition to spending cap bills on the House and Senate side. However, there are two concerns that we had with these bills from last year and they fall into two categories.

The first relates to the cap itself. We believe the more appropriate cap to use would be a population-plus-inflation model because it is more predictable and it is more responsive to the current economic conditions. For this reason, we would respectfully urge both bodies to adopt population plus inflation as the measure for determining the cap.

Our second concern relates to what happens to the money over and above the cap. A spending cap that allows more spending is really no cap at all which is why we prefer money held in a spending limit fund to be prioritized in two possible ways. Our first priority would be to dedicate surplus dollars to paying down the roughly \$20 billion in the state's unfunded liabilities linked to retirement. In the unlikely scenario these liabilities are fully paid back, we would then propose splitting the remaining funds equally, with half refunded to the taxpayer and the other half going to capital projects.

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 complete and unrestrained access to information regarding how their hard-earned tax dollars are being spent by state government. In this vein, we'd thank Representative Nikki Haley and Senator Harvey Peeler for their efforts last year for helping make both legislative bodies more accountable to the taxpayer. We also applaud the Comptroller General's office for its efforts to maintain a state Spending Transparency website which gives citizens 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 allows citizens to review state spending by agency and budget year. The site is located at <https://ssl.sc.gov/SpendingTransparency>. This website gives voters the ability to hold government accountable for its decisions.

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 2009, South Carolina's government structure still largely resembles the government first established by a 114-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 continue to be left behind if we fail to modernize and restructure state government.

The 1895 state Constitution was adopted in 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. Tillman was elected governor in 1890, and in his inaugural address he summed up the 1895 Constitution's purpose and intent by stating that "[t]he 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. Although this Constitution nominally referred to the governor as the "chief executive," the long ballot and other measures adopted by the General Assembly prevented him from carrying out his duty to manage the state's executive functions. For example, even though many other states were in the midst of 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, 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 diluted executive power by creating numerous state agencies that are not directly accountable to the Chief Executive. Until 1993, state government amassed **145 agencies** – not one of which was directly accountable to the governor. Most agencies were governed by a board or commission appointed by the governor, Legislature, or both.

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).

This menagerie of governance forms has resulted in fragmentation, confusion, redundancy, and a lack of accountability in state government that continues to this day. In fact, fourteen major studies over the course of 87 years came to the same conclusion: the General Assembly should consolidate state agencies and centralize executive authority.

Fifteen years ago, a movement to restructure and modernize state government began. Now, 15 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

For six years, this administration has said that government should be reorganized to run like a business – focused exclusively on its customers. Becoming more efficient, effective, and accountable to the taxpayer ultimately results in less waste and better services.

Unfortunately, South Carolina's 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.
- South Carolinians pay more than 17.2 percent of their 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 2008-09, 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 \$1.5 billion budget shortfall that could have been mitigated if the state had 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 us recover from the current budget crisis, but will 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 bi-partisan 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
- Seeks continuous improvement of the quality of policies and procedures

The study 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 15 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 fully to 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, finding ways to reduce costs, increase accountability, improve services, 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

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.

over the next few years – a significant amount that could have helped relieve our current budget shortfall.

Study after study has concluded that our current government structure is cumbersome, fragmented, inefficient, and unaccountable. Since previous restructuring efforts have proven the cabinet system works, it is time for the General Assembly fully to 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, and provided customers with an increasing number of online services, all while saving over \$65 million General Funds since 2003. As recently as FY 2008-09, 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 itself 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 personnel 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 fewer full-time employees 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 operations for eggs, saving taxpayers \$750,000 annually. The agency also cut 70 teachers and administrative staff and replaced them with media-based lessons, 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 since 2003, including: 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 \$20,000-per-month contracts with two lobbyists.

These are just a few examples that prove a cabinet form of government is far more likely to create greater efficiencies and accountability than is our current structure.

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)

Although the weakened national and state economies have deepened our budget shortfall, it is undeniable that spending restraint, better budgeting practices, and a more efficient government structure could have softened the economic blow.

While these times are challenging, it is also an opportunity to streamline and simplify government and make the chief executive directly responsible for government's performance. 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.

We have been very pleased to see the House of Representatives pass several parts of our restructuring plans over the years, including the creation of a 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 for 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 hybrid legislative/executive board, the Budget and Control Board, to oversee the state's administrative support functions. To better manage support services to state agencies, we propose placing crucial Board-managed administrative functions within a cabinet-level Department of Administration.

In 1919, the General Assembly created 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 five-member Budget and Control Board is an enormous institution that 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 Board is dominated by legislative influence that undermines the constitutionally-based principles of separation of powers and checks and balances between the legislative and executive branches.

This cumbersome structure results in a lack of accountability and contributes to increased costs at the Board. The chief executive of any well-run company or well-run state must have direct, clear lines of authority to be successful.

As previously mentioned, the GEAR report highlighted the inefficiencies that exist under the current executive framework. In addition to finding \$500 million in potential savings, the GEAR report also found that the Budget and Control Board could release at least \$20 million in carry-forward funds to the General Fund, a surplus due to 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 government. As the state's chief executive, the governor should be responsible for the central administration of the executive branch – a responsibility given to every other governor in the nation.

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

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 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 executive branch power, 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 conflicting public policy. Although ostensibly for the voters' benefit, the current Executive Branch structure results in a bifurcated system with no clear lines of responsibility. South Carolina will be better served by having the governor appoint these officers.

For example, consider 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 – yet no clear lines of accountability exist. The governor has little authority to implement any reforms, no matter how desperately they are needed and no matter how loudly 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. We are not suggesting that a governor-appointed Superintendent of Education will solve all of our education problems. However, a cabinet-level Superintendent will provide one coherent education policy throughout

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

Another example is our administration's concerns over the recent program created by the Lieutenant Governor's office called Senior Shield, which helps senior citizens identify legitimate businesses in the state. While our administration supports this program's good intentions, we do not believe the state should be spending scarce dollars on a program 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.

We propose reducing the number 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).

Allow the Governor to appoint the following cabinet positions, 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 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 the government disjointed, unwieldy, and unaccountable. We have a hodgepodge of 70 independent agencies, commissions, and departments, which provide hundreds of often-redundant programs or services.

Although the General Assembly made limited reforms to the executive structure in 1993, more than 80 percent of our executive agencies remain outside the scope of the governor's authority. To provide better service and better value to our clients – the taxpayers – we need to consolidate departments under the cabinet.

The 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
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 nearly \$17 million for FY 2010-11.

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 the following plan:

State Department of Education

1. Transfer the State Board of Education's powers 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**

We propose that those agencies' current responsibility be given to the Superintendent of Education, and that each entity's executive board would serve in an advisory capacity.

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, noting that five of the eight agencies are outside the governor's cabinet. The LAC found that multiple agencies provide similar services – increasing the cost of coordinating health care services. Predictably, the costs were due to administrative overlap primarily in the areas of finance, personnel, and IT.

The LAC report also found, because 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.

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 it findings. Our main concern is the desire for services that efficiently and effectively meet consumers' needs – which our current system clearly fails to do.

We propose to merge these health and human services agencies into a single 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: \$4,501,147**
2. Division of Mental Health (currently Department of Mental Health). **Savings: \$5,563,376**
 - 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: \$78,434**
3. Division of Disabilities and Special Needs (currently Department of Disabilities and Special Needs). **Savings: \$2,052,701**
 - 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: \$360,654**

Department of Rehabilitative Services

1. Merge the Vocational Rehabilitation Department with the Commission for the Blind. **Savings: \$798,931**
2. The administrative responsibilities of the Vocational Rehabilitation Department and the Commission for the Blind would be given to a 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 changes at DOT are 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 eliminating funding for a Washington lobbyist.

While these results are encouraging, it might take more than one attempt to achieve true reform. The DOT's Commission continues 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 existing system by eliminating the Commission.

The following proposal will allow the Department of Transportation to be more accountable and cost effective, and most importantly, will improve transportation services.

State Department of Transportation

Transfer the powers of the Commissioners of the state Department of Transportation to the Secretary of the Department of Transportation.
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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 the Department of Health and Environmental Control (DHEC) should be split into two separate state agencies under a more accountable cabinet structure. This proposal will bring us in line with similar agencies in neighboring states, like the North Carolina Department of Environment and Natural Resources and the Georgia Department of Natural Resources – both of which provide environmental regulation and enforce wildlife laws.

Our current system's inefficiencies 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 of this crucial state resource. Additionally, the need for more accountability at DHEC is obvious due to numerous incidents where the agency has failed to balance business interests with the duty to regulate environmental pollution. Without direct accountability, DHEC will continue to avoid the consequences of its mistakes.

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: \$957,607**
 - 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: \$453,440**
 - 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 divide the Department of Corrections' functions from those of the Department of Probation, Parole, and Pardon Services (PPP). Our proposal creates a single cabinet agency that will ensure offenders are managed by the same entity from initial incarceration to final release. 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 have similar budgets, even though the DJJ Parole Board hears far fewer cases each year. Because both boards have similar missions, their merger presents an opportunity to realize significant cost savings.

Department of Corrections and Probation

1. Division of Corrections.
2. Division of Probation, Parole and Pardon Services. **Savings: \$622,126**
 - 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 is currently facing 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, and planning, a comprehensive strategy can stabilize and energize South Carolina’s economy. 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 for South Carolina:

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

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 nearly-identical missions, along with our tendency to allow powerful legislators to spend significant resources on local projects that do little to promote lasting economic development, minimizes the effect of these resources.

For an example of more effective use of resources, look to the Workforce Investment Act (WIA), that 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 \$79 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

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 into one agency. Unfortunately, the General Assembly did not include this change in its Restructuring Act of 1993. By contrast, the North Carolina Department of Cultural Resources was formed in 1971 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 our proposal will streamline these agencies and reduce administrative costs as follows:

Department of Literary and Cultural Resources (DLCR)

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: \$164,606.** We also propose moving the Institute for Archeology and Anthropology from USC to this division. **Savings: \$496,812.**
3. State Library. **Savings: \$90,121.**

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. 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 activities. 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

Government programs, once launched, never disappear. Actually, a government bureau is the nearest thing to eternal life we'll ever see on this earth!

– Ronald Regan.

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. For example, Texas enacted one of our country's most progressive sunset programs in 1977. Under the Texas Sunset Advisory Commission statute, the charter of nearly every state agency generally expires every 12 years, unless renewed by the Legislature. The Sunset Commission reviews each agency on a 12-year cycle – one agency is reviewed each year. The 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 Texas Legislature adopted 207 out of 230 recommendations made by the Texas Sunset Advisory

Commission, which resulted in \$17 million in taxpayer savings. 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. In those states, 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.⁵

South Carolina officials interested in running our government more effectively and more efficiently have a lot to learn from the experiences of Texas and Florida. A South Carolina Sunset Commission could identify and eliminate waste in government agencies, while improving the quality and lowering the costs of government services. We strongly believe that a regular review of existing state agencies will provide substantial benefits to our taxpayers.

⁵ 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.

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 increasing amounts of 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 time period, South Carolina has consistently performed poorly on the SAT compared to other states.

SAT Results: Ranking of Southeastern States

State	2004	2005	2006	2007	2008	2009
Kentucky	5	3*	5	4	4	1
Tennessee	3*	1	1	1	1	2
Arkansas	3*	5	2	3*	2	3
Mississippi	7	3*	6	5	3	4
Louisiana	1*	2	3	3*	5	5
Alabama	1*	6	4	6	6	6
Virginia	6	7	7	7	7	7
North Carolina	8	8	8	8	8	8
Florida	9	9	9	9*	9	9
Georgia	10	10*	10	9*	10	10
South Carolina	11	10*	11	11	11	11

*Tie

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. Although we have made many changes over the years – such as creating the Offices of Public School Choice at the Department of Education – it remains to be seen whether these initiatives will propel our students forward in global competition. We know that incremental increases are not enough, and we must focus our energy on developing an educational system that makes the most of the available funding and meets students’ needs.

Challenges in Student Performance

Parents send their children to school with the expectation that their children will be ready for challenges ahead. 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 state of affairs is unacceptable in today's highly competitive world.

Falling Short of the 2010 Goal

In 1998, the Education Accountability Act (EAA) set the ambitious goal that South Carolina's student achievement would be ranked in the top half of states in five target areas by next year. Although student performance has improved since that time, the students' scores on current rate of progress with regard to the NAEP, SAT/ACT, on-time graduation rate, closing achievement gaps, and Advanced Placement programs is insufficient to reach EAA's goal. Here is 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 are 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 scores – a key indicator 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 allows more students to take the SAT than other states, which results in a lower average score. However, a greater percentage of students in Georgia and Virginia

take the SAT than South Carolina, yet these states still have higher SAT scores. In fact, 71 percent of Georgia's high school students and 68 percent of Virginia's high school students took the SAT in 2009 compared to 67 percent of South Carolina's high school students, yet both states had average scores higher than South Carolina (1,460 in Georgia and 1,521 in Virginia, compared with South Carolina's score of 1,452).⁶ During the past five years, South Carolina's composite reading and math score has remained virtually constant while the Southeastern average has slightly increased. Currently, we fall 57 points below the national average of 1,509. This year's scores ranked 48th among other states – ahead of only Hawaii and Maine.

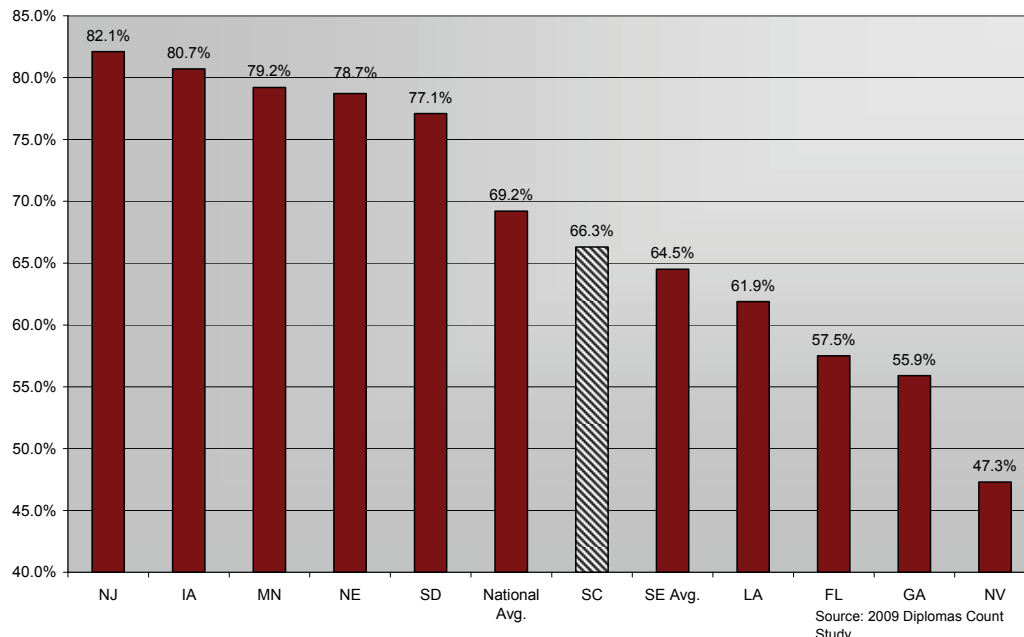
3. Advanced Placement (AP)

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 – approximately 73 percent of AP participants in 2008 were Caucasian, 16 percent were African-American, four percent were Asian, three percent were Hispanic, and less than one percent were Native American.

4. Graduation Rate

Year after year, high school graduation rates in South Carolina are unacceptably low. According to the 2009 version of Diplomas Count, a study performed for the Bill and Melinda Gates Foundation, 66.3 percent of South Carolina's students enrolled in 9th grade in 2005-06 will graduate high school four years later – putting us 37th nationally. The same study found that approximately 1-in-3 students – or 122 pupils each day – dropped out, were held back, or failed to complete the full diploma requirements.

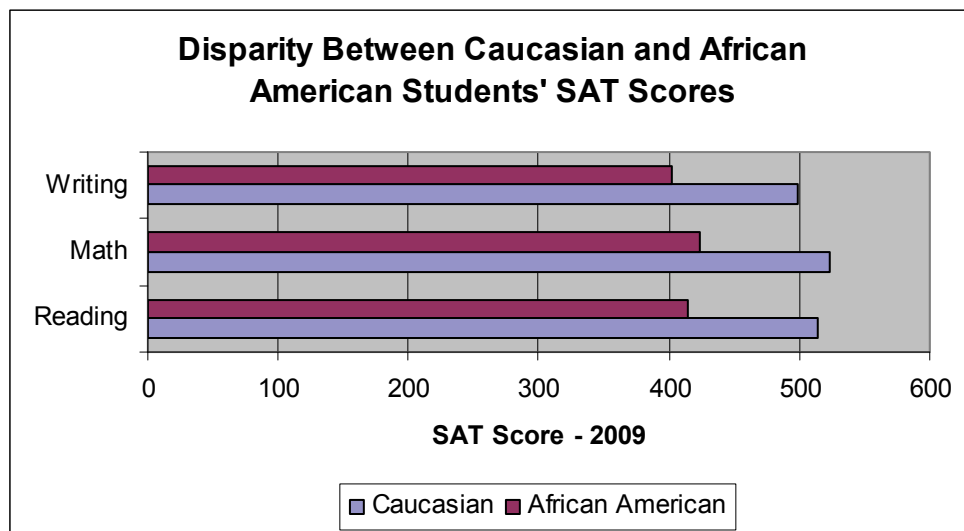
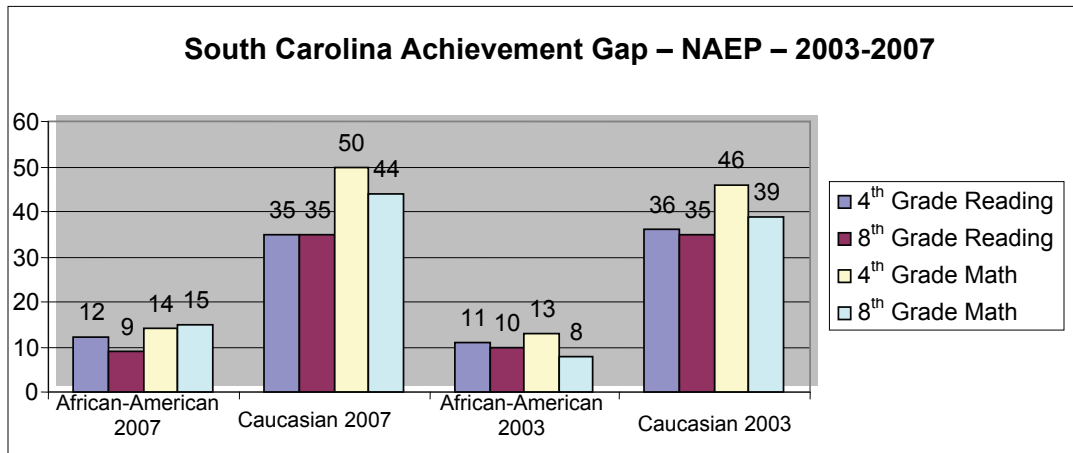
School Year 2008-2009 National High School Completion Rate



⁶ Since 2005, the SAT has included a writing section – making 2,400 the highest possible score.

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 2009, there was a 100-point difference between reading and math scores of African-American and Caucasian children, and almost a 100-point difference in writing scores 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.

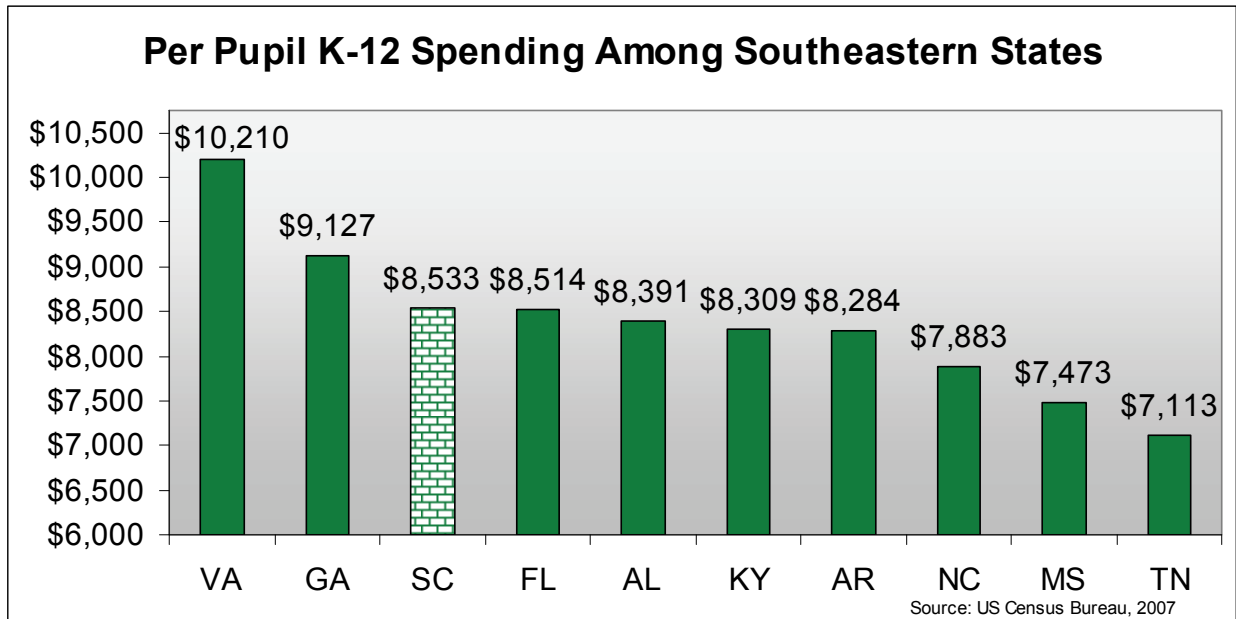


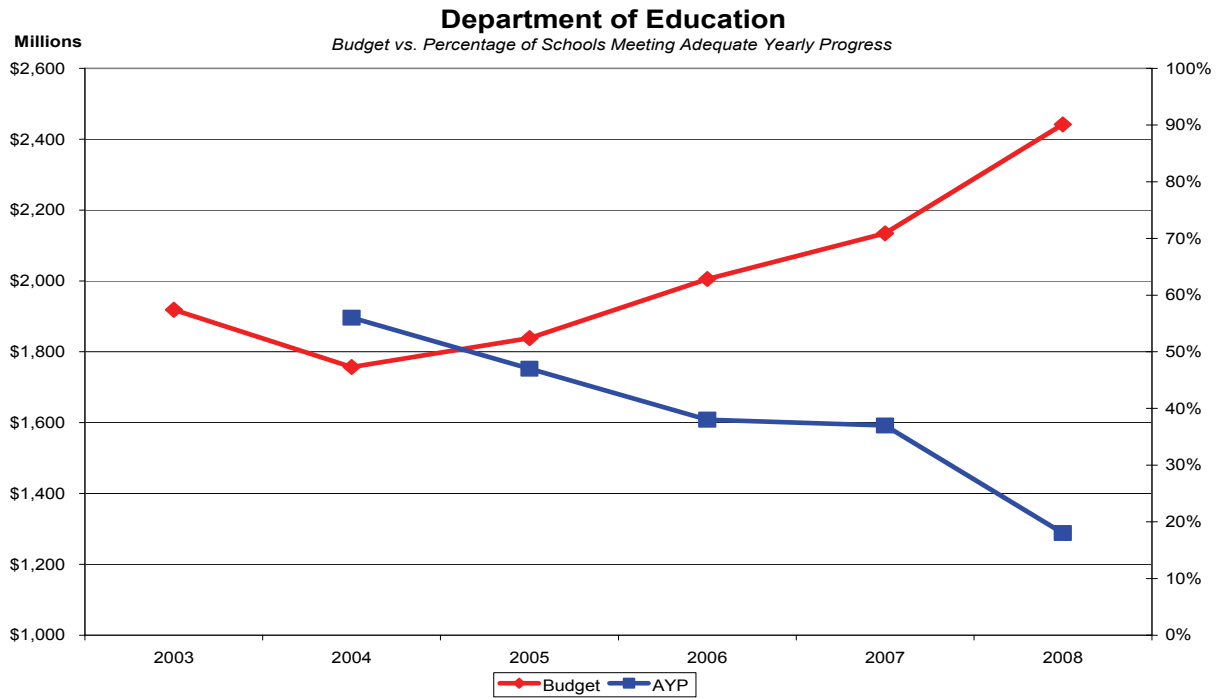
The Need for Postsecondary Education

For many years, South Carolinians were able to find decent paying jobs in manufacturing or other industries, which required only a high school diploma. Today, our citizens need more than a high school diploma to find a job in the competitive global community. Our low high school graduation rates negatively affect our state in other ways as well. 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 per year). 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, the state spends more than \$320 million in health care costs for high school dropouts over the course of the dropouts' lives. Much more needs to be done to equip students to finish high school on time and succeed 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 approximately nine 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.





Throwing increasing amounts of money into a flawed system will not change the quality of our system's educational product. We believe that focusing more money into the classrooms would go a long way toward achieving our progress 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 our education system 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 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

Approximately 74 percent of American students remain in government-assigned public schools, and the majority of South Carolina's students are assigned to a particular public school because of the students' zip code. Unfortunately, only 11 percent of schools in our state were rated "Excellent" according to the 2008 School District Report Cards issued by the Education Oversight Committee. By contrast, 38 percent of schools in South Carolina were rated "Unsatisfactory" or "Below Average." Although the Report Card is not 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. 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 our neediest students deserve more choices, the Education Oversight Committee (EOC) has recommended school choice programs 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 do not improve in the Absolute Rating on their 2009 School Report Card, students in these schools will be allowed to transfer to a different public school with a higher Absolute Rating. The child's district of residence would provide to the receiving district an amount equal to the receiving district's per-pupil revenues. 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 the EOC credit for putting students' needs ahead of any other consideration. 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.

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 demand for their children's education. 10 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, Louisiana, Iowa, Pennsylvania, Ohio, Delaware, 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, Georgia, Iowa, Pennsylvania, Utah, and Rhode Island.

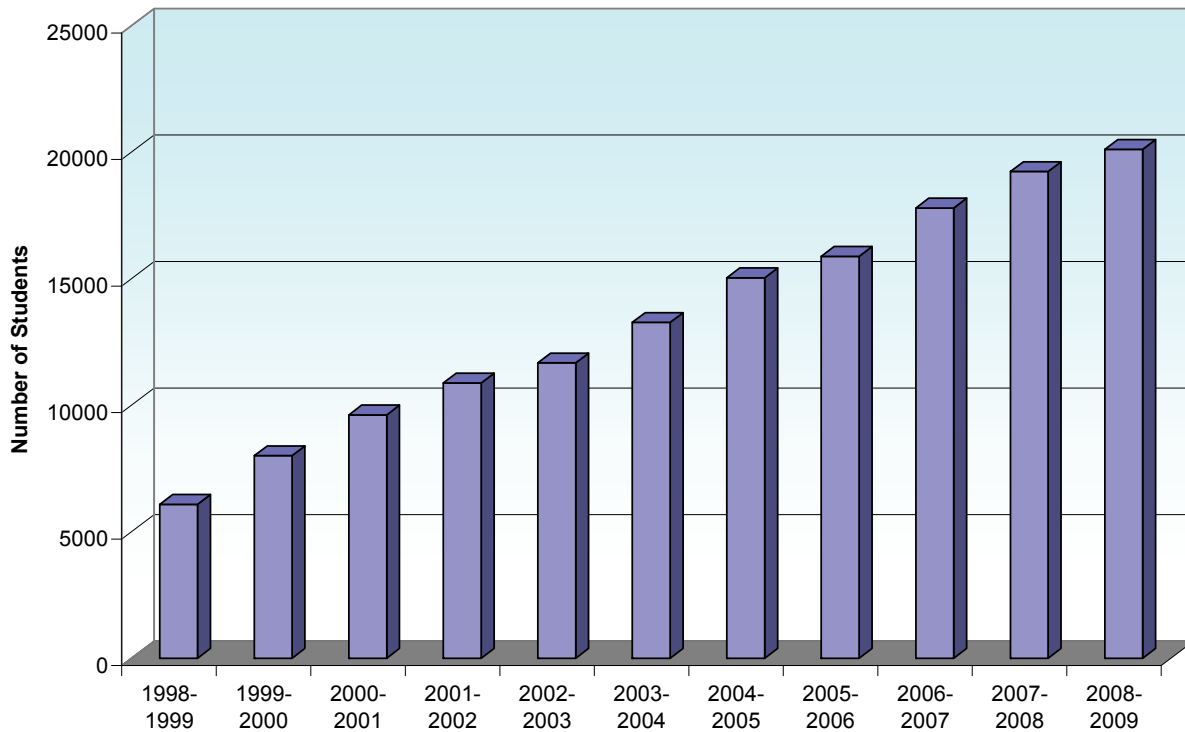
The chart below describes a few of the choice programs that have been implemented in other states:

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.

Florida implemented education scholarships 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.

Approximately 74 percent of students in Milwaukee's school choice program – the nation's largest and oldest program – graduate high school in four years, compared to 46 percent of students in Milwaukee's public school system. The Milwaukee program has also achieved substantial savings for taxpayers.

Milwaukee Parental Choice Enrollment



Source: U.S. Census Bureau, 2007

South Carolina provides scholarships to four-year-olds through the Child Development Education Pilot Program. We would like to see this kind of scholarship 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 stalled in the South Carolina General Assembly. Each year since 2003, there has been an effort to create an education scholarship program in South Carolina, and each year the effort failed to survive the legislative process.

The only school choice legislation to pass both the House and the Senate was the Open Enrollment Bill in 2007. Unfortunately, the bill was rife with capacity limitations and student transfer 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, and the bill likely would have had an insignificant impact on expanding choices for students most in need of improved educational options. As a result, this administration vetoed this legislation, which the General Assembly sustained.

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 program in Illinois and the scholarship donation programs 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 like 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 used 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 those who want to see true reform. Now, more and more people are realizing the potential positive impact that school choice can bring. In 2008, Reverend Al Sharpton, who had always opposed school choice, cited the continuously low achievement scores of African-Americans and Hispanics as the reason he has joined the choice movement. Sharpton eventually joined New York City Schools Chancellor Joel Klein in co-chairing the 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.

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 giving parents, educators, business leaders, and community members the flexibility collaboratively to create schools that offer innovative opportunities for students. As a result, South Carolina has been able to create a variety of charter schools.

Because some local school boards or district officials initially hindered these creative educational opportunities, we advocated for the creation of an alternative authorizer, the South Carolina Public Charter School District (SCPCSD), to offer prospective charter schools another sponsor. The SCPCSD, created in the spring of 2006, 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 2009-10 school year, there were two “brick-and-mortar” charter schools under the SCPCSD jurisdiction, and five virtual schools, serving approximately 5,800 students. Three more schools have been approved to open in the 2010-11 school year.

In order to continue SCPCSD’s work 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 2009-10, state funding for students in the SCPCSD is estimated at \$3,720 per student while that figure jumps to \$4,153 for traditional public school students. The total per-pupil funding for public schools is approximately \$11,242, including local funds, but charter schools do not benefit from local revenue sources. We must do more to equalize funding for students enrolled in the charter school district.

2. Offer Students Incentives to Succeed

For decades, South Carolina’s high school seniors have expected their last year of high school to be full of social interaction with few academic challenges. This holds particularly true for 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 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, taxpayers are still paying for the full per-pupil expenditure of \$11,242. 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, many students have not had math or science courses in over a year, which makes it difficult to draw upon these essential skills during their postsecondary studies.

Several states have found ways to address the senior-year inertia. 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 2008-09 school year, more than 6,783 students in Texas earned the Early High School Graduation Scholarship.

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 complete the required courses in a shorter period of time than the traditional four-year program. By extending student scholarships worth up to **\$2,000**, we provide students with 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, South Carolina schools received approximately \$11,242 per student – providing more than enough to fully fund 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 \$4.1 million. We hope the members of the General Assembly will consider legislation for this type of incentive.

3. Consolidate School Districts

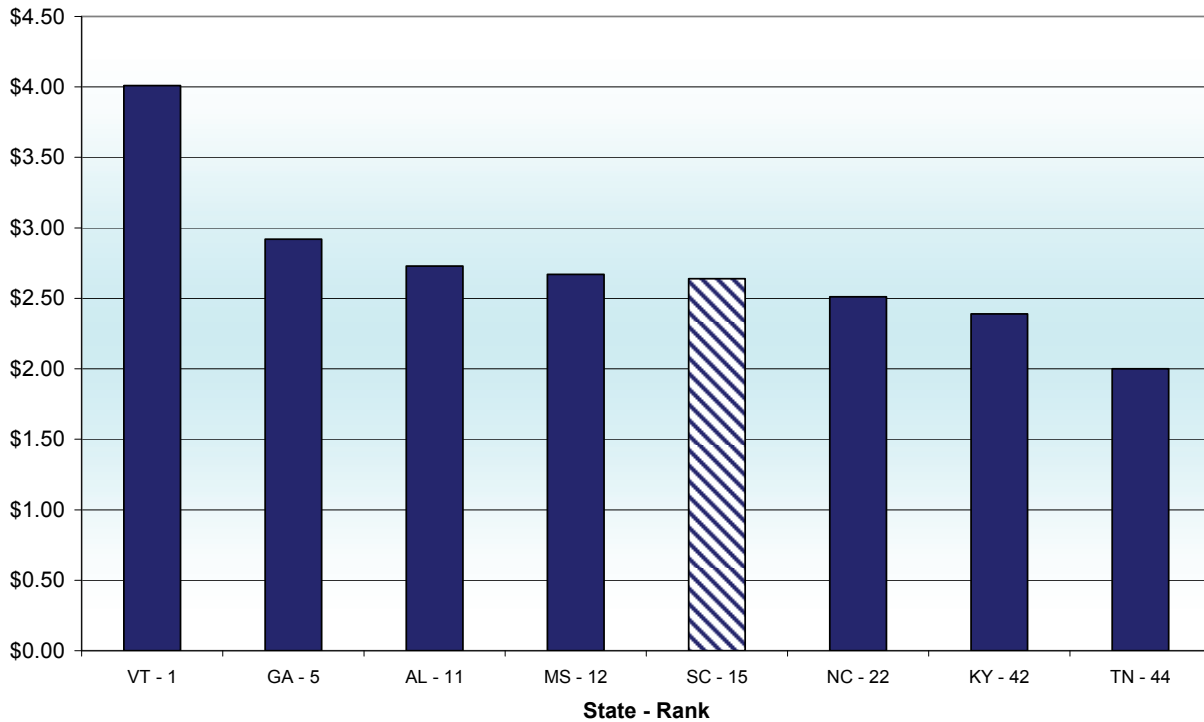
District consolidation is a concept that has been underway in South Carolina for some time, and this administration believes that continued consolidation will create an efficient and equitable education system. Since 1950, the number of school districts in South Carolina has declined from 1,220 to 85 school districts shared by 46 counties in 2009 – 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 approximately 70,000 students in Greenville County Schools down to fewer than 1,000 students in Dillon School District One.

The presence of a large number of independent school districts produces the same inefficiencies as having a large number of independent state agencies – specifically in the form of 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 have only 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 the smaller towns to feel that they were losing their identity, district officials estimate \$1 million in savings in the first year after consolidation by not operating the facilities of the smaller high schools.

Unnecessary expenditures on school administrative functions decrease the effectiveness of taxpayers’ investment in education. While we are optimistic that financial and economic realities will increase the number of districts that consolidate, in the mean time, individual districts must become more effective at reducing administrative costs.

Spending on K-12 School Administration per \$1000 of Personal Income



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 purchase 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 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 an exercise facility at a newly-planned school. The fitness center's 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 school districts, schools, municipalities, nonprofits, and privately owned businesses. The South Carolina Education Reform Council's report to the Governor supported this idea by recommended that South Carolina provide “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 optimum district size. 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 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 nearly 44,000 students and yet has one superintendent, as well as chief administrators for instruction, finance, and human resources. In Spartanburg County, which serves approximately the same number of students, there are seven districts—each with its own superintendent and administrative staff. Paying for seven separate school districts is an incredible

waste of money, particularly given our current economic situation. 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, 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. We basically agreed with the Task Force's proposals, 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 create innovative, 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 funding system that focuses on the student – not one that focuses on programs.

Last year, the state's Board of Economic Advisors estimated that we spend \$11,242 per pupil – yet, we have still seen no dramatic student achievement gains. Funding estimates are expected to increase to \$11,849 by FY 2010-11. Our focus should not necessarily be on *how much* we are spending on education, but rather on whether the activities we are funding produce positive results.

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.
- Ensure school funding arrives at the schools in the form of real dollars and not as staff positions or teaching ratios.
- Simplify the funding system, make it more transparent, and make it more accountable to taxpayers.

This administration supports a simplified funding stream for schools that is based on an updated Education Finance Act formula including factors for family income and student ability. Schools

should be given the flexibility to select and purchase the services they believe best meet students' needs.

Our proposal would not only allow greater spending flexibility for districts, but also greater transparency for the public. Our funding plan allows 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 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 academic improvement most. Moving to a more simplified funding system has been proven to address funding inequalities, reduce the perverse incentives created by programmatic funding, and force schools and districts to focus on students' needs rather than sustaining existing bureaucracies.

Our proposal will also fulfill our education budget's primary objective: focus more dollars directly to the classroom. In the last legislative session, the General Assembly temporarily gave school districts more flexibility to allocate funding as the school districts thought best. We are pleased to see that the General Assembly is giving local school districts more authority over how education funding is spent, but several programs are excluded from the flexibility proviso:

Programs Excluded from the Flexibility Proviso
♦ EEDA 8 th Grade Career Awareness
♦ EEDA Career Specialists
♦ Child Development Education Pilot Program
♦ School Employer Contributions
♦ 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. First introduced in 2003, SMART Funding legislation has yet to survive both legislative houses. 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. Offering competitive pay is one way to reward teachers for their dedicated service. This administration realizes the effect that teachers' salaries has on 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. Even though this year's budget cuts have allowed us only to maintain 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 reward teachers' success. Several urban areas have implemented pay-for-performance plans, and 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 \$37,551 salary in 2009)
Knowledge and Skills	Professional Development Units	\$751 (2 percent)
	Graduate Degree/National Certificate	\$3,380 (9 percent)
	Tuition Reimbursement	\$1,000 (3 percent)
Professional Evaluation	Probationary	\$376 (1 percent)
	Non-probationary	\$1,127 (3 percent)
Student Growth	Meeting Annual Objectives	\$376 (1 percent)
	Exceeding Student Performance Expectations	\$2,403 (3 percent)
	Distinguished Schools	\$751 (2 percent)
Market Incentives	Hard to Staff Position	\$2,403 (3 percent)
	Hard to Staff Schools	\$2,403 (3 percent)

The Denver ProComp system reflects current knowledge about merit-pay systems. First, teachers must not be forced to participate in the program. ProComp allows teachers to opt-into the program over a seven-year period or to continue with the traditional teacher salary schedule that bases salary increases on years of experience accompanied with inflationary adjustments. However, 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 measurement areas, increasing his or her 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 that has been modified to fit our state's needs. The TAP program builds on four elements that include merit-based compensation, multiple career paths for teachers, ongoing professional growth, and instructionally-focused accountability, and currently exists in 43 schools and 13 districts throughout South Carolina. 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. In fact, our TAP program is so successful that Minnesota Governor Tim Pawlenty based his state's teacher incentive program on South Carolina's 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. Even though the General Assembly limited this program's enrollment and funding

amounts during the last legislative session, 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.

Going forward, we recommend that the 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 student transportation continue to be one 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, and over 25 percent of our buses are more than 15 years old.

In 2006, the 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 Department of Education would gain by leasing a portion of its buses from a private provider rather than making outright purchases. 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. Given that the average life of a school bus is 15 years, we could send students to school in newer buses at a lower cost with a shorter replacement cycle by leasing.

We also recommend that the Department consider using buses that run on alternative fuels. The hybrid buses get almost double the miles per gallon compared to traditional diesel buses. Alternative fuels might present a more efficient and cost-effective means of transportation.

Conclusion

This administration's education proposal is simple: give students the tools they need to get the best possible education. Although we have made progress in some areas over the last few years, we still lag behind in many critical areas. As the number of progressive and innovative educational programs continues to increase around the country, we simply cannot afford to rely on our present system to improve our competitiveness. We believe our proposals will equip South Carolina's students to excel among students from other states, across the nation, and beyond.

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 all the challenges our state faces, we continue to succeed in attracting new business while allowing existing businesses to grow and compete in an increasingly global marketplace.

South Carolina is recognized consistently for its business climate by one of the nation's leaders in providing site selection and corporate relocation services. In 2009, the Pollina Corporation again named South Carolina among "America's Top Ten Pro-Business States." This study honored South Carolina for its progressive, pro-business policies that result in job growth. The state has been ranked among the top five states in the Pollina study each of the past six years. The continued efforts by this administration and our Department of Commerce to make South Carolina a better place to do business is at the root of this success, as the state continues to enjoy yet another year of record levels of capital investment and job creation for South Carolinians.

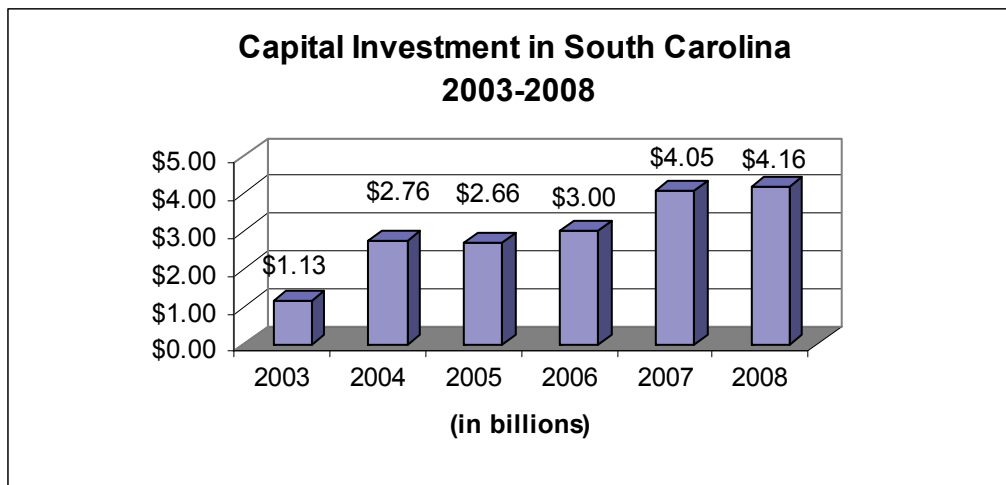
To have a clear understanding of where we are headed as a state, we must have an equally clear understanding of where we have been over the past several years. Since 2003, the Department of Commerce has been incredibly successful in attracting new businesses and industries to South Carolina and improving our business environment for the businesses and industries that already called South Carolina home. Over the last seven years, Commerce has completed 839 economic development projects, which created over 83,000 jobs and \$17.76 billion in new capital investment. Likewise, the Department of Parks, Recreation, and Tourism has partnered with private companies to provide taxpayers with hundreds of thousands of dollars in added value through better state park amenities and tourism promotions. PRT has also won several awards for tourism, stewardship, and conservation. Most notably, after re-opening the Charles Towne Landing Historic Site in 2006, PRT won the 2007 Southeast Tourism Society Travel Attraction of the Year award – all while increasing efficiency and saving money. We would like to highlight several of our executive agencies' outstanding accomplishments over the last several years:

- In 2009, Commerce's hard work garnered *Area Development Magazine's* "Silver Shovel Award" for recruiting a significant number of jobs and capital investment, and South Business Development Magazine recognized South Carolina as the #2 state in the Southeast for job recruitment in 2008.
- Commerce reduced the number of its divisions from 14 to nine, thereby eliminating unnecessary layers of management while enhancing efficiency and improving the agency's focus.

- PRT reorganized itself internally, reducing unnecessary personnel by 53 employees and becoming 78 percent self-sufficient by 2009 – resulting in a combined savings of \$14.35 million and ranking in the top 10 among self-sufficient systems in the nation.
- In 2003, Commerce established a Small Business Ombudsman, creating a single point of contact for entrepreneurs and small business owners. The Ombudsman’s Office has assisted more than 2,750 small businesses and provided more than 250 larger companies with services and resources.
- Commerce’s export development activities have secured new markets for products and services for more than 2,500 South Carolina companies. The state’s exports have increased more than 100 percent since 2002.
- Commerce began the Jobs for America’s Graduates program in 2005 based on a national model. This high school dropout prevention program trains high school students for employment within specific industries and has received multiple awards – most recently being named a “Top State Organization for Multi-Year Programs.”
- During our administration Commerce and PRT have worked to reduce costs and operate more efficiently, resulting in a total cost savings of \$62,928,135.

Capital Investment

South Carolina continues to experience rapid growth in capital investment and new jobs. South Carolina’s capital investment has grown from \$1.13 billion in 2003 to \$4.16 billion in 2008 – an increase of 250 percent. The Department of Commerce has also recruited more foreign companies from countries such as Germany, France, Switzerland, Canada, and Sweden. In fact, South Carolina is second in the nation in foreign direct investment, trailing only Hawaii.



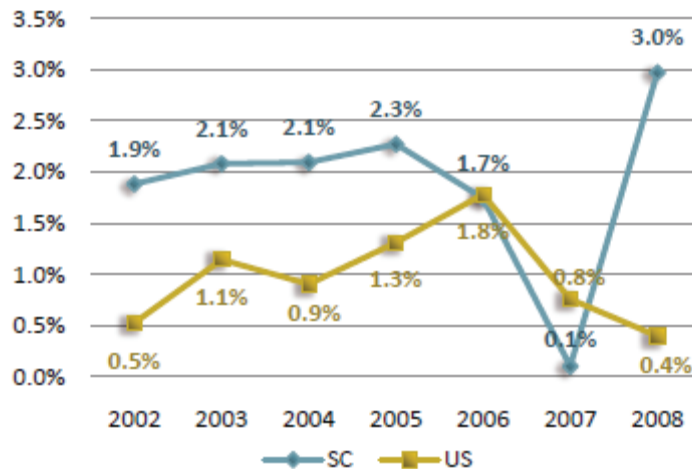
Boeing Company

We would be remiss not to comment on the state's monumental achievement in attracting Boeing and its 787 Dreamliner production line to South Carolina. Through the hard work of our administration, the Department of Commerce, and many state legislators, Boeing announced the largest development project in South Carolina's history – expected to produce a minimum of 3,800 new jobs and invest \$750 million in the North Charleston area. Boeing's investment adds to the already-thriving aeronautics industry in South Carolina, which has about 100 aviation-related companies employing over 16,000 South Carolinians. With this announcement, South Carolina seems well-placed to have another record year in 2010 and to maintain our national and international prominence as an ideal place to do business.

Employment in South Carolina

With the influx of people coming to South Carolina, our labor force continues to grow and impact our state's unemployment rate – which currently stands at 12.3 percent. According to the U.S. Bureau of Labor Statistics (BLS), since 2002 our labor force has grown by more than 267,000 people. Since January 2003, our state ranks 7th in labor force growth (10.49 percent) and 15th in employment growth (4.48 percent) among all states. By contrast, Massachusetts ranks 46th in labor force growth and 46th in employment growth over the same period of time, yet Massachusetts has only an 8.9 percent unemployment rate. As our labor force continues to grow, we must work even harder to spur economic development and job creation in South Carolina.

Labor Force Growth: SC Versus US, 2002 – 2008



Source: U.S. Bureau of Labor Statistics

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 works tirelessly to promote its strengths and existing framework for business while working to minimize or eliminate our weaknesses. Our state's access to markets, transportation and power infrastructure, available sites for development, nationally-recognized worker training programs, and strong technical college system are major points of interest for companies seeking to relocate or expand in South Carolina. Fortunately, South Carolina's weaknesses are identifiable and can be solved with the right approach. This administration firmly believes that we should make 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 of all sizes – 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 2008 *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 – into 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 for which we have advocated are devoted to equipping South Carolina to succeed in the 21st century and beyond. These changes include reducing taxes to stimulate the economy, reforming the judicial system to stop frivolous litigation, 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 carves out far too many incentives 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 it 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." Accordingly, we believe it is time to stop singling out counties or businesses and take a look at our tax code in a much broader perspective.

1. Film Incentives

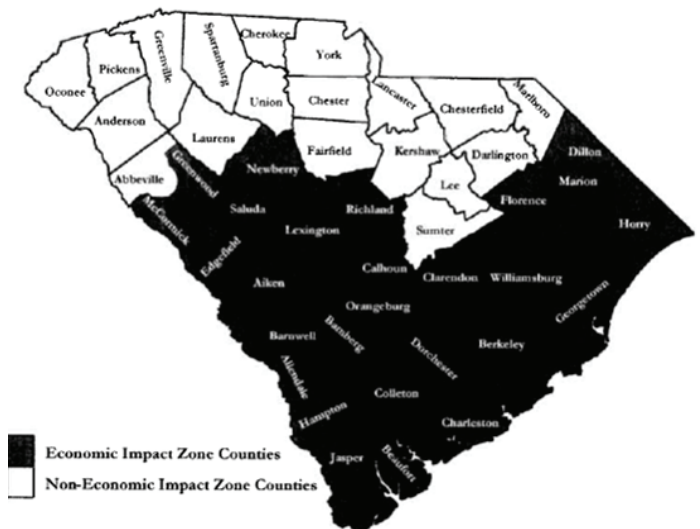
While we support the need for reasonable and effective film incentives, we continue to believe that South Carolina's current film incentives neither create permanent jobs for South Carolinians nor develop a sustainable, self-sufficient film production industry. Rather, in many cases film producers use the generous wage rebates offered under the current program to provide jobs to out-of-state film crews that only temporarily locate to South Carolina during filming. A study conducted by economist Frank Hefner of the College of Charleston confirms that our film incentives are not producing positive returns for the state. For instance, Hefner's study shows that the state's general fund loses 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 effectively create jobs and encourage economic development, as several other states are considering eliminating or modifying their film incentives. Moreover, we are pleased that the South Carolina Senate has joined in our efforts to improve the film incentive program by creating a study committee last year to review the program's effectiveness. We hope the General Assembly 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. Economic Impact Zone Incentives

The Economic Impact Zone incentives create the regionalization that fragments economic development efforts in South Carolina. As the map below demonstrates, half of the state does not receive any benefit from these incentives.

Because we believe it is time to stop the piecemeal approach to economic development, we support legislation that encourages business growth through eliminating the five percent corporate income tax as opposed to a litany of special tax incentives. According to our Department of Revenue, this proposal could be phased in by lowering the corporate income tax to 4.5 percent the first year and completely eliminating it over a nine year period.



A Simple, Low, and Flat Taxation Rate

During the 2005 legislative session, the General Assembly and this administration worked together to pass a measure that reduced the income tax rate paid by S-corporations, LLCs, and sole proprietors from 7 percent to 5 percent over a four-year period. It was important because it aided the almost 100,000 South Carolina small businesses that represent the backbone to job creation in this state, and when fully implemented this reduction will put nearly \$124 million each year back into the hands of small-business owners.

While this was a great step toward overall tax relief, this administration continues to believe it is time to offer the same tax relief to individual South Carolinians through a simpler and fairer overall tax system. Currently, South Carolinians are burdened by the second highest effective income tax rate in the Southeast. As a result, South Carolina is in danger of falling behind in the global competition for jobs and capital investment, and comprehensive tax reform is necessary to prevent falling behind. As the Taxation Realignment Committee (TRAC) reviews our state's tax code this year, we would propose a few ideas that we believe will spur our state's economic growth. These proposals would not only simplify the current tax code, but also attract economic and human capital to the state.

We would again raise the idea of raising our lowest in the nation cigarette tax, and offsetting it with a concurrent lowering of personal and corporate income taxes. Specifically we proposed raising the state's cigarette tax from \$.07 to \$.37, and eliminating some special incentives offered to a select group of big business—and instead replacing this with a phase out of corporate taxes which would uniformly be available to all big businesses. We offered this proposal last year:

1. An optional 3.7% income tax, which was offset by a \$.28 increase in the cigarette tax;
2. Fully indexing the tax brackets, which was offset by a \$.02 increase in the cigarette tax; and
3. A 10-year phase out of the corporate income tax, along with the elimination of most of the existing tax exemptions and credits.

Overall, our revenue-neutral plan reduced income taxes by \$135 million in the first year and increased the cigarette tax by \$.30.

Alternatively—and on a more comprehensive plane—we would endorse the idea of eliminating all sales tax exemptions not mandated by federal law or the South Carolina Constitution, and with this concurrently eliminate the three taxes below:

1. Eliminate the corporate income tax;
2. Create a flat, 2% personal income tax (lowered from 7%) while exempting the first \$10,000 of income (indexed for inflation); and
3. Lower the statewide sales tax from 6% to 4.5%.

Again this is possible if one were to eliminate the over-100 sales tax loopholes/exemptions and the sales tax holidays.

Because this idea hasn't been debated, we would highlight a few of the benefits of doing this sort of thing:

1. Eliminating the Corporate Income Tax:

Practically speaking, there is no such thing as a corporate tax—the corporate tax merely spreads the tax obligation among consumers, employees, and shareholders. The economic toll of the corporate tax is extremely high, especially during downturns like the one we are currently experiencing. For these reasons, we could eliminate the corporate income tax as one method to reinvigorate economic growth in South Carolina—producing an estimated \$167 million in tax relief.

2. Creating a Flat 2% Personal Income Tax:

Under current law, our state taxes everything except the first \$2,360 of annual earned income. Our high tax rates severely hamper economic growth by discouraging work and risk-based entrepreneurialism. In light of our high effective income taxes and the current economic difficulties our state is experiencing, we could create a flat tax of 2% on income earned after the first \$10,000 (indexed for inflation). Broad-based income tax cuts would allow capital to be used more efficiently than it would otherwise—benefiting all individuals.

In order to protect those at the lower end of the earning scale, exemption of initial earnings (up to some level) and indexing this income tax exemption for inflation would also be critical. Without indexing de facto tax increases or nominal income, increases come due to inflation. This “inflation tax” results in higher tax burdens on taxpayers, usually without their knowledge or consent. In light of the loose monetary and fiscal policies now being pursued, many prominent economists are rightly concerned about potential inflation. Should such fears of inflation materialize, not only will individuals see a decline in their savings, but more individuals, including the poorest among us, would be forced to pay more of their hard earned dollars to the state government. For example doing something along the lines of indexing the initial \$10,000 for inflation would help in preventing this encroachment.

Creating a flat 2% personal income tax would produce along the lines of \$1.6 billion in tax relief.

3. Lower the Sales Tax from 6% to 4.5%:

The Tax Foundation recently stated, “Broadening the tax base while lowering the sales tax rate will mitigate both volatility in revenue collections and the economic harm caused by a high tax rate. A high tax rate increases distortions in the market and can inhibit growth by making a state less attractive for individuals and businesses.” After eliminating the corporate income tax and reducing the personal income tax to 2% one could reduce the sales tax across the board, from 6 cents per dollar to 4.5 cents per dollar. Reducing the sales tax by 25% will produce \$633 million in tax relief.

The South Carolina Department of Revenue's most recent estimates show that the more than 100 sales tax loopholes totaled in excess of \$2.7 billion dollars for Fiscal Year 2009-2010. By narrowing the tax base and exempting politically-favored industries from sales taxes, tax loopholes force the state to fund government through higher tax rates on the cornerstones of sustainable economic growth—individuals' income and savings.

We applaud those in the General Assembly and the private sector looking at options to make our state more inviting to financial and human capital and are committed to engaging in this important upcoming debate. In this debate we believe a few things:

1. It is important that tax reform not become code for raising the aggregate tax load on South Carolinians.
2. We all recognize how we can achieve comprehensive, fair, growth- and job-friendly tax reform through multiple ways.
3. We focus on the final objective—freedom. It is the key to unleashing individual initiative and creativity key to any capitalistic system. Over time, and in every instance, places with greater economic freedom have consistently outperformed places of less economic freedom. Any tax reform therefore ought to focus on harnessing the free market's power while limiting political influence over how people and businesses spend and invest their money.

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. Former 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.” Current USDOT Secretary Ray LaHood has also indicated his support for these public-private partnerships. 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 into perspective, the agency’s total budget has grown 123 percent since 1995, while the total state budget has grown only 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. Indiana authorized the 75-year lease of the 157-mile Indiana Toll Road to private investors for \$3.85 billion in up-front cash. Meanwhile, Texas 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.

Florida is a terrific example of another alternative to traditional highway funding mechanism. In 2006, a reversible toll road opened in Tampa in an effort to reduce congestion to and from Tampa during rush hour traffic. Ultimately, the reversible toll road – which carries traffic towards Tampa during the morning commute and away from Tampa during the after-work rush hour – reduced the average commute time by one hour and costs each driver only \$3 per day. Additionally, the toll road was constructed as an elevated structure suspended over the existing highway, so the government did not have to acquire additional private land. Today, the toll road carries almost 16,000 vehicles per day to and from Tampa – all without a single tax dollar.

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 \$2.4 billion project, but so far only \$102 million has been allocated. 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.

Ultimately, finding alternative funding mechanisms for building and improving our roads and infrastructure would not only provide different means 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.

Workers' Compensation

Businesses have 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.

Three 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.

Key provisions of our reform law included abolishing the Second Injury Fund, strengthening the qualification requirements for people who testify as medical experts, and reversing a court decision that prohibited the employee's physician or health care provider from contacting the employer about the employee's injury.

Despite our progress, the Legislature has yet to adopt objective standards for workers' compensation awards. 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 method of awarding compensation 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.

Nonetheless, we are encouraged that reforms have had a positive 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. In addition to these cost-saving changes, we believe there are additional areas for improvement without our workers' compensation system.

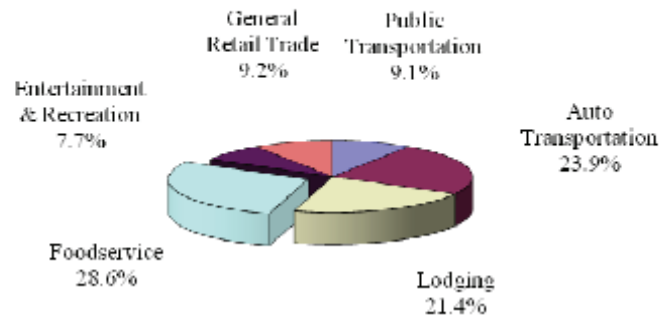
Tort Reform

A 2006 State Liability Systems Ranking Study prepared for the US Chamber of Commerce explored how US businesses perceived the fairness and reasonableness of each states tort system. Unfortunately, the study ranked South Carolina 42nd in the country and well-behind our Southeastern neighbors. The study noted that one major difference between South Carolina and other Southeastern states is that all of the Southeastern states that ranked ahead of us had enacted either punitive damages caps or appeal bond reforms. We are encouraged by the legislation introduced last session by Speaker Harrell and Senator Larry Martin which would create punitive damage caps, establish objective guidelines for damages awards, and reform our appeal bond laws. We hope to continue working with the legislature this session to improve South Carolina's legal climate.

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 \$17.2 billion tourism industry attracts tourists, and economy-boosting revenue, from all over the country. In fact, tourism generates employment for 12.6 percent of the entire workforce and is the leading industry in our state.

**Domestic Travel Expenditures in South Carolina
by Industry Sector - 2008**



Each year, more than 30 million people take trips in South Carolina, and tourism represents 10.9 percent of our total Gross State Product. Despite the recent economic downturn, last year's tourism-related gross sales increased by more than \$200 million in accommodations, food service, arts and entertainment, and auto rentals.

When deciding how best to allocate our tourism and marketing dollars, we must focus on activities that provide the greatest benefit to South Carolina's economy. Further development of effective marketing techniques is critical to attracting out-of-state visitors. PRT continues to improve in this area as seen in total visitor spending. Since 2003, domestic travel expenditures in South Carolina have grown by a total of 36.8 percent. Domestic travel expenditures totaled more than \$9.87 billion in 2008, up 1.7 percent from 2007.

Conclusion

Moving the state's economy forward by improving our underlying soil conditions for business is a significant priority for this administration. Maintaining a robust small business community, eliminating regulatory barriers for companies, and continuing to emphasize limited government spending and a low tax burden on our citizens will all provide South Carolina with greater opportunities for job creation and economic growth.

Meet the Health Care Challenge

Meet the Health Care Challenge

Congress is on the verge of enacting the largest unfunded mandate in American history. At a time when most states are struggling with rising unemployment, declining tax revenue and the worst national economic climate in 30 years, Congress is demonstrating that it is more out of touch than ever.

- **Former U.S. Speaker of the House, Newt Gingrich, and Texas Governor Rick Perry**

Health care reform – especially covering the uninsured – is being debated on the national, state and local levels. In 2007, two-thirds of governors introduced plans to cut the number of uninsured. Since states regulate health insurance for small businesses and individuals, and administer public programs (Medicaid, SCHIP), they are in a unique position to tackle the issue.

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.

Where We Are Succeeding

In the past year, we have had three major accomplishments regarding the State Health Plan that not only saves money, but also offers incentives to participants and encourages healthy behavior.

First, 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 2008, the Budget and Control Board approved a \$25 monthly discount for employees who do not use tobacco products. 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. A year later, the Board approved increasing this discount to \$40 single/ \$60 family to offset the estimated \$115/month in tobacco-related costs to the State Health Plan. The discount begins in January 2010, and with almost 425,000 participants, including employees and their family members, estimates show that around 75 percent of state workers will receive a discount. Individuals should have the right to use tobacco, but they should not expect others to pay for their poor health decisions.

Second, since almost 100,000 State Health Plan participants suffer from a chronic disease such as diabetes or cardiovascular disease (or both), we continue to believe that encouraging participation in a state employee wellness plan will help combat chronic disease and save money. In December 2009, the Budget and Control Board approved the State Employee Wellness Initiative. This plan offers educational activities that help address health concerns in a positive way. After completion of

a particular activity, the copayment for generic drugs will be waived for state plan participants. The Employee Insurance Program estimates the State Health Plan will save more than \$5.3 million a year with 25 percent participation.

Third, in July 2007, the Government Efficiency and Accountability Review (GEAR) Committee recommended changes to the State Health Plan's unlimited chiropractic benefit. In 2008, the State Health Plan spent more than \$25 million for this benefit. To combat excessive spending, in August 2009, the Budget and Control Board adopted a \$2,000 chiropractic limit per covered person per year. The State Health Plan expects to save \$6.98 million per year by capping services in the standard plan.

For us to have a clear understanding of where we are headed as a state, we must have an equally clear understanding of where we have been during the past several years. During our administration, our state has made significant headway in addressing the following health care costs and related concerns:

- Launching of "Healthy Connections Choices" gives Medicaid beneficiaries the option to choose among several market-based health plans that encourage healthy behaviors. By doing so, our state Medicaid growth is much lower than the rest of the country. South Carolina is averaging a five percent growth rate, whereas the national average is nine percent.
- Implementing a preferred drug list to save on Medicaid prescription costs and Medicaid fee-for-service co-payments.
- Reducing fraud and abuse in the Medicaid system. In FY 2009, the Department of Health and Human Services collected more than \$22 million from providers and beneficiaries through reviews for waste, fraud, and abuse, which is a 15 percent increase from the previous year.
- Supporting a life-saving organ donor registry which conserves an estimated \$24 million Medicaid dollars.
- Becoming the second state in the nation to offer Health Savings Accounts (HSAs) to state employees as part of the State Health Plan.
- Leading the fight starting in 2004 to restore adoption incentives from \$250 to \$1,500.
- Decreasing the time it takes to finalize adoptions. Currently, it takes 39 months to finalize the average child adoption process. This is a six month decrease since FY 2005-06 when it was 45.2 months. Additionally, 20.3 percent of foster children were adopted within 24 months. This remains well below the 32 percent national standard.
- Creating the Children in Foster Care and Adoption Services Task Force in 2007. The recommendations that have been implemented include creating a registry for birth fathers to help expedite the termination of parental rights process, streamlining the process for serving notice in adoption hearings; accelerating hearings for termination of parental rights; and more aggressively recruiting foster and adoptive parents.
- Reorganizing the Department of Alcohol and Other Drug Abuse Services (DAODAS) and allowing the resulting cost savings to be directed to the field

for direct services – to prevent or reduce the negative consequences of substance use and addictions.

- Preventing teens from gaining access to tobacco products to decrease health care costs. In 1995, children 12 to 17 years old were successful in purchasing tobacco from retail outlets almost 55 percent of the time. Ten years later, the purchase rate decreased to 11.2 percent.
- Enhancing core services that support the recovery of people with mental illnesses. The “Toward Local Care” (TLC) program at the Department of Mental Health (DMH) provides high quality community-based services that save \$34 million annually.
- Developing, through DMH and the Veterans Administration, a statewide referral system to provide timely information and assistance to soldiers and their families by participating in “The Returning Veterans and Their Families Strategic Planning Conference and Policy Academy.” Options include creating, through the private sector, recreation and athletic programs for soldiers, veterans, and their families and exploring ways to provide mental health services in rural areas.
- Pioneering the development of the nation's first statewide Telepsychiatry project helps to solve the difficulty in placing mental health patients waiting in emergency rooms. With a \$3.7 million grant from the Duke Endowment, South Carolina's DMH is the first to use this type of telemedicine statewide. Currently 15 hospitals are directly linked to DMH where psychiatrists are available 24 hours a day to conduct “face-to-face” consultations.

This past year we had additional accomplishments that will positively affect the health of our citizens, which in turn will help save taxpayers money. Accomplishments we are highlighting relate to the areas of health insurance, prevention, mental health, early detection and treatment, rehabilitation, nutrition, and fraud and abuse prevention.

Health Insurance Options

Medicaid is no longer a one-size-fits-all program. As we previously stated, by implementing “South Carolina Healthy Connections,” we 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 nine available options which include:

- Seven market-driven health plans that compete to serve Medicaid beneficiaries, which may provide extra benefits beyond traditional Medicaid. A key component of this reform is connecting beneficiaries to one primary care physician, or “medical home,” to better coordinate and improve care.
- Individualized services that encourage responsible use of Medicaid health dollars through 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 of their kind in the country. HOAs encourage prudent use of health care services and 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 these public and private efforts, the number of South Carolinians undergoing health screenings is increasing. We have succeeded on many levels during the past year:

- The Hollings Cancer Center's Mobile Health Unit traveled throughout 11 Lowcountry counties, providing almost 3,000 screenings to treat those living in medically underserved areas. In addition, the center continues to expand partnerships with employers and school districts.
- The "Healthy South Carolina Challenge" improves the health of our citizens, raises awareness of health issues, and encourages healthier decisions in day-to-day life. 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.
- DHEC continues to work with many partners by developing agreements with the 20 Federally Qualified Primary Care Centers to give free vaccines for underinsured children and youth. In February 2009, DHEC developed an 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.
- The number of women receiving breast and cervical screenings and cardiovascular risk assessment and follow-up increased from 9,000 to 16,000. 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. DMH reports that the number of persons waiting statewide in emergency rooms for mental health or substance abuse treatment has declined almost 10 percent when compared to the same timeframe last year (July 1 to September 30). DMH and DAODAS took the following steps:

- Sharing funding with and providing crisis intervention services at all 17 local mental health centers to those with co-occurring substance abuse and mental health disorders – both geared to prevent unnecessary emergency room admissions and assure more appropriate treatment needs are met. DMH has dedicated more than \$4.5 million dollars to alleviate this crisis.
- Contracting with private psychiatric or detoxification inpatient facilities to expedite movement from an ER setting to a more clinically appropriate one.

By doing so, patients are less likely to return to the ER for mental health or substance abuse treatment – especially if followed intensively as an outpatient once discharged from those private settings.

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 disabilities, the state has seen success in many areas.

- The Hollings Cancer Center obtained the prestigious National Cancer Institute (NCI) designation (spring 2009). Hollings is the only cancer center in South Carolina – and just one of 65 centers in the nation – to hold NCI designation.
- In October 2009, the Hollings Cancer Center also received accreditation from the National Accreditation Program for Breast Centers (NAPBC). This recognition, administered by the American College of Surgeons, is a three-year accreditation given only to centers that have voluntarily committed to providing the best in breast cancer diagnosis and treatment and complying with established standards.
- MUSC continues to participate in many clinical research trials. For example, MUSC is leading a national, multi-center clinical trial studying the effects of combining powerful drugs in patients with advanced hepatocellular carcinomas, or cancer originating in the liver.
- 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. 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 as more than 73 percent report no alcohol use following discharge from services (35 percent increase from 2008) and more than 76 percent report being employed following discharge from services (7.4 percent increase from 2008).
- 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 83 percent of the 30,000 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 for 2009 indicate rehabilitated clients will pay back \$3.33 for every vocational rehabilitation dollar spent. That results in the client repaying the cost of rehabilitation within 5.5 years – which is an 18 percent annual rate of return. In addition, we would like to recognize:

- Walgreens, with support from DDSN and the South Carolina Vocational Rehabilitation Department (SCVRD), has hired more than 200 workers with disabilities (40 percent of the facility's workforce). Walgreens, the nation's largest drugstore chain, became a showcase for the employment of people with disabilities when it opened last year its new distribution center in Anderson, South Carolina. Their goal is to have 1,000 employees with various disabilities employed by 2010 with starting salaries comparable to non-disabled coworkers.
- In 2009, SCVRD rehabilitated 8,510 people with disabilities into employment. Since 2005, the department has had the nation's second highest rate of persons rehabilitated (193 per 100,000 population).

Nutrition

Unhealthy eating and inactivity contribute to between 300,000 and 600,000 deaths each year, according to the U.S. Department of Health and Human Services – that's 13 times more people than are 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.

- The Senior Farmers 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 35 counties and provides benefits to approximately 24,000 low-income seniors.
- The "Elderly Simplified Application Project" simplifies the Food Stamp application process for our low-income elderly citizens. Since the inception of the federally approved project, the number of cases in South Carolina has more than doubled in four years from 11,134 (Sept. 2005) to 23,741 (June 2009).

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 Partnership which is working to create and promote communities that support healthy eating and active living. This partnership is an ongoing collaboration between state agencies, business and industry, health care organizations, schools, and community members.

AIDS Drugs and HIV Testing

While investment in treatment and research is helping people with HIV/AIDS live longer and more productive lives, the disease continues to spread at a staggering national rate of more than 40,000 new infections a year. In 2007, South Carolina ranked 8th in the nation (among all 50 states and the District of Columbia) for AIDS case rates. There were approximately 732 South Carolinians diagnosed with HIV/AIDS in 2008, bringing the total number of citizens living with HIV/AIDS to almost 14,000. The actual number living with HIV/AIDS in the state is unknown because many are unaware of their infection status. 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 the following steps toward this mission:

- Providing HIV testing in 2008 to more than 54,400 people, an increase of more than five percent compared with 2007, despite staff shortages in many settings.
- Expanding HIV testing to reach more African-Americans – 73 percent of men and 83 percent of women diagnosed in South Carolina are African-American. DHEC received a three-year grant from the Centers for Disease Control and Prevention that allows DHEC to create new partnerships with hospitals to initiate routine HIV testing in counties with the highest infection rates.

Fraud and Abuse Efforts

Through its Program Integrity division, DHHS has aggressively pursued Medicaid fraud and abuse and dramatically increased collections. The agency has:

- Increased the number of referrals this year to the Attorney General's Office by more than 60 percent, from 37 cases to 60.
- Instituted a pharmacy "lock-in" program for beneficiaries who show patterns of prescription drug-seeking and abuse. (Prescription drug abusers, sometimes referred to as "high flyers," often attempt to utilize multiple pharmacies and doctors to mask their habit.) The program ensures the individuals must get all prescriptions from one pharmacy. Several dozen beneficiaries have been identified through a data analysis that flagged unusual claims activity. Data analysis of the initial results shows an average savings per beneficiary of \$6,699 since January 1, 2009, through fewer filled prescriptions and hospital visits.

Opportunities for Improvement

While 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 more than 60,000 employees, state government is the largest employer 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. For example, many private companies offer smoking cessation programs with premium incentives because it makes good business sense. It is no secret that healthier workers are more productive workers.

With our support, the Budget and Control Board has included smoking cessation as part of the State Employee Insurance Plan since 2006. Interest continues to grow, 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 4,400 participants and has a 45 percent quit rate. Our hope is that more state employees will take advantage of this opportunity to beat their nicotine addiction.

As stated earlier, we believe state employees who do not use tobacco should not have to pay for the poor health choices of their coworkers – especially since the State Health Plan spends \$75 million per year on tobacco-related illnesses. Our administration pushed for the initiative to give state workers a discount if they do not use tobacco products. The discount begins in January 2010 and with almost 425,000 participants, including employees and their family members, estimates show that around 75 percent of state workers will receive a discount. Individuals should have the right to use tobacco, but they should not expect others to pay for their poor health decisions.

Adoption and Foster Care

We have long believed that one of the state’s primary roles is to protect and provide for vulnerable children. With that in mind, this administration has consistently called for improvements in the state’s adoption and foster care services. Over the past 10 years, more than 4,200 children were adopted in South Carolina, with more than 500 of those adoptions occurring just this past year. Still, about 1,600 children still seek an adoptive home in our state.

We hope to see the General Assembly evaluate the remaining Children in Foster Care and Adoption Services Task Force recommendations, including hiring more DSS and court personnel dedicated to reducing the termination of parental rights caseload. We believe this 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

In December 2009, the Small Business and Entrepreneurship Council recognized South Carolina as the first among all 50 states in terms of health care policies that lead to greater affordability of health coverage. However, our 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 \$402 (single coverage) that the Kaiser Family Foundation states is the 2009 average monthly premium cost. Many of the uninsured are healthy young adults who could benefit from this type of coverage because they 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 continues to support initiatives that increase transparency in government.

Beginning in 2008, DHHS has made detailed spending activity available online. The first phase of the initiative was to post administrative expenditures on the agency Web site. This searchable database lists all travel expenditures, expenditures for office supplies more than \$100, and contractual expenses more than \$100.

To expand upon government transparency, DHHS also launched the Medicaid Provider Transparency Tool, which is a searchable database compiled from more than 25 million claims paid to health care providers throughout the state each year. The site can be searched by name, provider type (physicians, dentists, nursing homes, hospitals, etc.), or by provider location. The Provider Transparency Tool lists the dollar amount individual providers received, the number of patients served, and the average paid per visit. Hospital data also includes Disproportionate Share payments. All enrolled Medicaid providers are included by name, unless they serve so few Medicaid patients that the inclusion of data could be used to identify individual patients. The site has proven to be popular. Since last summer, it has been visited almost 20,000 times. The upcoming inclusion of a second year’s worth of data likely will drive additional traffic to the site.

Since the vast majority of Medicaid’s \$4.4 billion in expenditures are claims, our administration strongly believes allowing the public the opportunity to see where the money is being spent is important. We share these ideas to encourage all state agencies to increase, via the internet, this type of government transparency.

Health and Human Services Agency Restructuring

The Legislative Audit Council recommended in 2003, and we continue to agree, 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. Since 2000, none of the LAC’s restructuring recommendations have 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.

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, and this administration strongly supports the restructuring efforts supported by several legislative members during the last few years. We look forward to working with both the House and Senate in 2010 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

Providing for public education is one of the most important functions of any state government. The quality of a state's educational system will partly determine a state's level of economic development, health care, public safety, and overall quality of life. With increasing economic globalization, 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, especially when our state and nation face unprecedented economic difficulties. During lean budget years, we believe it is important to continue to put the maximum amount of resources into the classroom – not on administrative programs. It is critical that we eliminate duplicative, non-performing programs and instead use our money to raise scores on state and national assessments, close the achievement gap between racial and socioeconomic groups, and produce more graduates ready for college or the workforce.

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

- ✓ 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.

Last year, State Education Superintendent Jim Rex and the Education Oversight Committee 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 significant budget reductions have prompted us to recommend a similar salary freeze for FY 2010-11.

Operating our education system on limited resources does not mean that educational quality should suffer. Rather, it presents an opportunity to find creative ways to teach our students. Every child is unique, and we believe that parents can best determine what most benefits their children. Ultimately, we want to restore parental control over education by introducing market-based principles of educational choice, improving public school performance, and expanding educational opportunities for low and middle-income families.

Developing Our Purchasing Priorities

Our goal since the beginning of this administration has been to see every child excel academically from the first day in kindergarten to the day of high school graduation. To that end, we examined the major indicators of success to determine whether our state is reaching its goal. We have found

that South Carolina is making some progress, but the many opportunities for improvement have determined this year's purchasing priorities.

Where We Are Succeeding

We have made some progress in K-12 education, especially during this past school year. The new Palmetto Assessment of State Standards (PASS) test gives teachers more detailed information on students' academic progress earlier in the school year – allowing teachers to tailor their lesson plans to students' needs. We expect that the Department of Education will publicly release the first year's PASS scores in January 2010.

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. Additionally, we are increasing student participation and scores on the Advanced Placement exams. Incredibly, a Mauldin High School senior and a Riverside High School senior – both in Greenville County – had perfect scores on this year's SAT. According to the College Board, only 300 of about 1.5 million high school seniors that took the SAT nationally in recent years had perfect scores.

On a national level, we are delighted that twenty two of our schools earned recognition through *U.S. News and World Report* rankings as "America's Best High Schools 2010." 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 twelfth 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 dropout 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 four 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 expanded to a total of 14 Star Academies in 12 South Carolina districts.

Jobs for South Carolina's Graduates is another successful dropout prevention model. Our office has supported JAG-SC – which was adopted from the national model called "Jobs for America's Graduates" – since its inception in 2005. Begun under the State Workforce Investment Board at the state Department of Commerce, 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 scores 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. That same year, the program served approximately 800 participants and saw a 92.33 percent graduation rate – well above the national JAG standard

Opportunities for Improvement

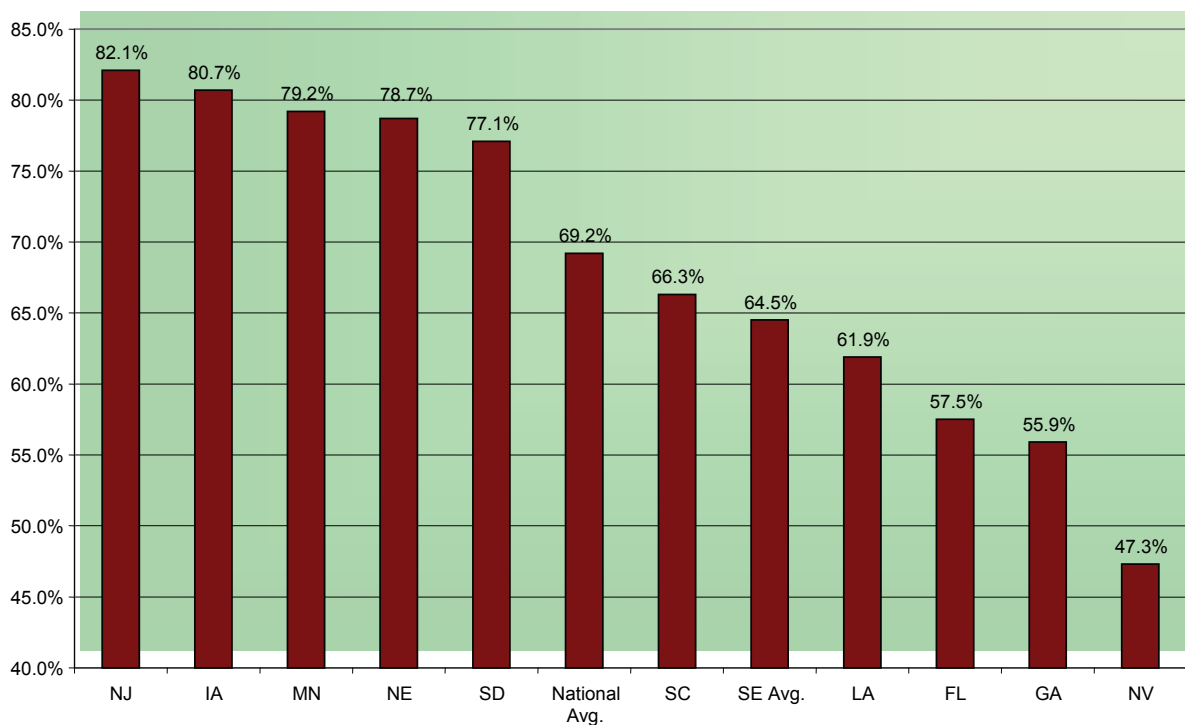
Although we have made some progress in educational performance due to the outstanding efforts of teachers, students, and parents, we cannot ignore the statistics that indicate we have much farther to go to close the gap that exists between South Carolina and the rest of the nation. To help every child succeed academically, we have established five goals – the first and most important is to increase the number of students that graduate from high school.

1. Increase the high school completion rate.

Research reports uniformly indicate that South Carolina's high school completion rate is entirely too low. It is unreasonable to expect our state to move in a positive direction when only 60 percent of South Carolina's students graduate high school in four years. Our goal is to increase significantly the percentage of entering high school freshmen who complete the 24 credits required for high school graduation in eight semesters or less.

According to the 2009 version of Diplomas Count, a study performed for the Bill and Melinda Gates Foundation, 66.3 percent of South Carolina's students enrolled in 9th grade in 2005-06 graduated high school four years later – putting us 37th nationally. The same study found that approximately 1-in-3 students – or 122 pupils each day – dropped out, were held back, or failed to complete the full diploma requirements. Additionally, the National Governors Association published a study in 2009 that revealed that 98 high schools in South Carolina graduated less than 60 percent of students within four years.

National High School Completion Rate



Source: *Diplomas Count, 2009 Study*

In this year's executive budget, we outline several major goals and invest in activities that increase the likelihood that students 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 quality 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. We must strive not only to get our students through high school, but also to prepare our students for college or the workplace.

To increase student participation and success in high-quality courses, our budget funds activities that challenges students who are proficient, helps students who have fallen behind in core classes, and ensures that our youngest learners have a strong foundation. To measure South Carolina's progress, 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 quality 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.

Since 2005, South Carolina's average test scores for graduating seniors on the SAT and ACT have decreased slightly – while most other states are improving. 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. With the goal's deadline now upon us, we have made little progress toward meeting this goal.

We will continue to measure our progress towards academic excellence 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. On the 2009 SAT, there was a 100-point difference between reading and math scores – and a 96-point difference between the writing scores – of African-American and Caucasian students in South Carolina. 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. Our current challenge is to understand these gaps, and ultimately to raise lower-achieving students' performance level.

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

Reaching our educational goals is directly tied to maximizing the percentage of the educational dollar spent directly in the classroom, but our current fiscal conditions require us to operate with significantly limited resources. We believe our state can make progress by eliminating expenditures on services that are not linked to specific goals, reducing or eliminating expenditures associated with activities that have poor outcomes, minimizing duplicative services, and improving productivity. Last year, one recent example of poorly prioritized spending was found in Richland School District One, which spent more than \$400 million on a 17-school building program. Within this project, \$64 million was spent on "architecture, engineering and professional services," according to the Columbia Business Report. In light of the economic events since that time, focusing our money on capital projects is an obviously unwise decision.

Reducing administrative overhead is another way that money could be reallocated to the classroom. According to the Census Bureau's most recent data, the amount South Carolina spends on school administration relative to personal income ranks 15th nationally and 5th among Southeastern states, ahead of North Carolina, Florida, Virginia, Louisiana, Kentucky, and Tennessee. Since we have cut \$1.8 billion from the state budget since the summer of 2008 and reduced the base student funding from \$2,578 in FY 2008-09 to \$1,912 last year, we must be more careful about how we spend educational funds.

Our purchase plan maintains many educational services but redirects some existing funding to activities that directly impact students and teachers in the classroom. Overall, we recommend dedicating \$1.93 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 EOC to maintain teacher salaries at the current average of \$47,421.

Because of the tough fiscal year that our state faces, the General Assembly cut millions of dollars from our K-12 education system – ultimately eroding the Base Student Cost. We recommend fully funding the Base Student Cost of \$2,044, but we want to point out that the Base Student Cost does not reflect the total per-pupil funding amount. Although the Base Student Cost is sometimes used as the ultimate measurement of education funding, South Carolina's average per-pupil funding is \$11,849 in FY 2010-11 counting federal and local funds.

Purchasing Priorities

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

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

If children are not adequately prepared to learn while they are young, then it becomes increasingly difficult for them to meet academic challenges as they progress through the school system. Making sure that all children are well-prepared for formal schooling requires that any 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.

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. Education is not simply an end unto itself, but a means to our ultimate goal of cultivating a productive workforce. We want our educational system to challenge 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.

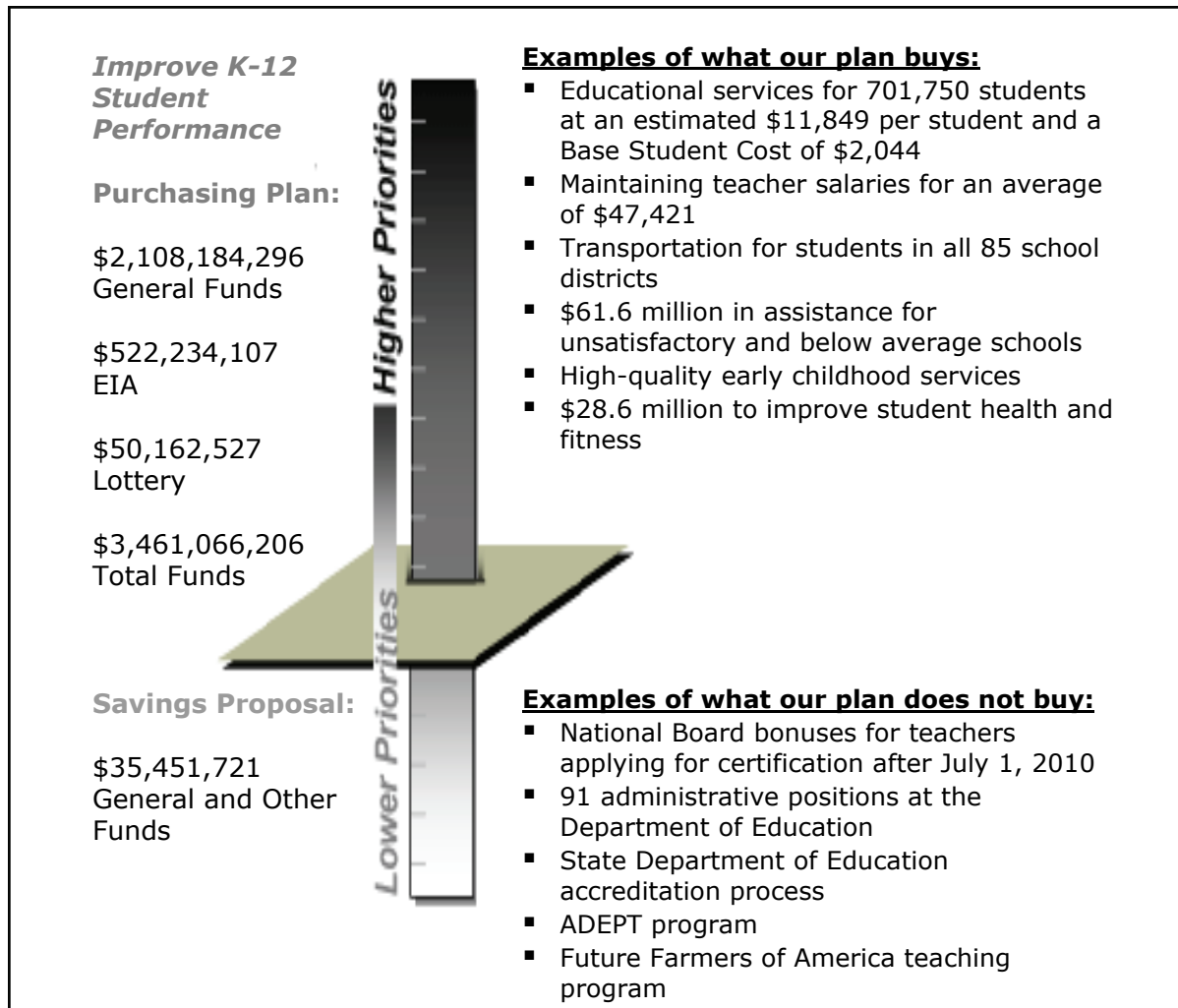
Before the school system can provide students with the skill sets they need, their minds have already been shaped by various societal forces. Since there are so many factors that influence how, when, and whether a child learns, it stands to reason that an effective school system will offer a multitude of learning environments to find the right fit for the students.

4. Provide public, accessible, 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 their children's district or school compares to others. In the spring of 2008, our state made significant revisions to the accountability system. The state's standardized test, PACT, was replaced with a new exam for students in third through eighth grades called the PASS, or Palmetto Assessment of State Standards, test. With this exam, teachers and parents receive student performance data more quickly than they received the PACT data, and thus can target how best to help a student earlier in the school year. Given that many groups have expressed concerns about whether the new scoring system and performance ratings system will improve curriculum development or student achievement, we eagerly await the release of the PASS test results early in 2010. Although we recognize state teachers' desire for better diagnostic data in a more timely fashion, we suspect the new testing scheme will do much 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 K-12 performance. In many cases, we have used cost savings methods simply to *maintain* current funding levels for high priority services. By contrast, we do not purchase services that are relatively low priorities. 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 over 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 \$2,044 per weighted pupil unit distributed through the Base Student Cost formula, we are granting local school districts complete funding flexibility to provide educational services to kindergarten through 12th grade students. We believe that this flexibility should be used to prioritize funds primarily to the classroom – specifically for teacher salaries. Granting school districts maximum flexibility will allow us to **maintain teacher salaries for the FY 2010-11 year** and 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 with grants that can offset the cost of 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 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 the South Carolina Public Charter School District, which offers parents more educational options for their children. Paying for 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 \$3,344,115 in total funds** to continue services offered through the statewide charter schools district.

Funding the Student Health and Fitness Act of 2005 to address the growing obesity rate among the youth of our state. The Student Health and Fitness Act is an effort to combat the growing health problems that are emerging as a result of our students’ declining health. Starting at an early age, increasing citizen-awareness about health choices can lead to healthier lives. We propose **maintaining funds of \$28,665,985** for its continued implementation.

Addressing childhood obesity through the FitnessGram assessment. Dr. Kenneth Cooper, of the Cooper Clinic in Texas, developed a health program called the FitnessGram that tests children’s strength, endurance, and agility. In 2007, Texas Governor Rick Perry signed into law new requirements for public school physical fitness classes and also mandates each school to test its students annually using the FitnessGram. One year after Texas implemented the program, preliminary surveys found that Texas’s 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 would greatly benefit by using the FitnessGram 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 childhood obesity problems. In 2008, this administration and Superintendent Jim Rex of the Department of Education formed a partnership to promote FitnessGram as a part of South Carolina’s overall student fitness plan. 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 of the 2009-10 school year, every public school in South Carolina that provided a physical education program to children in 4th grade or older used the FitnessGram program to

measure students' physical fitness. We fully support this initiative because of the impact that healthy living has on academic performance.

Funding the Education and Economic Development Act (EEDA) to restructure elementary and secondary school curricula to be 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 \$30,593,494** for this program's fifth year of implementation.

Supporting the South Carolina Virtual School programs 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 would otherwise be limited to students in schools with large enrollment levels. At the same time, this program provides the opportunity for poorly-performing students to receive remedial education that the students' assigned schools are unable to provide. Although we recommend freezing vacant positions for this program because of budget shortfalls, **we support \$2,462,298 in funding for the South Carolina Virtual School program.**

Providing transportation to and from school for more than 700,000 students. We understand the need to support the state's 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 \$108,099,566.** In addition to fully funding our public school transportation system, our **purchase plan provides more than \$55,401,104 in general funds for school buses and \$41,462,985 in local maintenance staff salaries.** Even though we are recommending these expenditures, 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 rather than purchasing more school buses. So far, the TransPar Group's recommendations have gone largely ignored. During these tight budget times, we once again propose that the Department of Education issue a request for proposals for lease agreements that could be used to accelerate the rate at which we replace our older buses. The leasing option will provide safer transportation to our children at a lower cost to the taxpayer.

Assistance and accountability for underperforming schools. The 2008 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 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 16 percent of students in South Carolina are enrolled in 185 schools with a rating of "Unsatisfactory," while nearly 24 percent of students are enrolled in the 298 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 turnover rates that cripple the schools' efforts to improve. In order to help these schools overcome the obstacles that have limited their success, we concur with the EOC's recommendation of reducing technical assistance funding by \$32 million, which leaves **\$61,690,956 million to fund this item.**

High-quality pre-school programs that provide direct services for almost 25,000 pre-kindergarten children throughout the state. The First Steps program works with public and private institutions to improve family literacy rates, employment rates, and the quality of childcare to better prepare young students for kindergarten. We believe that by coordinating 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 \$16.6 million** to support its efforts. Additionally, we will continue to support the Childhood Education Development Pilot Program, and we recommend funding **\$17.3 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, 2010. We accept the EOC's recommendation to discontinue these salary bonuses because 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 2010-11 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. As of December 2009, there were 798 more teachers who earned the certification, which obligates our state to \$59.8 million over the next 10 years to support bonuses just for these new entrants. Discontinuing the bonus will result in a **cost savings of \$2,750,000 this year alone. Additionally, 244 certified teachers are scheduled to end their ten year certification on June 30, 2010. Discontinuing any further incentive payments to these teachers saves \$2,205,760.**

Eliminating funding for assessments, evaluation, and review of the High Schools that Work model and Making Middle Grades Work model through the EEDA. Last year, Department of Education officials recommended suspending any assessments that were not required by federal regulations. The assessments required by High Schools that Work and Making Middle Grades Work fell in this category. Additionally, the budget cuts this year have forced us to reevaluate the sheer number of programs aimed at raising high school achievement and graduation rates. Because the budget cuts this year have been so dramatic, and because the Department has undertaken new achievement and assessment programs like the Core Standards initiative, we recommend eliminating funding for High Schools that Work and Making Middle Grades Work this fiscal year. Our proposal results in a **cost savings of \$1,756,516.**

Making Tough Choices:

The current economic challenges have forced many South Carolinians to make some serious decisions about how they will spend their personal income. Similar to the challenges facing households across South Carolina, the state's limited resources require that we make difficult choices about how we will direct our spending during FY 2010-11. These choices reflect our desire to be fiscally responsible with taxpayer dollars by limiting government spending to high-priority activities. The following items represent some of the difficult choices we have made on educational activities that we chose not to purchase in this year's executive budget.

Reducing administrative costs at the Department of Education. In spite of our emphasis on maximizing the percentage of education funding that reaches the classroom, the Department of Education has chosen to limit the difficult cuts that should be made in Columbia, and instead has slashed classroom funding. While we understand that eliminating jobs at the Department of Education is a difficult decision to make, we believe that unnecessary staff positions at DOE should be cut to allow more dollars to flow into the classroom – particularly when the average compensation for SDE administrators is over \$70,000. Reducing administrative staff by 91 positions – 15 percent of the current staff – will produce cost savings of **\$6,549,797**. We believe this money should be **redirected to the Base Student Cost**. In tough fiscal times, we must 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 funds for Agricultural Education Teachers. This funding is a pass through that goes from Clemson University to the K-12 school districts and supports Future Farmers of America teaching positions. While the agricultural science lessons learned through the FFA courses are valuable, they are elective courses that reach only five percent of high school students. According to the South Carolina Department of Education, 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 is unfair to continue to support this special funding. Although agricultural education courses have merit, we should focus primarily on funding teaching positions that will aid our students in earning a high school diploma. This will result in a **cost savings of \$304,199**.

Eliminating the ADEPT program. The Assisting, Developing, and Evaluating Professional Teaching (ADEPT) program, which is similar to the National Board Certification process, has the potential to improve teacher development throughout South Carolina. However, it is duplicative of – and less effective than – other development programs that the state currently offers. For instance, the Teacher Advancement Program and the South Carolina Teacher Incentive Grant program each offer valuable teacher development services and are directly tied to academic gains in student performance. Because other, more successful programs exist, there is no need for our state to fund the ADEPT program. This will result in a **cost savings of \$1,881,035**.

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; encourage economic growth; and, primarily, create jobs. The challenge is to achieve these goals with dwindling resources, as significant budget shortfalls resulted in cuts to higher education budgets by more than roughly \$200 million since 2008. We want to give more South Carolinians access to our higher education system – and ultimately improve that system – so they can excel in an increasingly competitive job market.

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. We also 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 coordinated statewide plan. By coordinating our higher education efforts, we can eliminate duplication and allow the institutions to have distinct missions, together serving the educational needs of our citizens.

Our mission for higher education is simple: to provide a high quality education at an affordable price for our citizens. 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 want to maximize private and non-profit interaction to enhance our many wonderful community arts and cultural programs.

Developing Our Purchasing Priorities

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.

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

- ✓ Improve the access and affordability of our Higher Education system.
- ✓ Encourage increased employment and quality of life opportunities for graduates.
- ✓ Create an efficient and effective statewide higher education system by establishing a Board of Regents.
- ✓ Provide a greater number of cultural opportunities in South Carolina.

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:

- Clemson University was again recognized as one of the top public universities in the country.
- The University of South Carolina's Moore School of Business was ranked as a top business school, while the undergraduate international business program has been ranked in the top two of all institutions for 20 consecutive years.
- The University of South Carolina-Upstate is in its third 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.
- The Citadel was ranked by *U.S. News and World Report* as the #1 best value and #2 public college overall in the South for masters'-granting institutions, while the University of Charleston and Winthrop University were both ranked in the top 10.
- The success of readySC, a division of the Technical College System, in training existing high tech aerospace employees was critical in attracting Boeing to South Carolina.
- Over 1,000 Citadel graduates are serving or have served the United States in Iraq or Afghanistan.

Additionally, enrollment in South Carolina's higher education system is increasing. In our public institutions, there are 33,757 more students enrolled now than in 1999 – a 22 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 more than 24 percent increase in the total number of degrees awarded by our colleges, universities, and technical colleges. Additionally, minority enrollment went up by more than 35 percent between 1999 and 2008 and by five percent between 2007 and 2008. Our technical college system saw a six percent increase in enrollment between 2007 and 2008, but the cause may be two-fold. First, more South Carolinians are realizing the value of obtaining a postsecondary degree to increase employability. Second, technical college enrollment has historically increased during economic downturns. The latter reason likely explains the enrollment increase, according to officials at the State Technical and Comprehensive Education Board, which means we must make higher education more accessible, affordable, and effective for our citizens.

Opportunities for Improvement

To achieve our goals of preparing our workforce for the global economy, 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 with various levels of education. If our state is going to be more competitive, then 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, but, unfortunately, rising tuition costs are making postsecondary education less accessible for many people in our state.

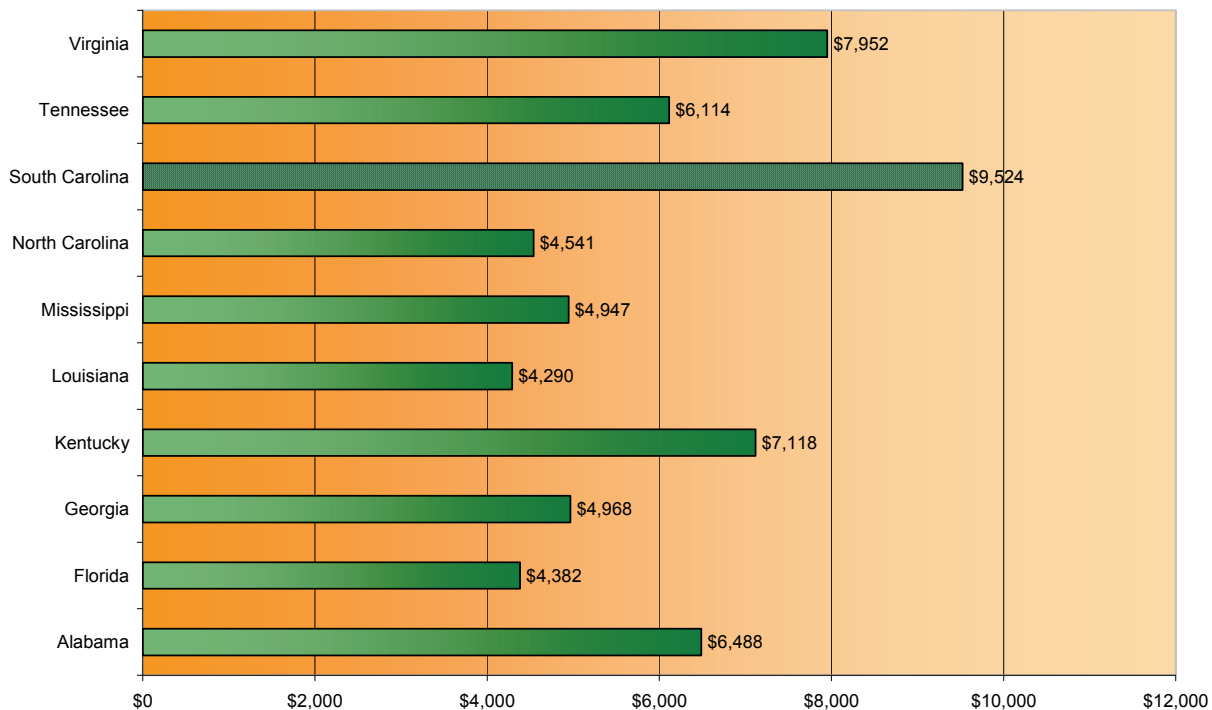
Rising Costs of Higher Education

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.

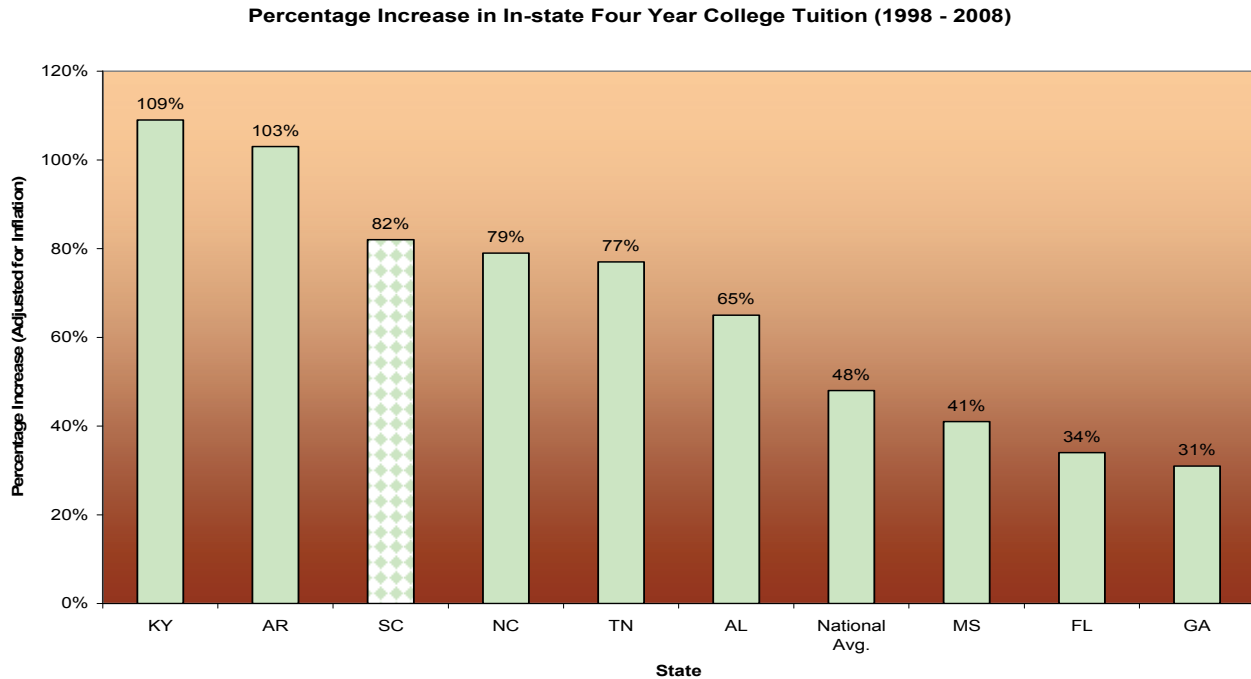
Offering first-class educational programs is useless if our citizens cannot afford to attend. Nearly double-digit percentage hikes in tuition in recent years are putting higher education out of reach for many in our state. According to The College Board, the 2009-2010 national average for in-state tuition and fees at public four-year institutions is \$7,020, marking a 6.5 percent increase from the 2008-09 fiscal year. In South Carolina's public four-year colleges, in-state tuition grew by 4.3 percent between 2008-09 and 2009-10 and averages \$9,524, which is \$3,722 higher than the Southeastern average.

Average Public College (4-Year) Tuition and Fees in the Southeast

Source: The College Board, *Trends in College Pricing 2009*

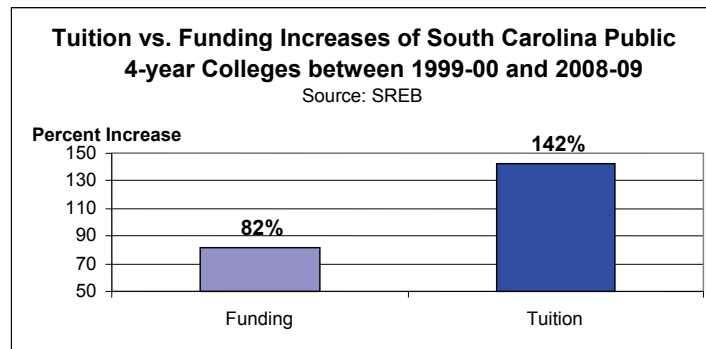


As illustrated by the chart below, tuition at four year colleges in South Carolina increased at almost double the rate of tuition nationally over a ten year period.



Source: *Southern Regional Education Board*

Despite the fact that tuition has increased by 143 percent over the past ten years, total funding (including state, local, and supplemental) has increased for our state's four-year public colleges by 82 percent.



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) in an effort to make sure tuition increases do not outpace the actual cost increase.

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 an advanced 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. This report is published every two years, and in three consecutive reports, South Carolina has received the lowest possible grade for college affordability. Even after receiving aid, poor and working-class families devote 34 percent of their annual family incomes 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 four-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 10.9 percent of the general fund 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 (CHE) 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, our inefficient system of underutilized campuses has made higher education *less* accessible. At a time when all state agencies weathered harsh budget cuts – and economists project a grim economic outlook for the next year – it is critical that 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:

1. Provide for an efficient and effective statewide higher education system by creating a Board of Regents.

Our current higher education structure includes 17 public universities and 16 technical colleges, each with an independent mission and focus, and each controlled by its own governing board of trustees. Although each campus is unique and desires to maintain its own identity, the absence of a unified plan for higher education has promoted a lack of focus within and between our institutions. During the past few years, we have seen a few examples of our need for a unified statewide educational plan:

- USC-Sumter circumvented the Commission on Higher Education 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 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 because the Commission's approval was either unwanted or unnecessary. These structural weaknesses and lack of planning will continue to contribute to rising costs and duplication in the higher education system, so we propose once again that South Carolina establish a Board of Regents as part of a statewide plan for higher education in South Carolina.

Tennessee, Kansas, and Louisiana each have a Board of Regents. Georgia's university system was unified under a single governing and management authority in 1931 (the Board of Regents), 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.

2. 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; therefore, 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 2010 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.

3. Increase the employability of graduates.

Earning a degree is a measure of achievement and an indication of practical ability. 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 as they prepare to become productive citizens. Also, we need to work hard to make sure students are aware of the employment opportunities available in South Carolina, in addition to being aware of the majors our universities offer. 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 gives technical college students on-the-job training with the prospect of a job offer upon graduation. The program is in its third year of operation, and the number of apprenticeships has increased from 777 in July 2007 to the current level of 1637 – an increase of 111 percent. This program is helping to create a larger pool of qualified workers in the areas of health care, tourism, and advanced manufacturing. 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.

4. Increase the effectiveness and efficiency of cultural opportunities and agencies through consolidation of duplicative services.

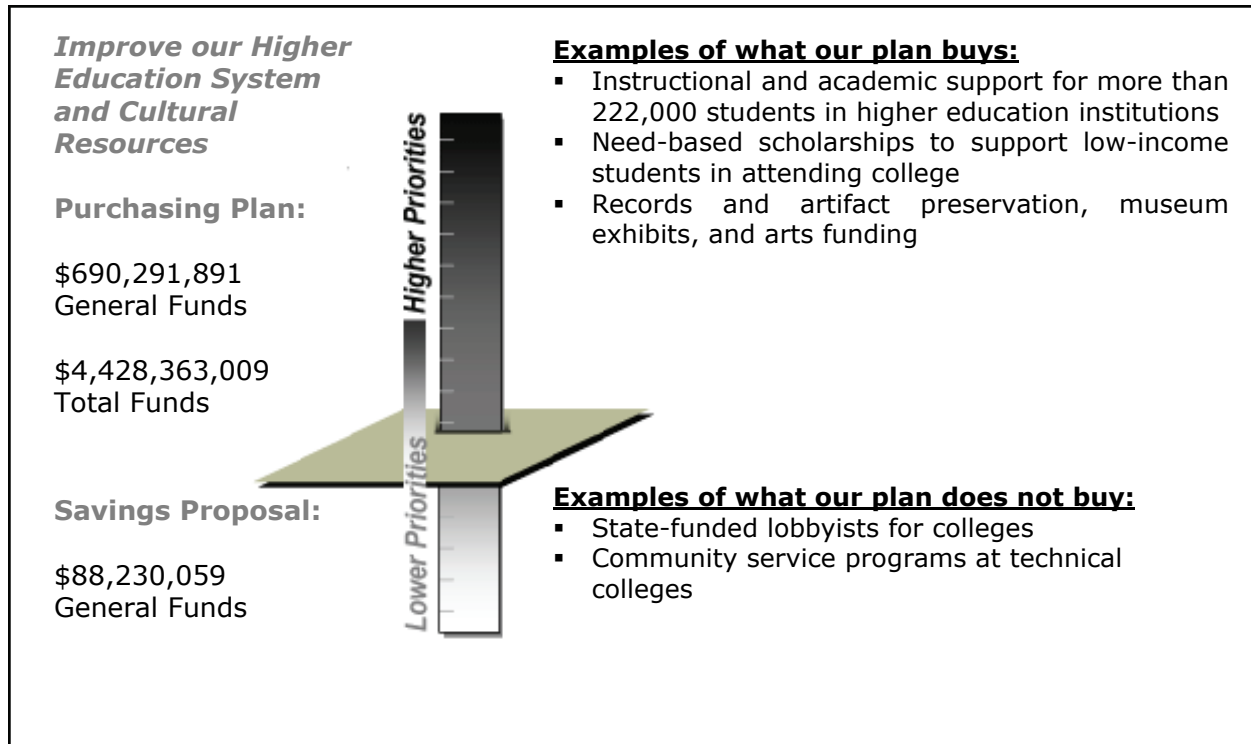
This administration continues to believe that duplicating government services is a misuse of taxpayer money. Our cultural agencies can combine efforts and save taxpayer dollars by sharing building space and streamlining administration functions. The State Library, Arts Commission, State Museum, and Department of Archives and History have discussed sharing human resource functions, and we would like to see this discussion turn into action.

5. 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, potential 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 higher education and promoting our cultural resources. 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, although valuable, have been identified as lower priorities. 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 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 **\$439,189,195** in **recurring general funds**.

Program coordination and oversight by the Commission on Higher Education. The CHE, while limited in authority, reviews academic and scholarship programs, collects relevant educational

data, and coordinates school facility usage. Until the CHE is given more authority, or until a Board of Regents is established, we propose **recurring general funding** in the amount of **\$30,849,071**.

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. 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."

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 unprepared 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 2009 will retain it in the fall of 2010. 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 **\$12,287,922**
- **LIFE Scholarships** for total funding of **\$158,133,731**
- **HOPE Scholarships** for total funding of **\$7,219,398**
- **Palmetto Fellows Scholarships** for total funding of **\$41,084,688**

Tuition grants for students attending private colleges in South Carolina. This investment is returned many times over by using the capacity of private 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 300,000 South Carolina students, totaling more \$620 million. We propose **funding in the amount of \$21,741,037 in recurring general funds and \$35,618,073 in total funds.**

The Lottery Tuition Assistance Program for students at two-year technical colleges. Each student is awarded a scholarship based upon the number of eligible recipients, and the amount of available funding each year is limited to the cost of tuition. 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. Since the start of the economic downturn, the technical colleges have had to absorb their share of our state's \$1.8 billion budget cuts. One way for the technical colleges to save money going forward 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 – because they have the largest enrollments – with the merger and proposed cost savings as follows:

Upstate-Region (Greenville)	Midlands-Region (Midlands)	Low-Country-Region (Trident)
Piedmont: \$993,561	Aiken: \$1,049,995	Horry-Georgetown: \$1,753,378
Spartanburg: \$983,375	Orangeburg-Calhoun: \$1,034,237	Williamsburg: \$289,967
York: \$1,251,293	Denmark: \$592,355	Florence-Darlington: \$2,998,466
Tri-County: \$2,010,356	Central Carolina: \$993,963	Technical College of the Lowcountry: \$1,166,958
Northeastern: \$707,690		

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.

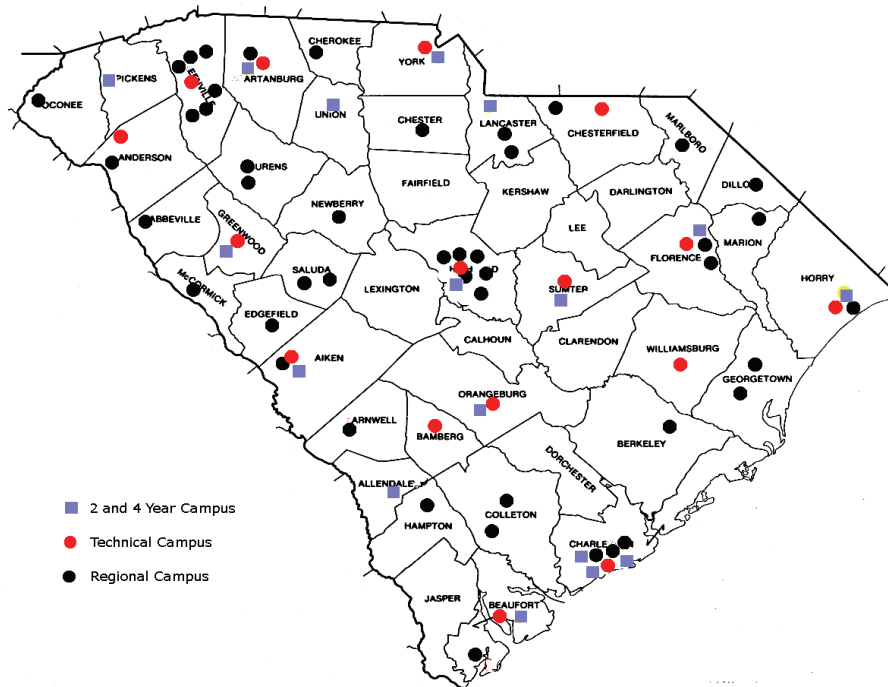
Georgia approved a similar consolidation in October 2008, which merged 13 technical colleges into six, saved the state an estimated \$3.5 million. Also, the distance between schools should not discourage consolidation – Valdosta and Central technical colleges in Georgia will consolidate even though they are 70 miles apart.

Our proposal, including employee benefits, **would save an estimated \$22.6 million.** 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. In light of the significant budget reductions higher education institutions have faced over the last year, we believe it is more important now than ever before to streamline 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 \$12 million.**

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 are currently performed by each satellite campus.

Facilities and Maintenance Cluster Initiative. Collaborating maintenance and facility operations will yield significant savings 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 staff. For example, MUSC, The Citadel, and the College of Charleston are located within five miles of one another, yet all three schools have separate facilities and maintenance 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 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 resources. By reducing costs to the participating universities, we will prevent significant tuition increases for our state's students and families. This initiative will provide **\$7,684,524 of general fund savings.**



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 the state continue funding university lobbyists. For example, 15 institutions of higher education employ lobbyists – paying salaries, lobbying fees, support staff, and rent. 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 eliminating lobbying by

higher education will produce **cost savings of \$2,784,880 million** for all state agencies and schools in general funds.

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 allows the Commission to cancel the lease without penalty upon 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 current location until 2012. We think it is unnecessary for the state to pay operations, leasing, and maintenance costs on a building that serves only three people. Tuition Grants could easily share space with another state agency like the Department of Education which currently has 94 unfilled positions and probably has extra office space. **Cost savings from this consolidation will amount to \$20,700.**

Consolidating the Institute for Archeology and Anthropology into the Department of Archives and History (DAH). The Institute's function could be easily absorbed and housed at DAH, particularly since DAH has adequate physical space and because the Institute and DAH share the overall mission of cultural preservation. 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.**

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 compared to other activities. 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 must fund only those activities that 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 topics related to the local community. Currently, state funds support a portion of instructors' salaries, but we believe the significant user fees generated by this program – over \$3 million – are sufficient to support the program without the need for additional state funds. This will result in a **savings of \$697,927** 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. We support this type of collaboration, particularly 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 University Center's operating costs. This will result in **savings of \$345,250** in general funds.

Arts Commission. Like many states, our state's difficult financial position this year has forced us to make some equally difficult funding decisions that we normally would not propose. In this year's Executive Budget, we propose eliminating funding for the Arts Commission. The Arts Commission administers federal and state grants to local schools, communities, and individual artists. We recognize that artistic and cultural programs add great value to our state, but we simply cannot justify spending money on arts programs when law enforcement and core academic programs are facing such steep budget cuts. Schools in South Carolina already provide arts education and programs to their students, and we believe the State Department of Education is competent to administer these grants to schools. Regarding grants to community programs or individual artists, we do not believe the state should be picking particular entities or artists to support-particularly in an area where the line between good or bad is so subjective. Eliminating funding for the Arts Commission will result in **savings of \$2,453,985**.

State Museum. Similarly, this year's Executive Budget also proposes eliminating funding for the State Museum. The State Museum houses many wonderful exhibits, and has been recognized as one of the best museums in the Southeast by Southern Living Magazine. As with the Arts Commission, we recognize that artistic and cultural programs add great value to our state. Nonetheless, we believe these state funds are more appropriately spent on more core functions of government. Because of the Museum's popularity, we believe the Museum can recoup the decrease in state revenue by modifying its admissions fee schedule or through its endowment. Eliminating funding for the State Museum will result in **savings of \$3,205,385**.

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 worked toward creating the best business climate possible for large capital investment and jobs. We are proud of our Department of Commerce's successes in attracting large-scale capital investment projects. In 2007 and 2008, South Carolina saw record-breaking amounts of capital investment – \$4.05 billion and \$4.16 billion, respectively. Likewise, South Carolina ranked in the top five business-friendly states for the past six years by the Pollina Corporation, ranking number 5 in 2009.

Unlike in years' past, when South Carolina competed with only its regional or national neighbors, our state now competes globally – against countries like China and India that continue to train their workforces and develop their abilities to compete across a broad spectrum of industries. Given this ever-changing global economy and the current global financial crisis, we believe it is imperative that we do what it takes to enhance South Carolina's competitive position.

It is crucial that we provide the Department of Commerce and other development-related agencies with the tools to attract to our state companies looking to begin or expand their operations. Our administration has been consistent in its commitment to create a friendlier business climate in South Carolina.

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.

Developing Our Purchasing Priorities

To develop our purchasing priorities, we first examined the major indicators of success to determine whether state government is currently reaching its goal of improving the conditions for economic growth. We have found that South Carolina is making significant progress, but there are areas that need improvement. Our major funding priorities are those that will best achieve our goal of improving the conditions for economic growth as follows:

Provide for the growth and sustainability of all communities through broad-based incentives and grants programs. South Carolina's approach to economic and competitive challenges in South Carolina should be holistic rather than piecemeal. We want to increase the potential for *all* South Carolinians to benefit from this administration's economic development efforts. Providing for consistent and continued success throughout South Carolina is a vital step toward global competitiveness. We support the Department of Commerce's efforts to determine how best to facilitate our state's economic growth.

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 the positive aspects of living and

working in the Palmetto State provides tangible benefits – every dollar properly invested in marketing returns more than \$20 in direct tourism spending to the economy. Continually emphasizing South Carolina’s superior tourist destinations and business-friendly climate will serve to bring in tourism and capital investment projects, both of which create jobs for South Carolinians.

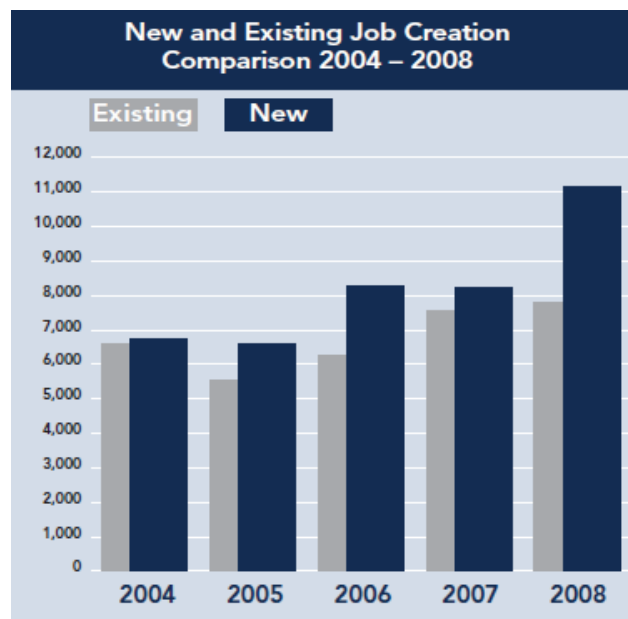
Provide resources and infrastructure for a more skilled and prepared workforce. South Carolina is consistently recognized for its ability to prepare its workforce for the highly-skilled jobs of the 21st century. Through the Center for Accelerated Technology Training, and its programs that work to supply businesses’ labor needs, South Carolina continues to provide top-level training for the jobs created by emerging technologies. 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.

Where We Are Succeeding

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 \$4.16 billion in capital investment and nearly new 19,000 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 tax cut increased opportunities for small businesses in the state to grow, as well as created new investment and jobs. The state now has over 3,000 more small businesses than it had when our administration began. We believe that this pro-business reform will continue to foster small business growth in South Carolina.



Export Growth

South Carolina has seen significant growth in its export markets during this administration. In 2008, export growth increased by 19.65 percent over 2007’s numbers, totaling more than \$19.8 billion in goods sold. Our export growth ranks 18th among the 50 states and 4 U.S. territories and third in the Southeast.

As the state's exports grow, so do our opportunities. About nine percent of South Carolina's total private sector manufacturing employment is supported by exports. In 2008, South Carolina exported goods to 193 countries, including traditional trading partners like Canada and the United Kingdom and quickly growing or emerging markets in China and Vietnam. Last year, South Carolina's number-one export market was Germany, which purchased more than \$4.78 billion in products. Making export-business growth a priority will help diversify South Carolina's presence in the global marketplace.

Opportunities for Improvement

Improving Economic Soil Conditions

This administration has mentioned numerous times that to increase South Carolina's global competitiveness, we must level the playing field as much as possible. Unfortunately, rural South Carolina still lags behind in access to high-speed internet connections. While the United States as a whole has over 75 million total broadband subscribers, the United States is ranked 24th globally in broadband availability – behind South Korea and a majority of the European Union. 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. In the Fall of 2009, our administration created the state's Broadband Commission to determine how to allocate state and federal funding to best provide broadband internet access across our state. As a part of this effort, a non-profit company named Connected Nation is performing broadband mapping services to guide our long-range planning efforts and show us precisely what parts of South Carolina still lacks internet access. In 2007, Connected Nation performed a similar service for Tennessee, which since then has seen a 26 percent increase in broadband internet use and a 90 percent increase among low-income minorities. We look forward to watching our state grow and develop as a result of this initiative.

While we have improved some economic soil conditions, South Carolinians are still burdened by the second highest effective income tax rate in the Southeast – behind only North Carolina. 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 proposed offering an optional flat tax. The tax will not only simplify the current tax code, which includes confusing paperwork for exemptions and deductions, but will also attract economic and human capital to our 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." Simply stated, lower tax rates result in higher economic growth.

We have also expressed concerns that our tax code carves out far too many incentives for only one geographic area of the state or for only one business or industry that may come to our state. According to the Department of Commerce's 2007 report on our incentive system, "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 the five percent corporate income tax as a way to encourage business growth, instead of the special incentives currently in our tax code. South

Carolina would be only the fifth state to phase out the corporate income tax – 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. We have made progress by enacting comprehensive workers' compensation reform in 2007, but the business community still needs the protection of objective standards for determining awards.

Despite South Carolina's 12.3 percent unemployment rate – which translates to over 250,000 unemployed citizens – our state's Employment Security Commission continues to perform mostly as a check-writing agency rather than a job-placement agency. Although more than eight agencies have employment-related programs, there is very little coordination among the agencies – partially because ESC's computer system is so out of date that inter-system communication is impossible. Additionally, under ESC's leadership, the Unemployment Insurance Trust Fund has lost approximately \$1.5 billion since 2001 and is expected to be over \$665 million in debt by the end of 2009. An independent auditor's 2008 report determined that the ESC's accounting staff unfortunately lacked the requisite skills, training, and certification to manage properly ESC's accounts. ESC's mismanagement of UI funds, internal accounting procedures, customer relations, and inter-agency coordination clearly show the need for a single, cabinet-level employment agency directly accountable to the Governor's Office. We look forward to working with the General Assembly on reforming ESC into an efficient, responsible employment agency within our proposed Department of Workforce.

Finally, we remain committed to reducing the burden that frivolous lawsuits have on businesses in South Carolina. Although the tort reform legislation enacted in 2005 has helped reduce business costs associated with litigation, much remains 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 among states in the fairness of its legal climate – the worst ranking that the state has ever received. For South Carolina to remain competitive in a global economy, we need to continue reducing these unnecessary costs incurred by businesses. Nonetheless, there is good reason to believe that meaningful tort reform can be implemented during the next legislative session, as evidenced by legislation proposed by Speaker of the House Bobby Harrell and Senator Larry Martin. The proposed legislation would:

- Allow the non-use of seatbelts to be admissible in civil cases to reduce damages if injury was caused by failure to wear a seatbelt
- Cap punitive damages at the greater of two times compensatory damages or \$250,000
- Cap punitive damages at the lesser of two times compensatory damages or \$250,000 for small businesses
- Establish guidelines for pain and suffering awards and caps at \$350,000
- Limit appeal bond amount to \$25 million (or \$1 million for small businesses)

We will work diligently with the General Assembly to enact business friendly reforms during its next 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:

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.

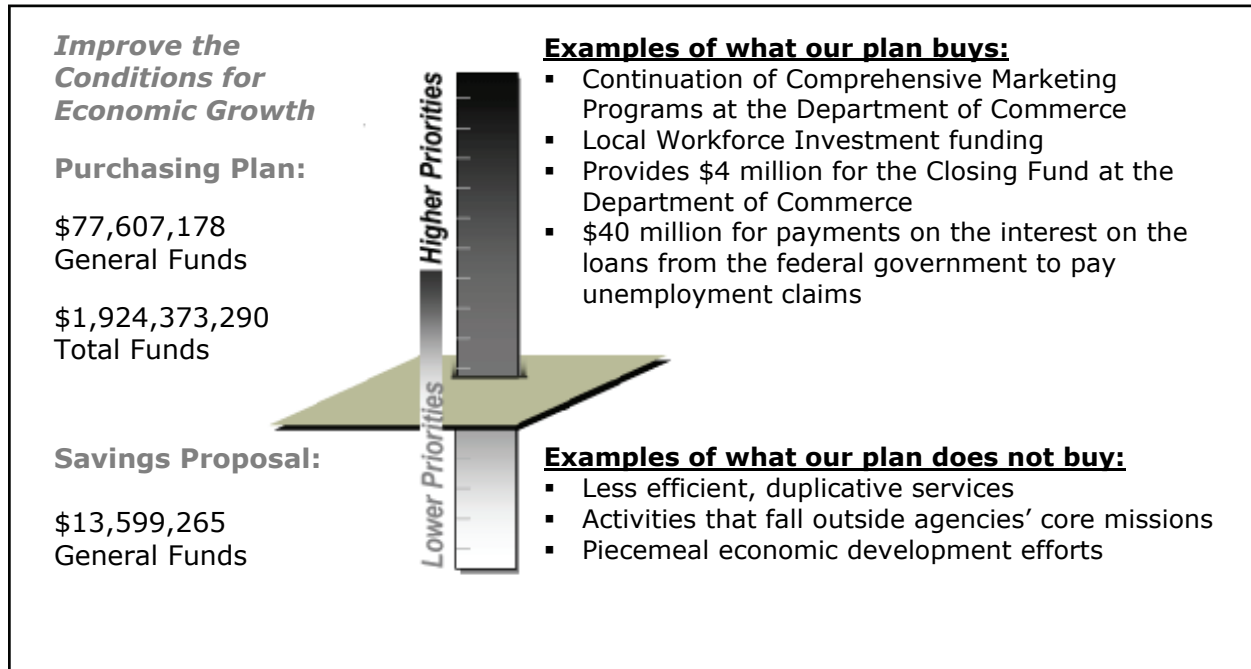
Provide for more effective and broad-based incentives and grants programs. The Department of Commerce has done a good job providing South Carolina with important information on how best to compete by providing the best mix of incentives and grants for our state's economic development efforts. By leveling 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 used cost savings methods simply to *maintain* current funding levels for high priority services. We do not purchase services that, although valuable, have been identified as lower priorities. 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:

Interest Payments on Federal Loan for Unemployment Compensation Benefits. Since 2008, the Employment Security Commission (ESC) has requested federal loans totaling almost \$660 million to cover a shortfall in the Unemployment Insurance Trust Fund. Because of the terms set by the U.S. Department of Labor, the interest on the loan began to accrue because the state failed to repay the loan within one year – increasing the state's liability by approximately \$40 million. 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 **\$40 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's 2009 report, South Carolina's unemployment tax already ranks 7th worst in the nation. As we discussed above, we believe that any attempt to address the loan or future shortfalls must be tied to significant

reforms of the ESC. We eagerly await the Legislative Audit Council review of the agency, which we hope will give us a clear picture of how best to reform the ESC.

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

The Department of Commerce continues to impact 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. Therefore, we propose **funding of \$2,930,357** 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 2008 domestic travel expenditures in South Carolina totaled over \$9.87 billion, a 1.7 percent increase from 2007 and a 36.8 percent increase from 2003. 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 the areas of our state's tourism industry that have the greatest potential to generate 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 tourists from all over the world. We propose recurring funding of **\$8,282,423** 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 **current funding of \$1,663,267** for this workforce training program.

Local Workforce Investment. This initiative helps 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 2010-11 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 the lead agency on economic development for the state, the Department of Commerce should be the agency in charge of all funds directed toward growing our urban and rural economies. We have long advocated that having only 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 the past three years, more than 29 percent of jobs recruited to South Carolina went to

rural communities. Further, in its 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. We believe that we can make this program more successful by moving this program and all associated grant funds to the Department of Commerce. This move would generate **general fund savings of \$133,472** by eliminating duplicative administrative costs.

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, contrary to state law. We propose directing the state amount of funds from the gas tax to run this program. This will allow the agency to hire the needed inspectors to ensure this program is managed well. This will generate **general fund savings of \$390,606**.

Making Tough Choices:

Given the state’s finite resources, we had to make some difficult choices regarding which activities to fund this year. 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 goals. The following reflects these difficult choices:

Reducing pass through funding. This administration has always believed that any public-private endeavor should be open and objective, rather than obscured by complicated funding practices. An example of this type of funding is the Regional Promotions pass through at the Department of Parks, Recreation, and Tourism – a pass through which the agency recommended should no longer be funded. We believe that funding appropriated for an agency 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 for a better funding mechanism for these projects than pass through funding. **General fund savings of \$1,375,000.**

Public Service Activities reaching outside of their core mission of agriculture. Our administration continues to recognize the valuable role that Clemson's and South Carolina State's PSAs play in our rural areas. 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. Such non-core activities include Clemson’s Rural Community Leadership Development program and South Carolina State’s Community Leadership and Economic Development program. Not only are the programs outside Clemson’s and South Carolina State’s core missions, but they are duplicative of services provided through the Department of Commerce and the State Housing Finance and Development Authority. These activities represent a **general fund savings of \$5,770,484**.

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

In South Carolina, nearly one out of every four state tax dollars is directed toward health care. Unfortunately, that significant investment has not led to satisfactory health outcomes in our state. To help South Carolinians get the most out of their health care dollar, we brought the benefit of market-based principles to our health care system. South Carolinians deserve a health system that encourages cost-effective preventative care and offers a wide range of health care options.

Another key ingredient of an individual's high quality of life is the ability to live in a safe and stable environment. South Carolina has programs to reduce child poverty, find permanent homes for foster children, decrease the rate of child abuse and neglect, improve the living conditions of our seniors and those with disabilities, and improve rates of self-sufficiency among our low-income citizens.

Nonetheless, our efforts to improve South Carolina's overall quality of life will be compromised if South Carolinians do not get the efficient and accountable service delivery system that we have called for the past seven years. If South Carolina's government were to be recreated today, then it is inconceivable that 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:

- ✓ 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, which help detect breast cancer in its early stages. Although the overall number of women who get mammograms is

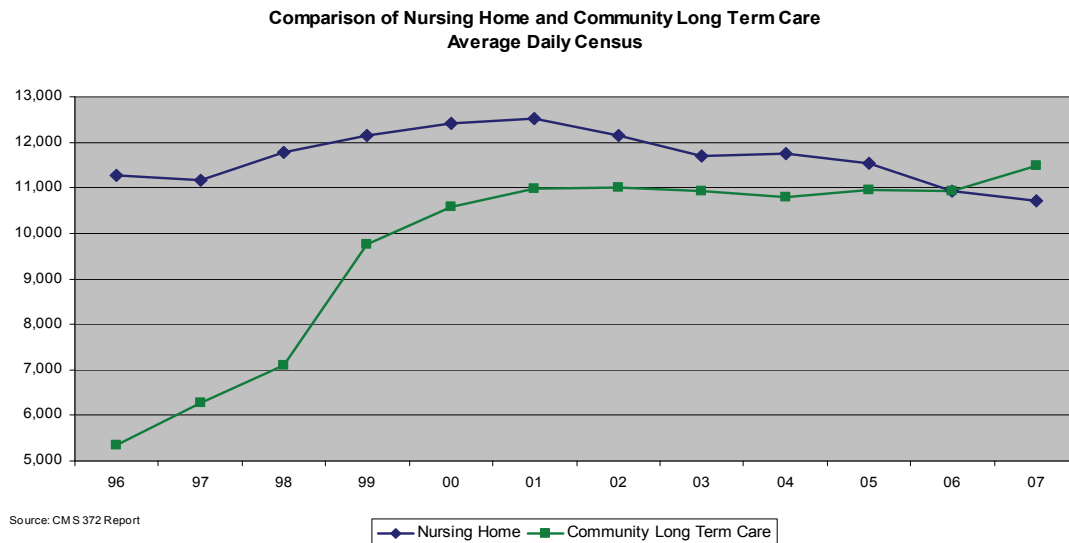
increasing, many women – particularly those who are uninsured, older, or members of certain racial and ethnic minority groups – do not get mammograms at the same rate. Thus, we lowered the “Best Chance Network” eligibility age from 47 to 40 to ensure more women receive the proper testing.

Living in a safe, stable environment. As stated earlier, since the beginning of our administration, the amount of time it takes for a child to be adopted is at one of its lowest levels in six years. In FY 2008-09, 20.3 percent of the Department of Social Services’ foster children were adopted within 24 months, and a total of 523 children were adopted. Since FY 2003-04, we have experienced a 59 percent increase in the number of adoptions finalized.

In addition, the average number of months a child spends in foster care continues to decrease. For the children that were reunited with a parent or caretaker during FY 2008-09, almost 75 percent were reunited within 12 months of being removed from their former environment. In the last three years, the average amount of months spent in foster care decreased from 18.6 to 17.3 months.

Self-sufficiency rates. Increasing rates of independence and self-sufficiency 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, 80 percent of elder-care is provided by an individual’s family.

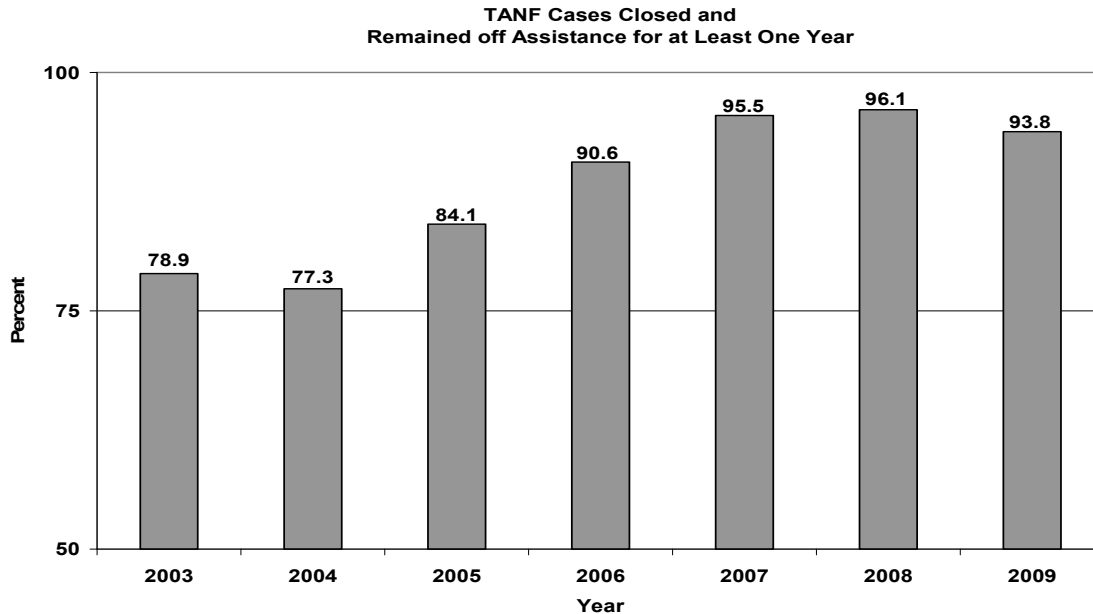
Additionally, we have seen community care surpass nursing home care since 2007. By receiving at-home community care, seniors and disabled persons are not only happier, but they help save taxpayer dollars.



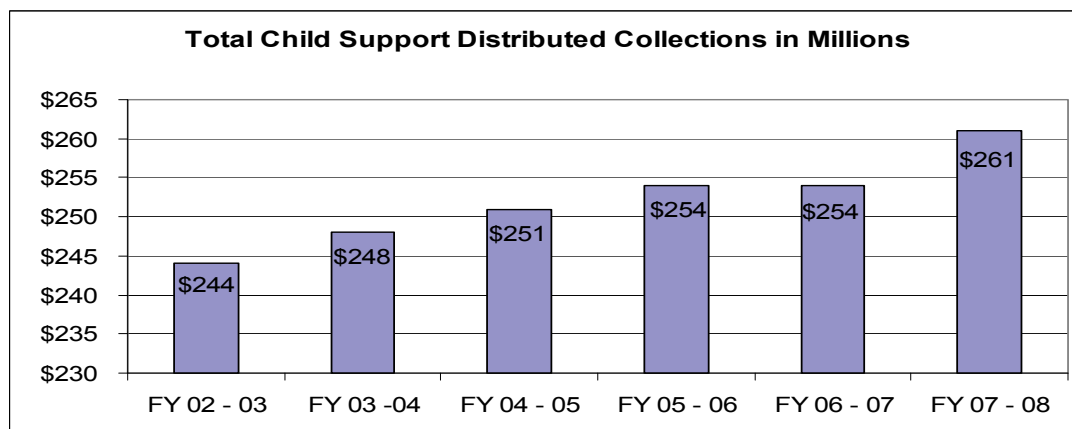
South Carolina is meeting its goals of increasing opportunities for self-sufficiency among low-income families and adults with disabilities. For example, efforts to maximize the number of eligible

persons receiving food stamps in South Carolina have been very effective – approximately 90 percent of eligible South Carolinians receive food stamps, up from 50 percent in FY 2000-01.

Success should not be measured simply by the number of South Carolinians receiving assistance, but also in the number of those who are able to leave the welfare system. The number of South Carolinians who obtain employment, leave the state assistance program, and remain off assistance for at least one year averaged 88 percent during our administration.



The purpose of child support is to ensure that the custodial parent and non-custodial parent share the financial responsibility of raising a child or children. According to the U.S. Census Bureau, approximately 25 percent of custodial parents who are not receiving the child support to which they are entitled live below the poverty line. Over \$106 billion is owed to custodial parents nationwide. In our state, child support distributed collections have steadily increased to \$261 million in FY 2007-08.



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 generally poor across the South, South Carolinians generally rank worse (48th nationally in overall health) than our neighbors in North Carolina and Georgia, who rank 36th and 41st respectively. This is despite the fact that we outrank both states in per capita public health spending. As seen in the "Public Health Funding" chart, we are clearly not getting enough value for our health care dollars.

2008 Public Health Funding (Source: United Health Foundation)		
State	Rank	Dollars per Person
SC	48	\$81
GA	36	\$75
NC	41	\$50

Increase the number of citizens leading healthy lives. Too many South Carolinians make unhealthy lifestyle choices and 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 do not engage in physical activity (47 percent). We rank 45th with regard to the number of women receiving prenatal care and 44th in the prevalence of obesity.

2007 Health Risk Factors Rankings (SC, NC, GA)			
Indicator	Ranking Among 50 States + DC (<u>lower</u> number indicates <u>better</u> 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' lifetimes.

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			

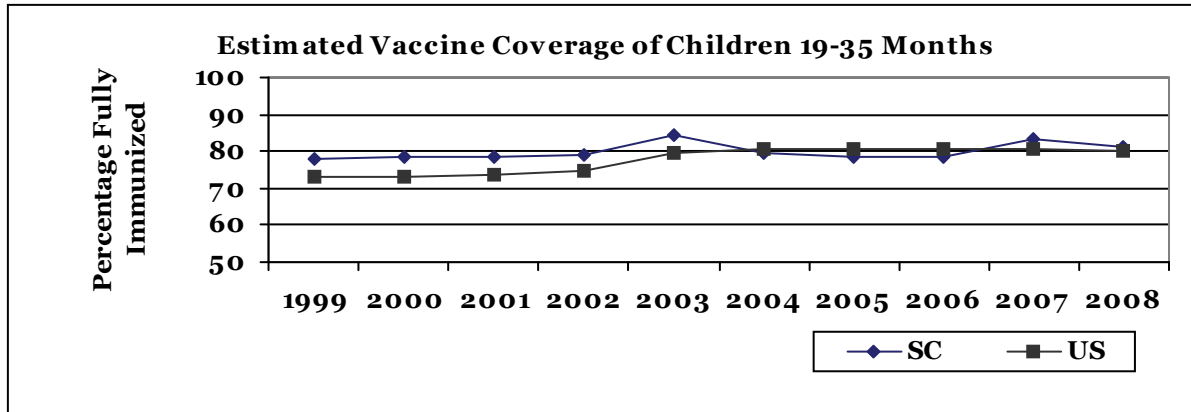
Access to care. About 46 million Americans, nearly 15 percent of the population, do not have health insurance. Although the rate of uninsured South Carolinians decreased by 8 percent over the past year, we still have significant room for improvement in the area of health care coverage. Overall, the uninsured rate in South Carolina (16.2 percent) sits above the national average of 15.5 percent. 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.

Lack of Health Insurance (Overall State Population)	
State	Percent Uninsured
Alabama	13.6
Virginia	14.1
U.S. Average	15.5
South Carolina	16.2
Georgia	17.6
North Carolina	17.2
Mississippi	19.8
Florida	20.7
Source: United Health Foundation, 2008	

Increase the number of children living in a safe and stable environment. According to national standards, more than 9.9 percent of children who have been returned home after a foster care experience will reenter foster care within 12 months because of unsuitable home conditions. In South Carolina (FY 2008-09), the percentage of children who re-entered care was 8.6 percent, which is slightly 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 2009, South Carolina was at 76.5 percent, still short of the national standard. There has been some progress in this area; however, the overall length of time children spend in foster care has decreased by almost 8 percent since FY 2006-07 (from 18.6 months to 17.2 months).

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 17th in the nation with 81.1 percent of South Carolina's children ages 19-35 months being immunized in 2008, which is slightly higher than the national average of 80.1 percent.



Occupational Fatalities represents the impact of hazardous jobs on the population. The state Occupational Safety and Health Act requires employers to provide their employees with a safe and healthy worksite. In 2008, our state had 8.7 occupational fatalities (per 100,000 workers), an increase from 6.7 occupational fatalities (per 100,000 workers) in 2005. In 2008, the national norm was lower at 5.2 deaths per 100,000 workers.

Among children, accidents are the number one cause of death in South Carolina. According to the National Safety Council, approximately 45 percent of unintentional injury deaths 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, 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. Racial disparities 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 directly indicate the economic well-being of children and adults, and are closely linked to physical well-being. According to the U.S. Census Bureau, the percentage of children in poverty (below 100 percent of federal poverty level) decreased from 19.4 in 2005 to 15.6 percent in 2006. However, in 2008 the percentage jumped to 21.8 percent. The percentage of

South Carolina seniors at the federal poverty line is 12.1 percent. The national average for seniors is slightly higher at 12.5 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 uninsured or underinsured. Health insurance coverage increases the likelihood that people will receive the preventive care they need to stay healthy. The increasing number of uninsured individuals will place a large burden on our emergency care systems. Every day in rural South Carolina, more than 100 people receive medical services for which they cannot pay. It has been estimated that the national cost to provide emergency medical services to uninsured is \$130 billion dollars annually. 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 2008 U.S. Department of Agriculture report reveals that 49.1 million Americans, including 16.7 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 six Southern states with high "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 2008 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 \$148,620 on one child up to the age of 17. The year before high school graduation, that child costs about \$11,180. Child support collection is important because 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.

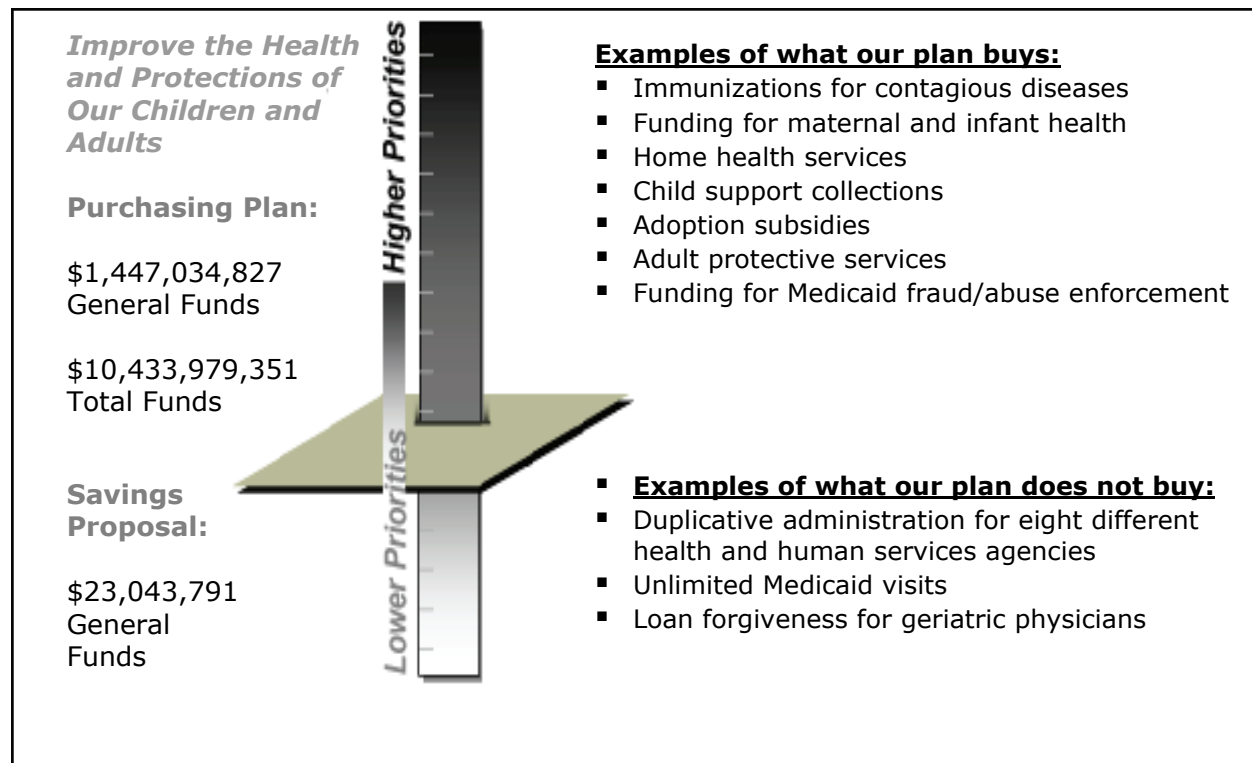
Provide timely and effective interventions when safety is compromised in the home or family environment. Children who are abused and neglected are 25 percent more likely to experience delinquency, teen pregnancy, low academic achievement, drug use, and mental health problems. To reduce costs to society 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

The Federal Medical Assistance Percentages (FMAPs) are used in determining the amount of Federal matching funds for State expenditures for assistance payments for certain social services, and State medical and medical insurance expenditures. As part of the America Reinvestment and Recovery Act, this past year, South Carolina received \$657 million in increased FMAP rate funds from Washington that the state had access to during FY 2009-10. At that time, the General Assembly was able to incorporate six quarters of increased FMAP in the budget – two quarters for FY 2009 and four quarters in FY 2010.

During FY 2011, our state will only have two quarters of FMAP unless Congress extends the windfall. In FY 2012, our state will not have access to this money – meaning that over a two year time period roughly \$650 million will have evaporated from the state budget.

The point is, while the number of Medicaid users and services continues to increase, available funding will decrease. It is important that this year we not only budget for the current fiscal year – but also the next. 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 disease prevention and promotion of 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 communities 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 \$2,914,250 in general 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 **provide funding for this activity amounting to \$3,024,618 in general 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 **provide funding for this activity, amounting to \$8,652,990 in general 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 **provide funding for this activity, amounting to \$373,536,613 in total funds.**

Medicaid fraud and abuse enforcement. In an effort to combat Medicaid fraud and abuse, we propose **increasing funding for the Medicaid Program Integrity Unit in the amount of \$50,000.** During State Fiscal Year 2009, the agency opened 580 cases related to fraud and abuse - more aggressively pursuing investigations of unusual provider billing patterns or recipient misuse of Medicaid services. One example of such efforts involved a pediatrician who 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. Because of the vital role that the Attorney General's Office plays in prosecuting Medicaid fraud and abuse cases, we also propose **increasing funding for the Medicaid fraud prosecution in the**

amount of \$125,000. DHHS estimates that the return on investment for program integrity efforts was \$7.83 for every dollar spent in State Fiscal Year 2009.

Disease prevention and 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 \$140,141,739 in recurring funds and \$69,096,983 in nonrecurring funds – amounting to \$209,238,722 in general 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 **fund this activity with \$542,946,110 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 funding for this activity amounting to \$7,668,461 in general 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 \$23,179,253 in general 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 treatments to specialized treatments 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 funding for this activity, amounting to \$4,176,501 in general 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 funding for this activity amounting to \$814,451,428 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 \$2,077,664 in general 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 program 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 \$7,063,328 in general 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 5.5 years. We propose using administrative savings derived from restructuring the Vocational Rehabilitation Department and the Commission for the Blind to **propose recurring funding for this activity, amounting to \$8,751,461 in general funds and \$41,777,419 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 **funding for this activity amounting to \$47,193,015 in general funds and \$153,570,162 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 12,000 jobs last fiscal year. We propose to maintain

funding for this activity amounting to \$8,622,258 in recurring general funds, and \$143,922,591 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 \$261 million in FY 2007-08. In actual performance, for every \$1 spent in child support activities, it returns \$4.83 (FY 2009). We propose recurring **funding for this activity of \$4,565,640 in general 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 **recurring funding for this activity of \$8,090,284 in general 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 **recurring funding for this activity of \$2,694,821 in general 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 **funding for this activity of \$11,866,719 in general 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 1,700 foster children with a plan for adoption. We propose to **maintain current funding at \$750,000 for this activity.**

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 **funding for this activity with \$4,117,472 in general funds and \$41,142,384 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 **funding this activity with \$565,197 in general funds and \$10,635,760 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 **\$13.3 million in general fund savings in the first fiscal year.** The administrative savings are delineated as follows:

- Department of Health and Environmental Control: \$4,501,147
- Department of Mental Health: \$5,563,376
- Department of Disabilities and Special Needs: \$2,052,701
- Department of Alcohol and Other Drug Abuse Services: \$360,654
- Continuum of Care: \$78,434

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 a one year enrollment cap for the expanded SCHIP program starting July 1, 2010. 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.

The Medicaid agency could then divert the funds that would have been needed to cover new children that became eligible during FY 2010.

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 a one-year cap of enrollees as of July 1, 2010, and **saving \$1,743,541.**

Eliminating the Office on Aging Geriatric Physician Program. Since this loan forgiveness program began in 2005, 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 \$140,000.**

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, substantive changes to services provided to beneficiaries had to be made as well.

S.C. 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 the S.C. State Nutrition, Diet and Health 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 \$159,026.**

DHEC's Bureau of Community Health and Chronic Disease Prevention is part of a network of chronic disease prevention programs aimed at improving the health of our communities across South Carolina. Additionally, SC was one of 20 states which received federal funding for a new five-

year cycle for a Capacity Building Heart Disease and Stroke Program. DHEC's Hypertension Initiative duplicates these efforts thus, we propose **eliminating this program and saving \$512,741.**

AHEC's Health Careers Program, formerly known as the Student Development and Diversity Program, is a well-intended statewide program to get more students interested in health professions. For three years, the Duke Endowment has funded more than half of the initiative. However, AHEC has difficulty collecting the pertinent data to determine whether or not the program is successful. Additionally, this program is less critical than other, core health services competing for scarce taxpayer dollars and should therefore be **eliminated saving \$264,229.**

The Palmetto Poison Center (PPC) serves as the regional poison control center and is the only poison control resource in the State. The PPC is a cooperative effort of Palmetto Richland Memorial Hospital and the USC College of Pharmacy, which provides free services to the public and health professionals. Although this is a worthwhile program, it should be run by one of the state's health agencies, not a state university. We propose **eliminating this program and saving \$186,066.**

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 better manage land use. 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.

Administration's Goals for Improving the Quality of Our Natural Resources:

- ✓ Managing state resources for public benefit.
- ✓ Minimizing the negative environmental effects of business and population growth, industrialization, and development.
- ✓ Regulating and enforcing quality standards.
- ✓ Producing outcome-driven solutions for citizen stewardship.

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 focus on activities that deliver positive outcomes and preserve South Carolina for future generations.

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, flagrant abuse of our environment by litterers 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 purchases land based on objective evaluations of the area's natural resource value, financial leverage, and relative benefit to the public. Since its creation, the Bank has

conserved a total of 141,879 acres of forest/wetlands, 736 acres of urban parks, 9,615 acres of farm lands, and 490 acres of historical lands. In its four years of funding, the Bank has conserved 152,720 acres of land at an average cost of \$528 per acre – 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. Also, the Department of Natural Resources has conserved an additional 86,168 acres of land, while the Forestry Commission has preserved another 15,637 acres over this same time period.

In addition to land conservation, 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 a home runs on solar fuel cells and uses less power than it generates, the excess can be sold 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.

Since 2003, 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.

A public-private partnership broke ground on the new Farmers Market in Lexington County in August 2008, providing an agricultural venue that is second to none. The new market will include an exhibition kitchen, a specialty foods shop, a dedicated children's play area, school bus drop off area, RV Park, on-site restaurants and a 400-seat amphitheater. When it opens in June 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.



Opportunities for Improvement

As we move South Carolina forward, it is clear that we need to rethink how we power our state's homes and businesses. Changes in federal policy and environmental regulations indicate that we can no longer rely on coal as our primary energy source, and that we need to look at alternatives that are both economical and environmentally friendly. These considerations influenced our decision to

oppose Santee Cooper's proposed new coal-fired electricity plant in the Pee Dee region, and we were pleased that Santee Cooper scrapped its plan by working with other utilities to meet our state's energy needs. Rather than relying on coal, South Carolina needs to look to nuclear power as the source for our next generation of electricity plants, and we support Santee Cooper and SCANA's move in this direction.

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. DHEC's environmental oversight is often compromised by its potentially conflicting objectives: weighing health and environmental protection against economic and industrial development. Unfortunately, DHEC's current structure gives the Legislature extensive control over the agency – subjecting DHEC to more politicization than is necessary. This is yet another example – seen all too often in state government – that 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.

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.

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.

Create statewide policies, incentives, and programs aimed at ecological sustainability. 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. Ecological sustainability requires programs that offer flexible and creative responses to conservation and preservation issues while respecting 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.

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.

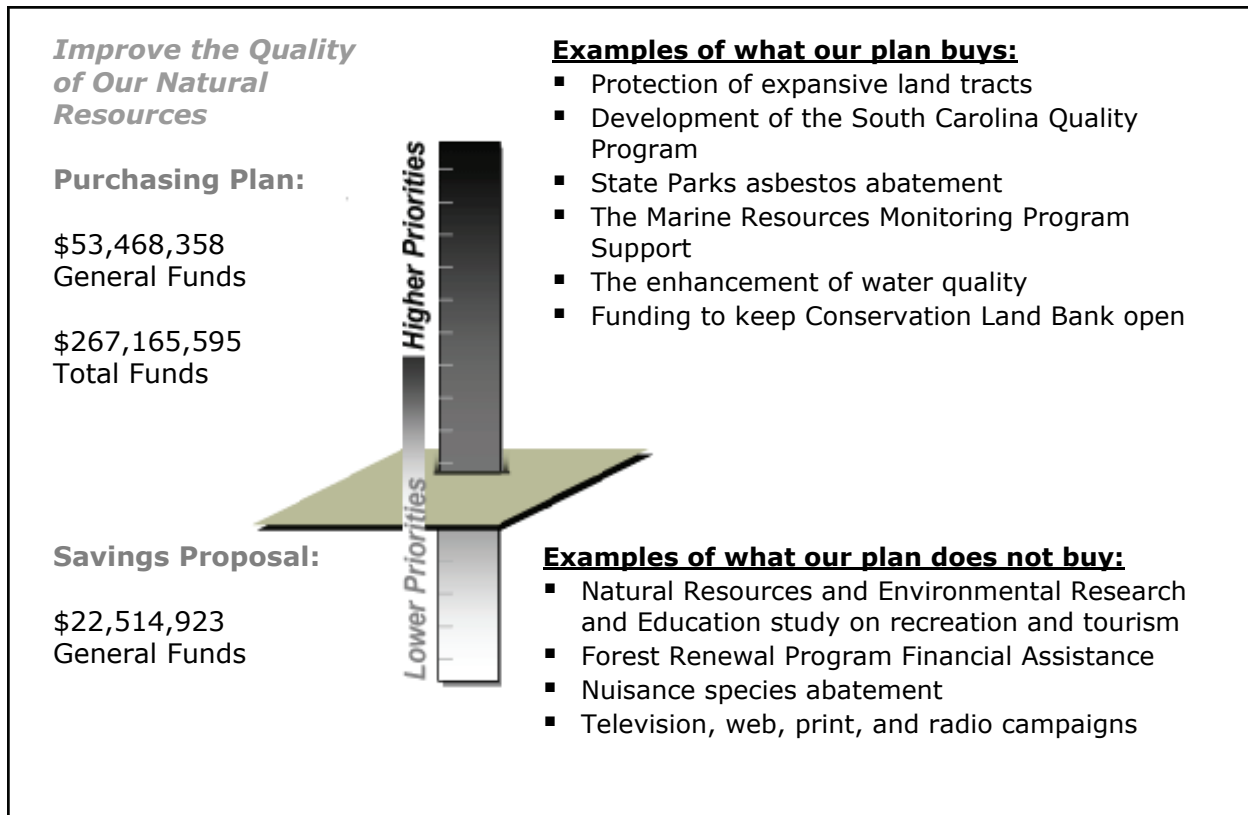
Create and maintain programs aimed at citizen-level stewardship and education. By educating the public, we can significantly reduce the amount of state resources spent to maintain and repair public property. Educational opportunities should provide public information encouraging environmental

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.

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:

Marine infrastructure and resources monitoring program support. This program strengthens South Carolina's marine infrastructure. Marine monitoring provides South Carolina with profitable tourism-related industries while promoting a sustainable ecosystem. We propose funding this program with **\$1,604,512** 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 a funding level of **\$10,953,259** for this program.

Our Plan Saves By:

Consolidating select DHEC, DNR, and Forestry Commission functions into the Department of Environment and Natural Resources. Less than 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 **\$1.41 million of general funds**.

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 \$1,551,891 of general funds**.

Consolidating our state's food-processing regulatory system. Although testing and inspecting South Carolina's food-processing operations is 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 exclusively DHEC's responsibility, thereby **saving an estimated \$474,836 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**.

Eliminating marketing programs currently being performed by Clemson PSA and the Department of Agriculture. The Department of Agriculture's "Certified South Carolina Grown" program provides marketing services for South Carolina's agricultural industry. As a result of the current budgetary needs, and because the Department receives separate funding to support the State Farmers Markets, we believe funding these kinds of marketing services are not a wise use of state revenue. Unlike tourism marketing, which brings in money from outside the state, these kinds of agricultural promotions do not provide the kind of economic return necessary to justify funding this year. We recommend eliminating the funding for "Certified South Carolina Grown" because spending general funds on advertising is not the most responsible way to manage the few dollars we have in this difficult budget year. Our proposal **saves \$1,789,901 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.

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 \$2,693,074 of general funds.**

Television, web, print, and radio campaigns. Our need to fund programs like "Making It Grow" or other media productions is a lower priority than other areas, such as law enforcement or health care. We propose eliminating funding for television, web, print, and radio this year – **saving \$1,294,726 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 South Carolina's "quality of life" a priority. South Carolina provides a unique look and feel that other states and countries cannot provide. We must continually to work not only to maintain, but also improve, our state's quality of life. Quality of life is important to companies that are considering where they want to invest resources and create jobs. Additionally, 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 a high quality of life – including our state's natural beauty, high quality education, and the ease with which citizens live their daily lives. At a fundamental level, however, few factors contribute more to a high quality of life than low crime rates and adequate preparation for natural or man-made disasters.

Unfortunately, in 2008, South Carolina ranked first among all states in the nation in violent crimes per 100,000 people, according to the most recent Federal Bureau of Investigation report. Many factors contribute to South Carolina's struggles in this area including population density, the concentration of youth, economic conditions, the strength of local law enforcement agencies, education levels, and family cohesiveness. However, the lack of consistent and adequate public safety funding has played a disproportionate role in our discouraging crime rates. 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, but the state has also been heavily impacted by droughts for the past several years. Fortunately, these droughts have recently been declared over by the state climatologist. Further, last April's wildfires ravaged portions of Horry County. Finally, Charleston's port and the eight nuclear power facilities spread across the state are also vulnerable to terrorist activity.

South Carolina continues to face challenges in the area of highway safety. In fact, South Carolina has been cited as having the second deadliest roads in the nation and continues to rank high among states in the number of alcohol-related fatalities.

Public safety is a primary concern for South Carolinians – it is a priority in our executive budget.

Administration's Goals for Improving the Safety of People and Property:

- ✓ Decrease personal injuries and property damage that result from natural and man-made disasters 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.

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. South Carolina is performing well in some areas, but there are many opportunities for improvement.

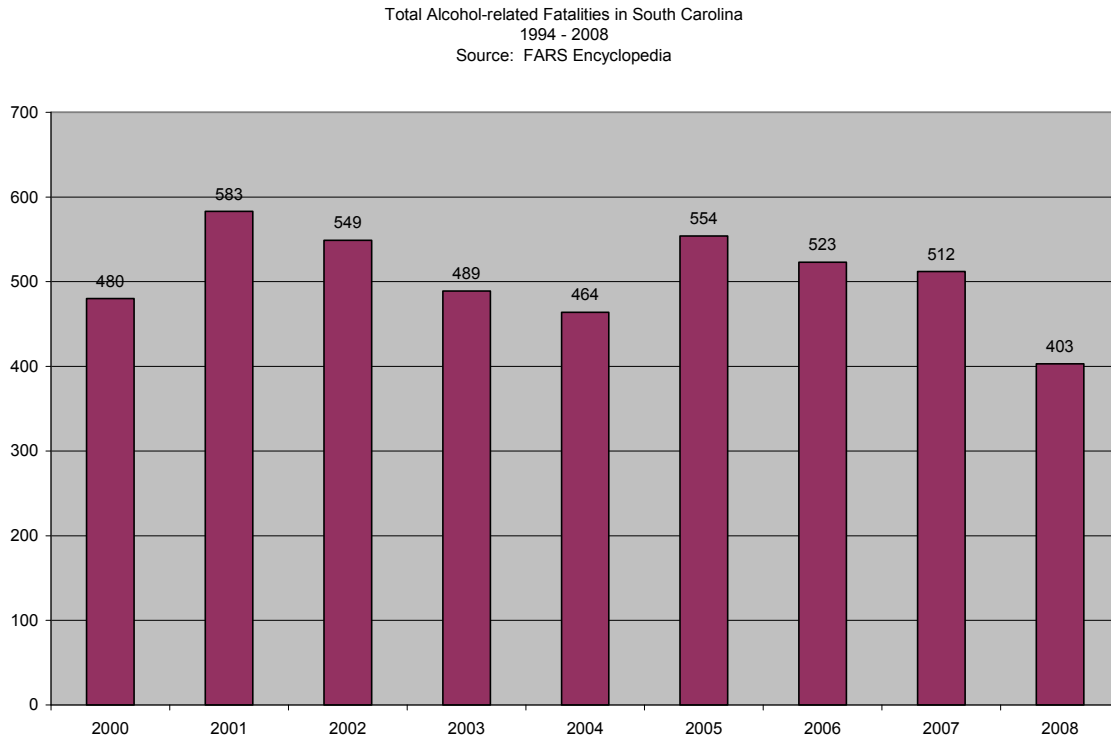
Where We Are Succeeding

As our administration winds down, we should not only look towards the future, but also recognize some of the accomplishments of the past seven years. Though much work remains, much has been achieved toward our goal of making our state as safe as possible for the citizens of South Carolina. The successes of our administration are due in large part to the hard work and dedication of the folks at law enforcement agencies both at the state and local levels. Though by no means exhaustive, our administration would like to highlight just a small sample of our accomplishments:

- Successfully proposed making the DMV a Cabinet-level agency and implemented reforms at the agency that reduced the average wait times at DMV offices from 66 minutes to 15 minutes.
- Successfully advocated for the passage of two bills increasing the penalties for driving under the influence (DUI). The first bill, in 2005, lowered the DUI limit from .1 to .08 in 2003. The second bill, in 2008, significantly toughened the penalties for repeat offenders and grossly intoxicated offenders, and increased the penalty for refusing to take a Breathalyzer test.
- Abolished the antiquated mini-bottle law, which encouraged higher alcohol content (in addition to harming the tourism industry).
- Advanced legislation aimed at reducing the number of domestic violence incidents in South Carolina, including creating a domestic violence task force, instituting mandatory minimum sentences for individuals convicted of domestic violence, and allowing courts to recognize domestic violence convictions in other states when judges are sentencing offenders in South Carolina.
- In 2008, the Department of Corrections executed a contract for energy savings at five of its institutions. 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 estimated annual savings of well over \$1 million in reduced energy costs. The estimated total energy cost savings will be \$11 million over the next 20 years.
- Between 2003 and 2009, the Department of Public Safety seized over \$250 million dollars worth of marijuana, cocaine, crack, heroin and other illegal narcotics and almost \$23 million dollars in drug money.
- Between 2003 and 2009, the Department of Public Safety made more than 4.15 million traffic stops and arrested more than 64,000 for DUI.
- In 2009, the fewest people died on South Carolina road in over a decade.

FY 2010-11 Executive Budget

This year, 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 512 in 2007 to 403 in 2008. While the state remains well above the national average for percentage of highway fatalities involving alcohol, we continue to make progress. During this administration the number of alcohol-related highway fatalities has decreased 27 percent – down from 549 in 2002.



In 2007, we enacted a law stating that South Carolina would not participate in the implementation of the federal REAL ID Act. Twelve other states have since joined our state in passing similar laws. This unfunded mandate by the federal government would force states to issue licenses in a uniform format and containing 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.

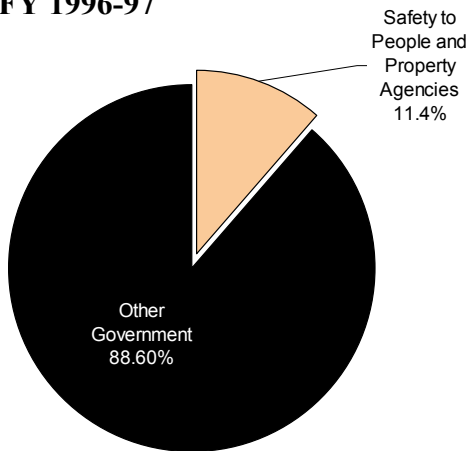
In March 2008 and recently again in December, the Department of Homeland Security attempted to force every state to comply with REAL ID by threatening to refuse to accept a state's driver's license for identification purposes to enter a federal building or board an airplane unless the license was REAL ID compliant. We successfully resisted this tactic, and our citizens still can use their drivers' licenses as a valid form of identification for federal purposes. We encourage the General Assembly to continue to resist REAL ID and encourage every state to join South Carolina in opposing this top-down federal mandate.

FY 2010-11 Executive Budget

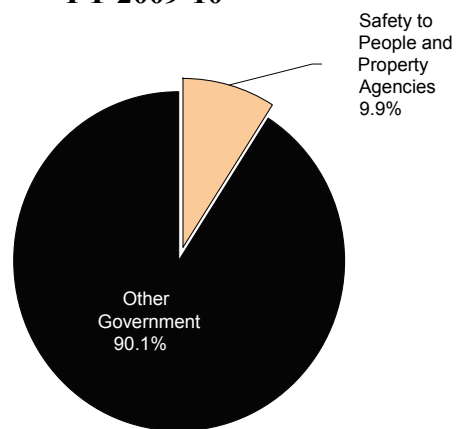
In 2008, our administration successfully promoted the toughest-in-the-nation illegal immigration reform law that did not include an I-9 loophole, but rather requires employers to use E-Verify to ensure that all hires are in the country legally. At the time, South Carolina was only the third state to require employers to use E-Verify – a free program run by the Department of Homeland Security – to check the legal status of their employees.

Unfortunately, from FY 1996-97 to FY 2009-10, 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 13.16 percent.

FY 1996-97

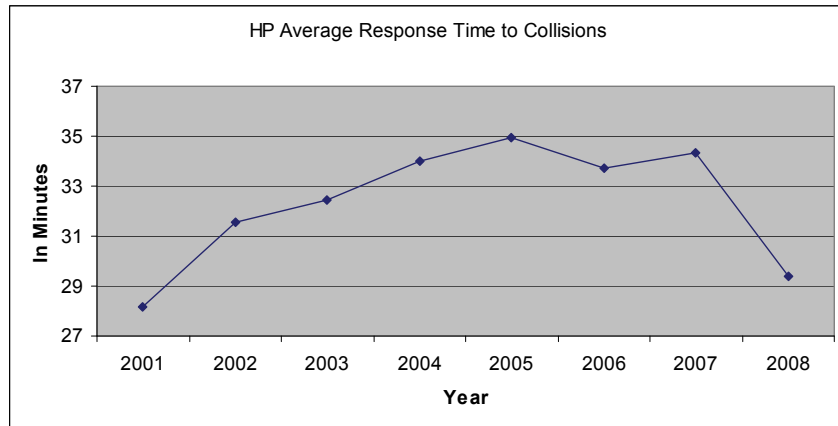


FY 2009-10



This reduction 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 result is a decrease in law enforcement agencies’ ability to retain staff and replace older, broken-down equipment. This percentage is poised to erode further once the stimulus dollars that the General Assembly used to fund many of the law enforcement agencies in FY 2009-10 evaporate next year. As we propose a budget plan for FY 2010-11, recognizing what lies on the horizon in FY 2011-12 and adequately funding law enforcement agencies.

Despite appropriating a smaller portion of the state’s budget, South Carolina continues to make progress in several of the areas relating to public safety: decreasing law enforcement’s average accident response time, the mileage death rate, and the DUI fatality rate. These successes indicate our administration’s continued progress of decreasing preventable injury and loss, increasing emergency response and recovery, and increasing citizens’ confidence in their safety. The state has made additional improvements in forensic casework management, recovering stolen vehicles, and fugitive arrests.



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 537 prisoners per 100,000 population. The state's prisoner incarceration rate ranked 9th in the nation and 8th in the Southern region. Due to managerial and policy changes, the state's inmate escape rate at the Department of Corrections has declined 37 percent, from 0.16 percent in 2002 to 0.10 percent in FY 2009.

Despite our first-in-the-nation violent crime rate, South Carolina has seen a decline in violent crime since 2007. According to the FBI, during 2008, the nation's violent crime rate per 100,000 population dropped by approximately 2.7 percent, while South Carolina's violent crime rate per 100,000 population decreased by 7.4 percent. Although there is obviously room for improvement, we commend South Carolina's law enforcement community for their efforts.

The Department of Juvenile Justice (DJJ) reports that since 2004, only two juveniles have escaped from its Broad River Road Complex – which houses the state's most dangerous juvenile offenders.

The combined assault rate at the Department of Corrections (Corrections) – the number of inmate assaults on fellow inmates, inmate assaults on guards, and inmate assaults on other persons – has decreased 16 percent from 4.3 percent in FY 2004-05 to 3.6 percent in FY 2008-09.

Additional offender management success is reflected by DJJ's School District receiving an "excellent" rating for the sixth consecutive year, as well as an "excellent" improvement rating for the fifth time in the last six years. With these ratings, DJJ was eligible to receive a Palmetto Gold Award – next awarded in January 2010 – for the seventh 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 2003. The 157 GEDs earned by DJJ students in FY 2008-09 represent a 51 percent increase over the 104 GEDs awarded in 2003. The DJJ average for completing the GED is 67 percent, compared to the state average of 60 percent.

FY 2010-11 Executive Budget

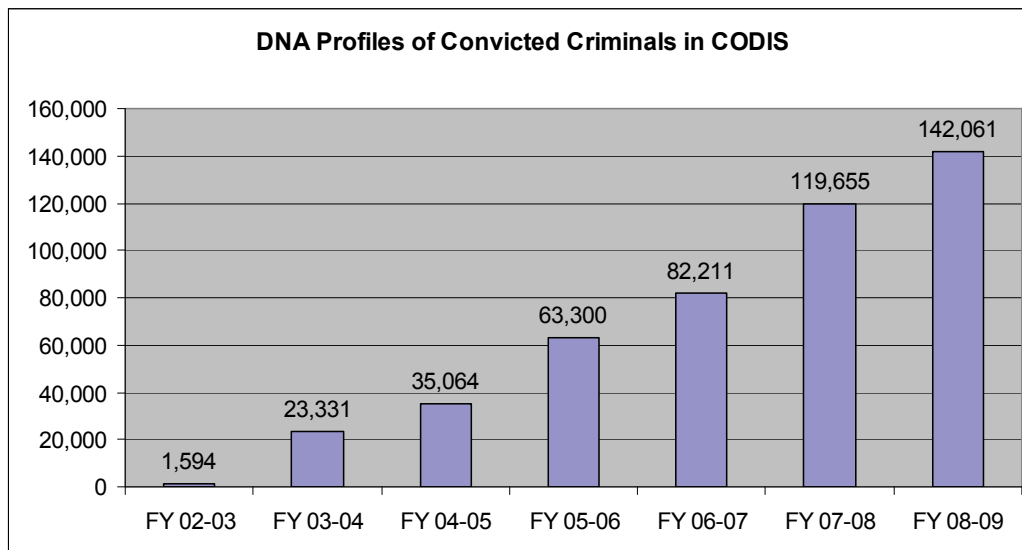
DJJ has seen a significant decrease in the number of lawsuits brought against the department by implementing measures to alleviate overcrowding and meet constitutional standards to ensure the safety of juveniles within its facilities. In 2003, DJJ had 31 pending lawsuits brought by inmates in its care, and inmates brought 12 additional lawsuits in FY 2004-05. Currently, there are only two pending lawsuits against the agency.

DJJ is also succeeding in preventing juvenile recidivism by offenders serving probation, 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 2008-09, DNR's Law Enforcement Division identified and resolved 35,664 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 7,600 man-hours of support to law enforcement agencies that prosecute public safety violations and conduct search-and-rescue operations. Finally, DNR's hunting and boating safety classes, which drew over 10,993 students last year, exhibit DNR's proactive approach to public safety.

The State Law Enforcement Division (SLED) has also made several achievements through its Forensic Laboratory, Vehicle Crime Unit, and Fugitive Task Force. During FY 2008-09, case backlogs were reduced in four of the forensic laboratory units, and forensic laboratory personnel were able to complete over 5.5 percent more cases compared to the number of cases completed the previous year.

SLED has steadily increased the number of convicted criminal DNA profiles that it maintains from 63,300 in FY 2005-06 to 142,061 in FY 2008-09 – an increase of 124 percent. Due to this increase, over the same period of time, the number of offender hits increased 142 percent from 258 in FY 2005-06 to 625 in FY 2008-09.



FY 2010-11 Executive Budget

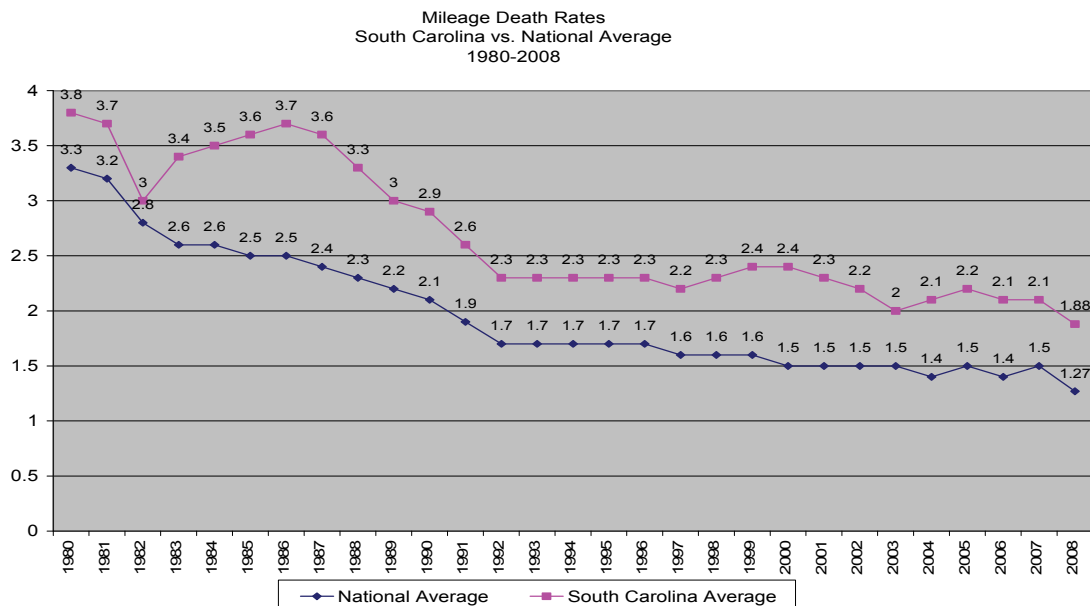
During FY 2007-08, the Vehicle Crime Unit at SLED conducted 532 investigations and made 240 arrests – a 57 percent increase from the previous year. The Fugitive Task Force’s investigations resulted in the arrest of 156 individuals during this period.

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 \$5,818,924 to victims. Since July 1, 1998, PPP has collected and disbursed \$64,167,092 to victims.

Opportunities for Improvement

Despite our many successes in the area of public safety, there remain many areas for improvement. For example, the number of alcohol-related fatalities has fallen from the previous year, but the state is still experiencing a spike that began in the late 1990s. Furthermore, South Carolina’s ratio of alcohol-related fatalities to overall fatalities is among the highest in the nation. As such, we remain committed to a greater reduction in alcohol-related traffic deaths and have taken steps toward reducing such deaths by promoting tougher DUI laws.

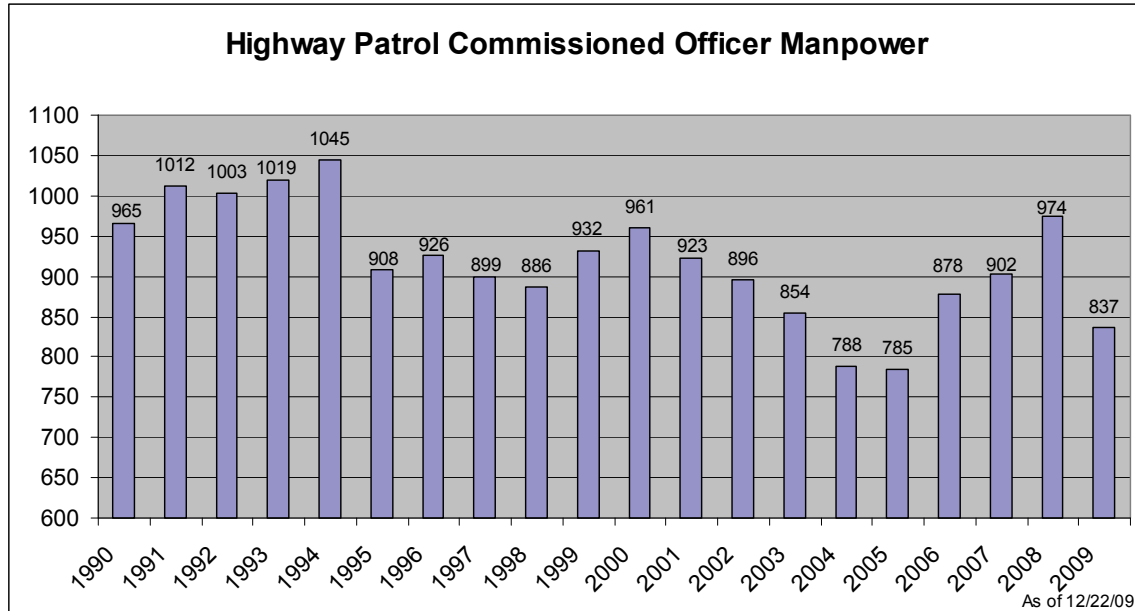
South Carolina’s mileage death rate (MDR), defined as the number of traffic fatalities per 100 million vehicle miles of travel, continues to be higher than the national average. Although South Carolina continues to trend slightly above the national average, fatalities decreased by 157 in 2008 – leaving the state’s MDR at 1.88. This is the lowest total in South Carolina’s history.



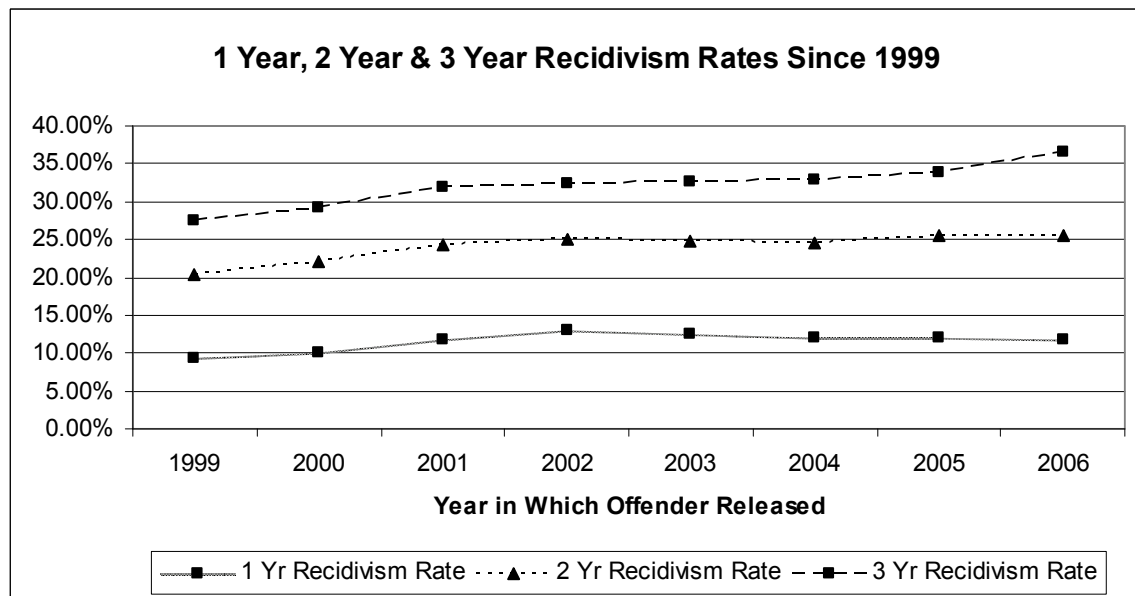
Highway officers currently patrol over 66,248 miles of state roadways, enforce traffic laws, investigate collisions, assist motorists, and provide a safe motoring environment for the public. After increasing the number of troopers to 974 in 2008, the Highway Patrol has, once again, seen its

FY 2010-11 Executive Budget

numbers decrease due to budget cuts. Maintaining the number of troopers is a priority in our executive budget to help to continue to combat the state's high drunk driving rate as well as improve the response time to collisions.

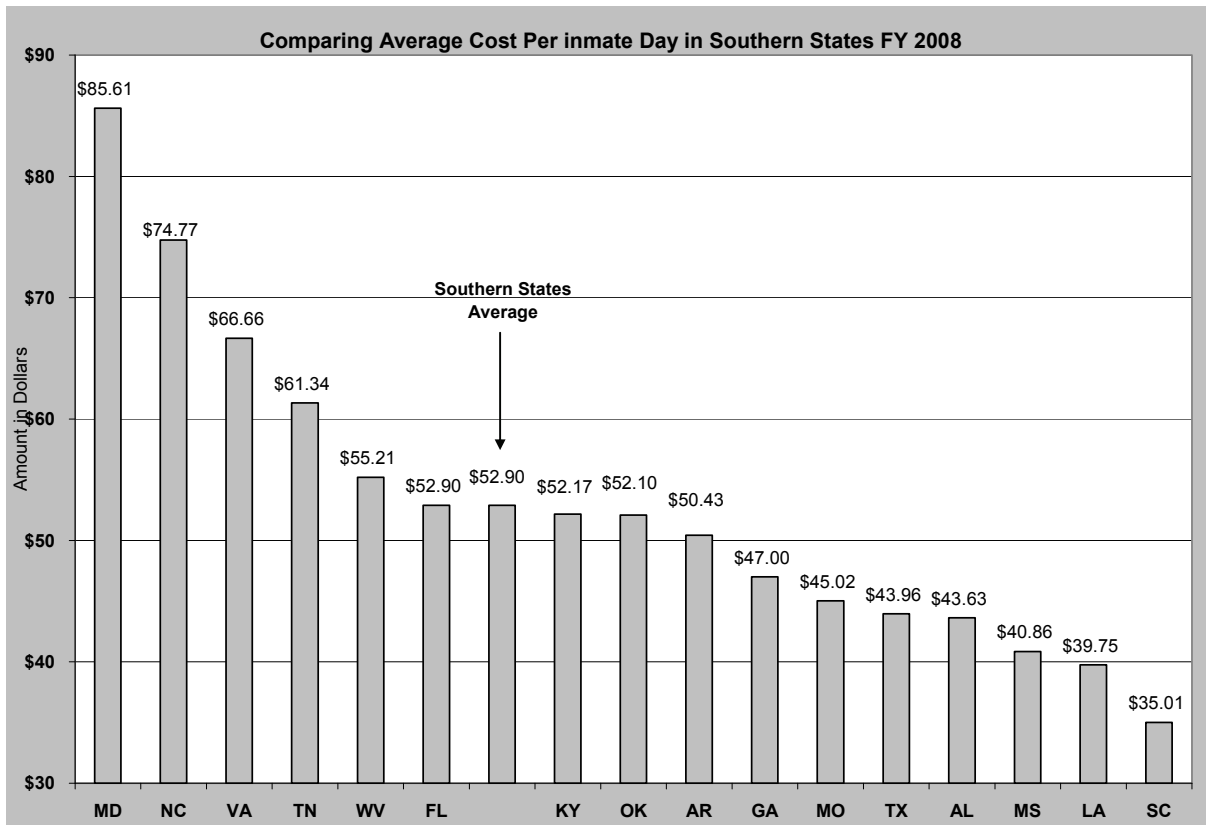


Improvements are also needed in South Carolina's adult recidivism rates, which have steadily risen since 1999. While the state's recidivism rate of 33.6 percent is close to the national rate of 33.6 percent, it remains too high – particularly when compared with recidivism statistics from previous years.



With an incarceration rate that ranks 9th 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 hope 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 systems – South Carolina ranks second to last in the Southeast in funding per inmate per day at \$35.01 (Southeastern average is \$52.90). Despite continued underfunding, Corrections has accomplished remarkable efficiencies – from operating with 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. At the same time, Corrections has gone beyond mere efficiency by reducing escapes and assaults and setting new records for GED completions. Corrections was recently reviewed by the Legislative Audit Council and the National Institute Corrections, and both reviews gave the agency passing marks. As we did last year, this year we request that the General Assembly fund Corrections as a core function of government and avoid another year of deficit spending.



Likewise, PPP has seen the portion of its budget composed of general funds decline from 59 percent in FY 2000 to 33 percent in FY 2009. PPP meets the majority of its funding needs by collecting fees from offenders – a particularly fickle funding source during difficult economic times. PPP needs to receive 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 2010-11 Safety of People and Property results team, are defined as follows:

Prepare for and prevent criminal activities and natural and man-made emergencies. To ensure that an agency is prepared to prevent and manage criminal activity and natural or man-made emergencies, it must be adequately staffed, equipped, and trained.

Effectively manage the state's offender population. The goal of effectively managing offenders is the same as the goal of crime prevention – reduce the risks of harm to our citizens and their property.

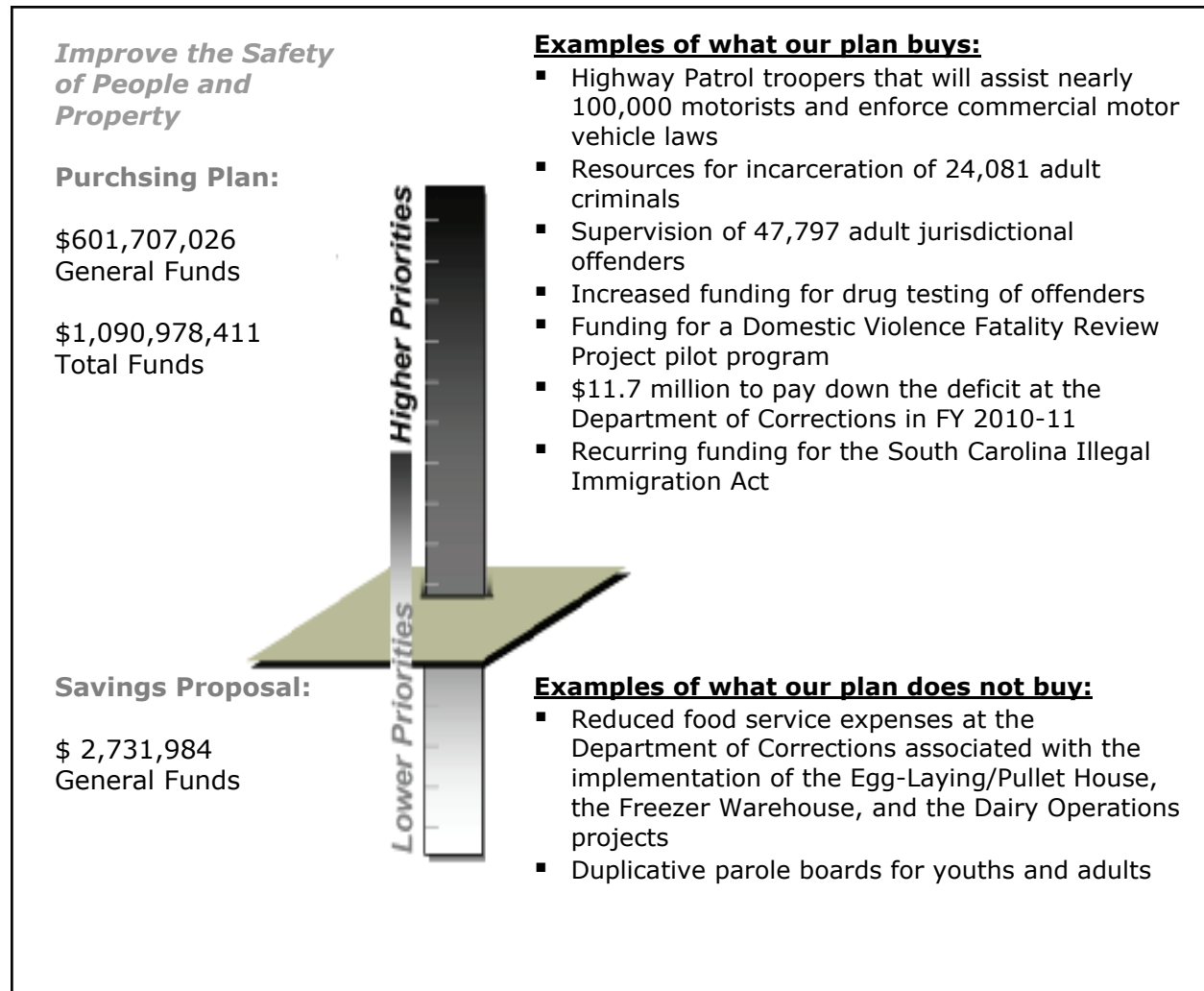
FY 2010-11 Executive Budget

Provide for the enforcement of state laws. The primary focus of our strategy is to ensure that agencies possess the tools necessary to enforce South Carolina's laws. SLED recognizes the need to address violent crime in our state and is doing so by embracing the formation of collaborative interagency law enforcement teams (local, state and federal) to better deal with violent crime in our state.

Provide for response and recovery activities following emergency situations. Once an emergency occurs, be it criminal activity or a natural disaster, the state must be prepared quickly to execute a response and recovery plan. A response and recovery 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, we must focus on purchasing only those public safety 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, while still considered valuable, have been identified as lower priorities. The following table identifies key purchases within our executive budget's total state public safety spending plan. Detailed highlights of our purchasing plan are provided below the table.



Our Plan Buys:

Funding to fully implement the South Carolina Illegal Immigration Reform Act in FY 2010-11. As of July 1, 2009, the South Carolina Illegal Immigration Reform Act requires businesses with

100 or more employees were required to have all new employees present either a valid South Carolina drivers license or use the E-Verify mechanism prior to employment. On July 1, 2010, all businesses, including those with fewer than 100 employees, will have to meet the same requirement. Our administration believes that a law is only worthwhile if it is enforced. Our budget, therefore, proposes an additional **\$2 million in recurring funding to enforce the South Carolina Illegal Immigration Reform Act.**

Funding to pay down the deficit at the Department of Corrections in FY 2010-11. Due to a lack of funding by the General Assembly, the Department of Corrections was forced to run a \$11.7 million deficit in FY 2009-10. We propose including **\$11.7 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 2008-09, these troopers assisted 85,628 motorists, issued 11,398 DUI tickets, and investigated 74,653 collisions. Enforcement of commercial vehicle laws by State Transport Police (STP) resulted in 37,687 driver violations with 1,911 drivers placed out-of-service, and 60,533 vehicle violations, with 10,109 vehicles placed out-of-service. We propose to **increase recurring general funding to \$61.3 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's response time to accidents.

Funding for incarceration of 24,081 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 recommend **increasing funding for this activity by providing \$255.8 million.**

Community Supervision of 46,629 adult jurisdictional offenders. These services include the regular supervision of adult offenders. In order to protect the safety of our agents in performing their duties, it is essential that they receive the proper safety training and equipment. We propose to **increase funding** for this activity by providing **\$17.8 million in our budget for FY 2010-11.** This funding will go towards replacing safety items such as flashlights, holsters, and firearms – thereby providing agents with reliable weapons and reduce the costs of repair and upkeep.

Offender Drug Testing Programs. In many cases, PPP is required to administer regular drug tests to offenders. However, a lack of funding has made it difficult to perform this function, forcing funds to be taken from other activities. In FY 2008-09, PPP conducted 57,115 drug tests, with the cost being paid out of “other funds.” We propose **increasing recurring funding** for this activity by **\$250,000** 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 is 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 in the future.

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 for college football games. Until the last legislative session, a proviso prevented the Department from charging for these services. We recommend that the Department to charge for providing traffic control services in FY 2010-11. This change will lead to **cost savings of \$983,133 annually** in general funds.

Combining the Parole Boards at DJJ and PPP. Currently, the state has separate parole boards at PPP and DJJ. The board at PPP has seven members and a budget of \$554,062, while the DJJ board has ten members and a budget of \$772,277. Despite having a larger budget, the DJJ board hears far fewer cases per year. Because these two parole boards have very similar missions, this presents an opportunity to gain efficiencies and savings by merging them. Combining the two boards will save **\$264,049** annually in general funds.

Making Tough Choices:

Given the state's limited resources, we had to make some difficult choices regarding which activities to fund this year. Due to the budget cuts that the public safety agencies have already sustained, and the fact that public safety represents the core function of state government, we are not proposing additional cuts to state public safety agencies. However, we recommend the following:

Seeking alternative funding for the Adjutant General's Operations and Training and Public Information activities will result in a **reduction of \$20,111** in recurring general funds. We encourage those maintaining this unit to seek other funding so that this service may continue. Crowd control is part of the National Guard's core mission.

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

Our 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; state agencies with multiple accounting and network systems that do not integrate well; and a Director of State Information Technology (DSIT) 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.

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.

Developing Our Purchasing Priorities

To develop our purchasing priorities, we first identified 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.

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 November 2009, the Federation of Tax Administrators reported that 70 percent of all South Carolina taxpayers filed their tax returns electronically in 2009. That means that more than 1.52 million South Carolina taxpayers are filing by computer, which is an increase of 74,326 returns 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 South Carolina taxpayers who earn \$30,000 or less, who are 65 years of age or older, or 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 40,000 taxpayers were able to take advantage of the free file program in 2009.

As a result of DOR's efforts 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 17, 2009, which was a full week earlier than the prior year. 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.

Since last year, the state has implemented a smoking surcharge on state employees' health insurance premiums to discourage smoking and ensure more equitable distribution of health care costs created by tobacco usage. Additionally, we have limited State Health Plan chiropractic care claims to prevent abuse and reign in out of control costs that will result in annual savings of \$6.9 million for the State Health Plan. Finally, the state initiated an employee wellness plan designed to improve chronic conditions of heart disease, diabetes, and obesity with a generic drug incentive for completion of educational programs, which will save the State Health Plan \$5.3 million annually.

This administration realizes the need to equip the small business community with the necessary tools to succeed in this global economy. With that in mind, DOR has worked with the Department of Commerce and other key agencies to implement and operate the South Carolina One Stop for Business (SCBOS). 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. 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 success is evidence that reducing the barriers to opening a business produces positive results in the form of new job opportunities.

At our initiative, the Budget & Control Board has approved several changes to the State Health Plan that will both lower health care costs for the Plan as well as improve the health and lives of our state's employees. First, this year the Board implemented our proposal to add a \$25 per month insurance premium surcharge on tobacco users, and the Board recently adopted our proposal to raise the smoking surcharge to \$40 for single-subscribers and \$60 for family-subscribers for the next Plan year. The surcharge is expected to reduce health care costs in the future by discouraging tobacco use and will result in smokers paying a more equitable share of the health care costs that result from tobacco usage. Second, as we have suggested in the past two executive budgets, the Board imposed a cap on benefits for chiropractic care to limit the abuse exacted by some employees. Although we would have preferred a lower cap, the Board approved chiropractic care limit of \$2,000 per person per year will save the Plan approximately \$6.9 million in this Plan year. Third, the Board adopted our proposal to develop an employee wellness plan geared to improving chronic conditions such as heart disease, diabetes, and obesity. The plan approved by the Board will provide generic drug incentives to employees who participate in educational programs, and it is expected to result in **\$5.3 million in annual savings** to the State Health Plan.

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 both 2008 and 2009, 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 these bills, the Senate has not passed these bills yet. 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 an employee from the state payroll after a standard probationary period. This system 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. According to the Census Bureau’s most recent data, 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 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 way to reduce the unnecessarily high number of state employees is to address the rate at which retired employees 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. 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 who may be trained for the long-run. The second class of TERI participants hit the five-year mark this past calendar year. We recommend that the agencies do not hire the majority of these employees back – as many agencies already plan to do – and disburse job duties among remaining employees, while also hiring new individuals who will be trained for the long-run. This proposal will save **\$5,695,777** in general funds.

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:

IMPROVE THE EFFICIENCIES AND EFFECTIVENESS OF CENTRAL STATE GOVERNMENT SUPPORT AND OTHER GOVERNMENTAL SERVICES

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 encourage the General Assembly 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 operations. With the recent contractual agreement between the state and South Carolina Interactive, a private information technology provider, 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 travel to 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. Reducing the fractured lines of responsibility in the executive branch of government is imperative.

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.

<p><i>Improve the Efficiencies and Effectiveness of Central State Government Support and Other Governmental Services</i></p>		<p><u>Examples of what our plan buys:</u></p>
<p>Purchasing Plan:</p> <p>\$650,535,440 General Funds</p> <p>\$938,702,655 Total Funds</p> <p>Savings Proposal:</p> <p>\$69,160,549 General Funds</p>		<p><u>Examples of what our plan does not buy:</u></p>
		<ul style="list-style-type: none"> ▪ Funding for the creation of a Sunset Commission ▪ Creation of a Central State Travel Office to save on travel expenditures statewide ▪ A statewide accounting system, including reforms to the current IT structure ▪ Military Base Task Force <ul style="list-style-type: none"> ▪ Administrative excess in the CIO's office ▪ Agency premiums paid into the Unemployment Compensation Fund in excess of maintenance levels ▪ Inefficiencies at the Budget and Control Board highlighted by the GEAR report ▪ Health care premium increases for state agencies

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 \$500,000** for the creation of a Sunset Commission.

**IMPROVE THE EFFICIENCIES AND EFFECTIVENESS OF
CENTRAL STATE GOVERNMENT SUPPORT AND OTHER
GOVERNMENTAL SERVICES**

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 recurring funding of \$19,044,941 in general funds for tax collections, compliance, and processing during FY 2010-11.**

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 maintaining recurring funding of \$3,234,047 in general funds** for taxpayer assistance during FY 2010-11.

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 \$2,283,097 in general funds** for the OSB during FY 2010-11.

A Central State Travel Office. South Carolina has over 70 agencies that make travel decisions without standardized regulations or central coordination. In 2007, the LAC recommended that we create a central travel office to oversee each agency's travel practices and ensure the state's travel expenses are as low as practicable. We recommend creating a Central State Travel Office, which will establish clear guidelines to ensure that each agency utilizes taxpayer dollars in the most efficient manner for state travel needs. This new office will also generate savings by negotiating bulk airline and hotel/motel purchases. This **proposal will save \$6,573,666 in general funds.**

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 that the state's current information technology system wastes millions of taxpayer dollars and hinders effective oversight. Here, we reiterate our call to create a cabinet-level Department of Administration to manage state's information technology responsibilities. Currently, the state's Director of State Information Technology (DSIT) has no direct responsibility or authority to deliver IT services to South Carolinians, yet it has unique authority over one of the principle means of improving IT services and reducing the costs of government. Unfortunately, the DSIT – which is overseen by the five separately-elected members of the Budget and Control Board – is insulated from accountability by several layers of government bureaucracy.

If the General Assembly adopts a restructuring plan to make the DSIT more accountable to the Governor during the next legislative session, we will support **providing funding in the amount of \$2 million** for the continuation of the five-year South Carolina Enterprise Information System project. We believe this is an opportunity to significantly reform and improve South Carolina's government.

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 and private-sector offices receive janitorial services at night. State agencies that lease property from the private sector – including the many divisions of the Budget and Control Board – receive standard nightly cleaning service with no reported problems. This simple and logical change would **save the taxpayers approximately \$988,357 annually.**

Restructuring for a more accountable executive branch. Many government agencies provide the same or similar services throughout our state, creating a duplicative system that is not only inefficient but also raises the costs for taxpayers. Our proposals to restructure state government are focused on (1) reducing the number of elected constitutional officers, (2) consolidating agencies that deliver health care services into one, cabinet-level agency, (3) further reforming the Department of Transportation, and (4) moving the Budget and Control Board's administrative functions into a cabinet-level Department of Administration. These proposals would **save the state nearly \$17 million in the first year.**

Reducing the retail lottery commissions to approximately the national average. In our previous four budgets, we have advocated that we reduce retail lottery commissions and use a greater percentage of the lottery-related funds to provide more money for education. Data from lotteries across the country show there is no correlation between a higher retail commission and higher lottery sales. In fact, one study showed that 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 same 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. If sales for the lottery's first year had been \$500 million as predicted, then 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 each, but they have enjoyed an average annual commission 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 **\$9,530,934 annually** that can be used for education.

We propose that all state agencies reduce their travel expenditures by 15 percent this year. Our proposed Central State Travel 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 \$969,718** during FY 2010-11.

**IMPROVE THE EFFICIENCIES AND EFFECTIVENESS OF
CENTRAL STATE GOVERNMENT SUPPORT AND OTHER
GOVERNMENTAL SERVICES**

Reducing the number of participants in the Teacher and Employee Retention Incentive (TERI) program. In many instances, TERI 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. In some ways, the TERI program has been unfair to South Carolina taxpayers because it asks them to contribute more tax dollars to high-salaried managers who were able to take advantage of the system. In fact, TERI employees are paid \$17,000 more than the average non-TERI state employee.

The second class of TERI participants has hit the five-year mark. We recommend that agencies rehire TERI employees only in extreme circumstances. Agencies should disburse job duties among remaining employees and look to hire and train new employees so that the agency can better cope with our current budget constraints. According to 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, we would realize an annual cost savings of **\$5,695,777**. 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.

Implementing efficient cell phone, pager, and satellite phone policies. In June 2008, the LAC issued its audit report of state agency wireless communication usage. 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 the agencies have inadequate usage and employee-monitoring policies. 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 we therefore include the recommendations in our executive budget. Our proposal **will result in cost savings of over \$777,253** according to the LAC.

Merging the Departments of Human Affairs and Consumer Affairs into the Secretary of State’s Office. Throughout this year’s Executive Budget, we have proposed ideas that will allow us to accomplish an increasing number of goals with a decreasing number of resources. As part of our plan, we propose merging the Human Affairs Commission (HAC) and the Department of Consumer Affairs (DCA) into the Secretary of State’s Office. Because HAC and DCA are both tasked with similar missions-protecting the public in the areas of the consumer, housing, and employment marketplaces-we believe it is appropriate to house HAC and DCA within the same agency. We believe the Secretary of State’s Office has the necessary resources and expertise to provide HAC’s and DCA’s administrative needs, given the role it plays in the regulation of businesses. We believe this **proposal will save \$486,360 in administrative costs** without negatively affecting the citizens served by these agencies.

Making Tough Choices:

Given the state's current financial restraints, we had to make some difficult choices regarding which activities to fund this year. Although the activities listed below may have merit, we did not think they will further our goal of making state 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 FY 2010-11. 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, state and local government employees nationwide receive an average of 11 days of paid vacation per 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 taken a similar approach. In addition, several private corporations have begun imposing unpaid holidays. Our proposal will save more money than a voluntary furlough because, unlike furloughs, state offices are closed on holidays – saving operational and utility expenses. Implementing this proposal for FY 2010-11 for nearly 65,000 state employees will result in a **cost savings of \$24.7 million.**

Making ancillary human resources functions self-sufficient. The Budget and Control Board provides a number of human resource services – such as training and development, temporary employment services, and recruiting services – to various state agencies. The Board receives an appropriation of general funds to support these services, but also charges agencies a service fee. We propose removing the general fund appropriation for these ancillary services and require the Board to justify its expenditures entirely in terms of services provided to agencies. Removing the general fund supplement for Human Resource Consulting, Training and Development Services, Temporary Employment Services, Recruitment Services, Workforce Planning, and Executive Education Training will save a total of **\$452,456** 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