



STATE OF SOUTH CAROLINA

Office of Comptroller General

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November 30, 2001

To the Citizens, Governor and Members of the South Carolina General Assembly

It is my pleasure to present to the citizens of South Carolina this Comprehensive Annual Financial Report for the State of South Carolina for the fiscal year ended June 30, 2001. The report provides financial information about the State's operations during the year and describes its financial position at the end of the year.

The report includes information for the use of all parties who are interested in the State's finances. This includes the State's taxpayers, members of the General Assembly, and directors of State agencies as well as the State's investors and creditors.

Management is responsible for the accuracy of the data in this report as well as the completeness and fairness of the presentation. To the best of our knowledge and belief, this information is accurate in all material respects and is reported in a manner that presents fairly the financial position and results of operations of the various funds, account groups, and component units of the State of South Carolina. The report includes all disclosures that readers need to gain an understanding of the State of South Carolina's activities.

For the convenience of users, we have divided the report into three sections as follows:

- The Introductory Section, containing this letter of transmittal; the Certificate of Achievement for Excellence in Financial Reporting for the report as of June 30, 2000; a list of State officials; and an organizational chart of State government.
- The Financial Section, consisting of the general purpose financial statements (combined statements, component unit combining

statements, and notes); required supplementary information; other combining financial statements; and schedules.

- The Statistical Section, presenting comparative financial data and other non-financial data.

MAJOR INITIATIVES

Legislative Initiatives

Like the rest of the nation, South Carolina encountered economic difficulties in its fiscal year ended June 30, 2001, which measurably impacted public programs and spending.

Meeting for its 114th session, the State's General Assembly enacted a budget for the 2001-2002 fiscal year that accommodated approximately \$500 million in revenue shortfalls and directed most State agencies to carry out spending reductions ranging upward to 15%. The budgetary austerity, however, did not deter the legislature from taking significant steps to sustain and accelerate its support of the State's public education system. Most prominent among those steps was the creation of a State-run lottery, the proceeds of which will be directed toward educational purposes. Specific uses of the lottery monies were left to the 2002 General Assembly, but planned lottery-supported programs include a range of college scholarship programs, expansion of school technology, free tuition to attend the State's technical and two-year colleges, youth education scholarships, and stipends for teachers to upgrade their skills.

Aside from creating the education lottery, the legislature took several additional initiatives relative to education. Among those initiatives were increases in funding for the State's basic Education Finance Act, new monies to keep the State's teacher salaries above the Southeastern average, additional funds for the State's K-12 programs, and increased funding for the State's colleges and universities.

Initiatives in areas other than education included funding for the Silver Card senior prescription drug program and additional matching monies for the Medicaid program. Other significant legislation stiffened the State's requirements for the use of seat belts and child restraint devices in passenger automobiles. New laws also provided for suspension of drivers licenses and auto registration for persons failing to pay auto property taxes.

Projects to Implement New Accounting and Financial Reporting Requirements

The Governmental Accounting Standards Board (GASB) issued Statement 33, *Accounting and Financial Reporting for Nonexchange Transactions*, in December 1998 and Statement 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*, in June 1999. As required by generally accepted accounting principles for governments, the State of

South Carolina implemented Statement 33, except for the accrual-basis revenue recognition provisions of that Statement, beginning July 1, 2000. The effects of that implementation are reflected in this report. For the fiscal year ending June 30, 2002, the State must implement the accrual-basis revenue recognition provisions of Statement 33 as well as Statement 34, except for the provisions of Statement 34 that relate to retroactive reporting of major general infrastructure assets. Beginning July 1, 2005, the State must implement the provisions of Statement 34 that relate to retroactive reporting of major general infrastructure assets. Management intends to comply with these requirements no later than the dates specified by the GASB. The State has performed an evaluation of its readiness to implement these pronouncements, has prepared a detailed work plan, and has begun implementation.

Note 3 in the Notes to the Financial Statements within this report reflects the effects of implementing Statement 33 (except for the accrual-basis revenue recognition provisions of that Statement). Management anticipates that compliance with GASB Statement 34 and the remaining provisions of GASB Statement 33 will significantly affect the content and format of the State of South Carolina's Comprehensive Annual Financial Reports (CAFRs) for fiscal years ending after the implementation dates described above. However, the State's management has not yet determined the extent of those effects on specific account balances, financial statements, notes to the financial statements, or other presentations within the CAFR.

ECONOMIC CONDITION AND OUTLOOK

Over the last three decades the economy of South Carolina has grown faster than that of the rest of the country. Businesses have migrated here from all over the world to take advantage of the State's skilled labor force, competitive wages, lower-priced land, excellent port facilities, accessibility to markets, and in recent years, substantial tax incentives. Since 1970, industry has made \$77 billion of investments in plants within the State.

The State's recreation and retirement industries also have been rapidly growing economic sectors over the last three decades. Each year more retirees move here to take advantage of the area's mild climate, lower cost of living and special tax incentives for people over 65 years of age. The number of individuals receiving Social Security retirement pay has grown at a rapid average annual rate of 4.0% since 1970. The annual income from retirement now exceeds an estimated \$9 billion.

The State's coastal areas have emerged as one of the leading recreation centers on the east coast, providing even more stimulus to South Carolina's growing economy. Personal income in Horry County, which includes the Myrtle Beach area, has grown at an extraordinary 9.8% per year over the last two decades and exceeds \$4.3 billion.

Since 1970, over 550,000 people have migrated to the State to take advantage of a growing economy and to retire here. Total personal income of South Carolina has grown over twelve-fold, one-fifth faster than growth in personal income in the United States. During the high inflationary 1970's, personal income grew at an

average annual compound rate of 11.9% compared to a much lower 10.7% nationwide. Even in the lower inflationary 1980's personal income in South Carolina grew a healthy 8.7% per year, compared to a lesser 7.8% nationwide. Employment in South Carolina over the last two decades has grown one-fifth faster than in the United States as a whole.

Although South Carolina has been one of the poorer states in the nation since the War Between the States, the State is closing the gap in wealth between it and the rest of the country. In 1970, per capita income of South Carolina was only 75% of the national average, but has since increased to 81% of the national average.

The State's economy has begun the 2001-2002 fiscal year with a modest slowdown in growth. Employment in the State was up by 350,000 in September 2001 versus its level during the recession of 1991. Although statistics for the fiscal year ended June 30, 2001, were not yet available from the Department of Commerce, the State's Board of Economic Advisors (BEA) estimated that personal income growth was in the range of 4.5% to 5.5%, but slower than last year's rate of growth.

In recent years, the State passed economic development legislation to further enhance the attractiveness of businesses to locate in rural sections of the State by increasing substantially the tax incentives that companies may be eligible to take. Through 2000, over 650 companies have taken advantage of the tax incentive package offered by the State. Global companies such as BMW, Honda of America, Bridgestone/Firestone, Michelin, and Hoffman-LaRoche have located corporate headquarters or have constructed multi-million dollar manufacturing facilities within the State. In addition to these projects, there have been other announcements of new plants or additions to existing plants in the State, which will contribute to the State's continued growth.

The BEA met on November 7, 2001, and reported that the State's Budgetary General Fund revenue collections at the end of the first three months of the 2001-2002 fiscal year were less than anticipated. As a result, the BEA lowered the Budgetary General Fund revenue estimate for the 2001-2002 fiscal year by \$310 million from the amount included in the Appropriation Act for the 2001-2002 fiscal year. The BEA anticipates a recovery in the State's economy in the 2002-2003 fiscal year as a result of interest rate reductions adopted by the Federal Reserve since January 2001.

FINANCIAL CONTROLS

Internal Controls

The Statewide Accounting and Reporting System (STARS) is the State's budgetary-basis operating accounting system. This double-entry system, installed in the 1981-1982 fiscal year, processes cash and budgetary transactions and maintains records for all budgeted funds and some unbudgeted funds. The State's higher education institutions and most of the enterprise entities maintain separate accrual-basis accounting systems.

The Comptroller General's Office maintains an automated annual financial reporting system as well as an automated interface between STARS and that system. The Comptroller General's Office uses these automated systems to prepare this report in accordance with generally accepted accounting principles (GAAP). State agencies that use STARS prepare year-end forms to report amounts needed to adjust their budgetary-basis balances to conform with GAAP. The Comptroller General's Office then enters the data from these forms into its GAAP financial reporting system. Additional information entered into the GAAP financial reporting system is derived from the audited financial statements of certain entities and from other supplemental data provided by those entities.

The State's internal controls, designed by the management of the State, provide reasonable assurance that the following objectives are achieved:

- Reliability of financial reporting,
- Effectiveness and efficiency of operations, and
- Compliance with applicable laws and regulations.

The concept of reasonable assurance recognizes that the cost of a control should not exceed the resulting benefits.

Budgetary Controls

South Carolina's annual Appropriation Act includes legally adopted budgets for the Budgetary General Fund and for aggregated Other Budgeted Funds. Except for the Retail Sales Tax and selected other taxes estimated on a modified accrual basis, the State estimates revenues on a cash receipts basis. Appropriations for the 2000-2001 fiscal year covered all expenditures deemed applicable to that year and paid on or before July 20, 2001.

In most years, a provision of the State's Appropriation Act allows agencies to carry forward up to 10.0% of original Budgetary General Fund appropriations to the next year. This provision, however, was automatically suspended for the 2000-2001 fiscal year in order to help prevent a deficit in the Budgetary General Fund. Any unexpended Budgetary General Fund appropriations lapse unless the Appropriation Act specifically authorizes agencies to carry them forward to the next fiscal year.

State law does not require encumbrance accounting. Accordingly, the State (except for some higher education institutions) does not record encumbrances. The State currently maintains budgetary control for expenditures at the level of summary object category within each program of each organizational unit. Except for accounts of higher education institutions, STARS verifies that an account has sufficient remaining appropriations before it will charge an expenditure to that account. Organizational units may request transfers of appropriations among object categories and/or among programs within the same budgetary fund. The Budget and Control Board has authority to approve these appropriation transfers within certain limits.

The initial budget appears in the annual Appropriation Act. The Budget and Control Board reduces the Budgetary General Fund's appropriations during the year if it anticipates a year-end operating deficit. Likewise, the State Board of Economic Advisors (BEA) may approve revisions of estimated revenues of the Budgetary General Fund during the year. The Budget and Control Board took action in November 2000 to sequester \$98.611 million that had been set aside for appropriation in the 2001-2002 fiscal year in response to the Board of Economic Advisors' (BEA) November 2000 downward revision of estimated revenues. In May 2001, the Budget and Control Board also reduced agencies' appropriations by approximately 1%, or \$48.117 million.

In November 2000, the Governor approved \$127.218 million of supplemental appropriations that the General Assembly had approved in June 2000. Budgetary surplus from the 1999-2000 fiscal year was the source of funds for these supplemental appropriations.

State law specifies procedures for processing requested budget changes in Other Budgeted Funds and for permanent improvement projects.

THE REPORTING ENTITY

The State's reporting entity includes all of the funds and account groups that make up the primary government of the State of South Carolina as well as its component units. The funds and account groups of the primary government are under the oversight of the State's General Assembly and the Budget and Control Board. The primary government consists of agencies, departments, funds, and institutions that are not legally separate from the State.

Component units are legally separate entities for which the State and its elected officials are financially accountable. Criteria to determine financial accountability include the ability of State officials to appoint a voting majority of the entity's governing body, the ability of the State to impose its will on the entity, and the potential for the entity to provide a financial benefit to the State or impose a financial burden upon the State. The State's discretely presented component units are: the South Carolina Public Service Authority (Santee Cooper); South Carolina State Ports Authority; Connector 2000 Association, Inc.; the Savannah Lakes Regional Loan Fund; and the South Carolina First Steps to School Readiness Board of Trustees. Note 1a in the Notes to the Financial Statements provides a more complete description of the State's reporting entity.

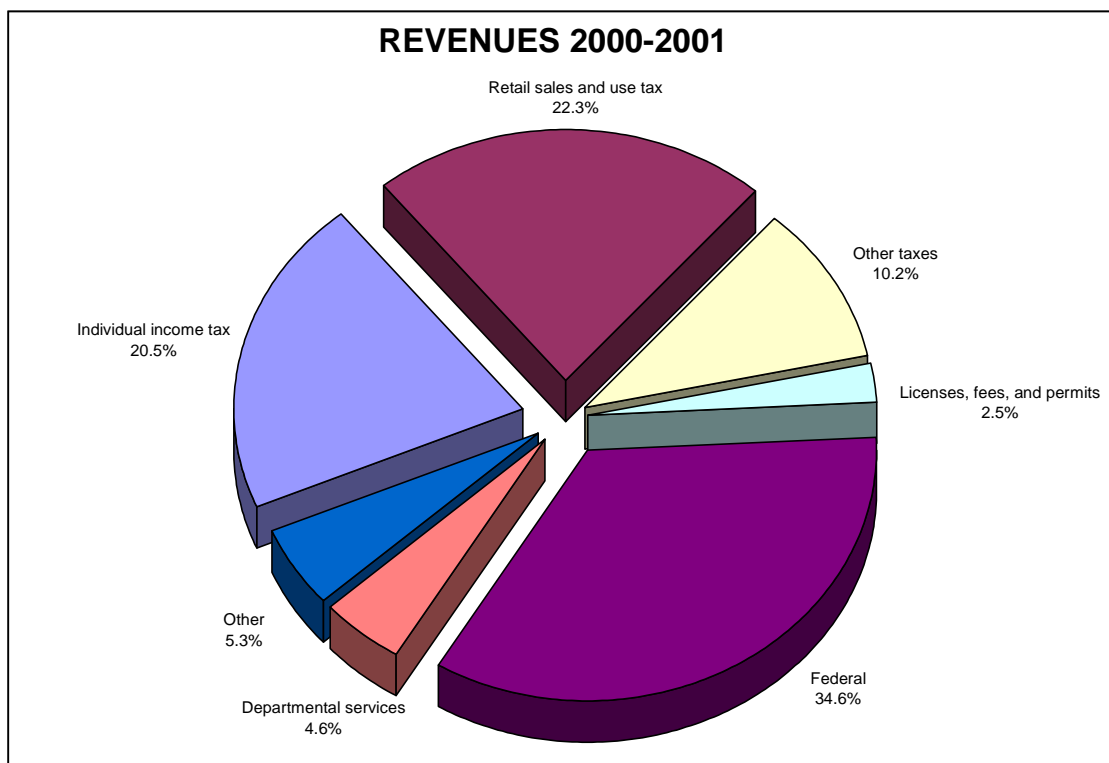
FINANCIAL OVERVIEW

The following sections detail revenues and expenditures of the State's General and Special Revenue Funds. In addition, for the fiscal year ended June 30, 2001, other financing sources exceeded other financing uses for these funds by \$865.704 million, primarily because of the bond proceeds associated with the State's securitization of its tobacco settlement revenue stream.

Revenues

The State's most significant sources of revenue are its 5.0% retail sales tax, its individual income tax (2.5% to 7.0% tax rates), and Federal grants. The following schedule summarizes revenues of the General and Special Revenue Funds for the fiscal year ended June 30, 2001 (expressed in thousands) and the amounts (expressed in thousands) and percentages of increases (decreases) in relation to prior year revenues:

Revenues	2000-2001 Amount	Percent of Total	Increase (Decrease) from 1999-2000	Percentage Increase (Decrease)
Individual income tax.....	\$ 2,492,877	20.5%	\$ 39,412	1.6%
Retail sales and use tax.....	2,705,207	22.3%	28,521	1.1%
Other taxes.....	1,241,362	10.2%	13,691	1.1%
Licenses, fees, and permits.....	309,017	2.5%	2,950	1.0%
Interest and other investment income....	243,201	2.0%	88,448	57.2%
Federal.....	4,172,450	34.6%	463,492	12.5%
Departmental services.....	563,667	4.6%	24,118	4.5%
Contributions.....	159,357	1.3%	(91,978)	(36.6%)
Fines and penalties.....	74,959	0.6%	5,942	8.6%
Tobacco legal settlement.....	73,747	0.6%	(22,527)	(23.4%)
Other.....	100,569	0.8%	16,919	20.2%
Totals.....	\$ 12,136,413	100.0%	\$ 568,988	4.9%



Interest and Other Investment Income increased because of gains on the sale of investments during the fiscal year and interest earned on bond proceeds held on deposit.

Federal revenues grew because of an increase in eligible Medicaid recipients and higher prescription costs and because of increased Federal highway funding received by the South Carolina Department of Transportation.

Contributions decreased as a result of the activities of the South Carolina Transportation Infrastructure Bank. The amount of contributions revenue that the bank received during the 2000-2001 fiscal year decreased in response to the completion of certain major road building projects.

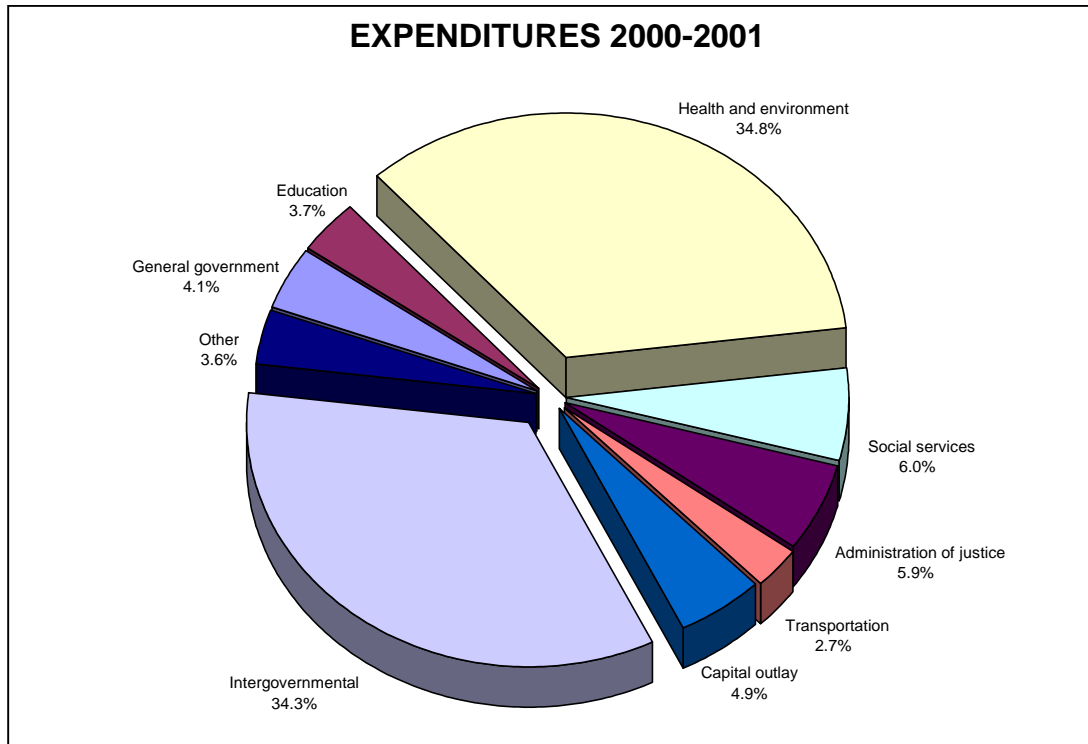
During the 2000-2001 fiscal year, the State received reduced Tobacco Legal Settlement payments. This revenue varies according to tobacco consumption and the financial capabilities of the settlement participants.

An increase in the Other revenues category resulted from larger than normal refunds of prior-year Medicaid expenditures being reported during the current fiscal year.

Expenditures

The following schedule presents a summary of General Fund and Special Revenue Funds expenditures for the fiscal year ended June 30, 2001 (expressed in thousands), and the amounts (expressed in thousands) and percentages of increases (decreases) in relation to prior year expenditures:

Expenditures	2000-2001 Amount	Percent of Total	Increase (Decrease) from 1999-2000	Percentage Increase (Decrease)
Current:				
General government.....	\$ 488,865	4.1%	\$ 65,930	15.6%
Education.....	443,540	3.7%	40,087	9.9%
Health and environment.....	4,200,086	34.8%	599,278	16.6%
Social services.....	720,602	6.0%	46,249	6.9%
Administration of justice.....	716,462	5.9%	21,617	3.1%
Resources and economic development	198,351	1.6%	17,948	9.9%
Transportation.....	324,207	2.7%	(194,377)	(37.5%)
Capital outlay.....	589,107	4.9%	61,338	11.6%
Debt service:				
Principal retirement.....	139,977	1.2%	32,356	30.1%
Interest and fiscal charges.....	102,435	0.8%	20,803	25.5%
Intergovernmental.....	4,132,596	34.3%	258,298	6.7%
Totals.....	\$ 12,056,228	100.0%	\$ 969,527	8.7%



Expenditures in the General Government category increased primarily because of tobacco settlement proceeds paid to tobacco growers, quota holders, and warehousemen for losses in reduced cultivation of tobacco in the State.

The growth in the Health and Environment category resulted primarily from increases in Medicaid eligibility and pharmaceutical costs.

Transportation expenditures were less in the 2000-2001 fiscal year because of the completion of certain major transportation projects, including the new by-pass near Myrtle Beach.

An increase in various State road and bridge construction projects led to an increase in expenditures for Capital Outlay.

Debt Service expenditures for retirement of principal and interest increased due to the issuance of State School Facilities Bonds and bonds issued through the State Transportation Infrastructure Bank during the 1999-2000 fiscal year.

Status of Fund Balances

GAAP-basis fund balances for the General Fund and Special Revenue Funds at June 30 (expressed in thousands) for the last five years were:

	2001	2000	1999	1998	1997
General Fund					
Reserved.....	\$ 153,079	\$ 388,139	\$ 335,038	\$ 286,945	\$ 450,686
Unreserved, designated.....	—	—	31,360	—	—
Unreserved, undesignated.....	(173,802)	33,297	—	(109,468)	(294,233)
Total General Fund.....	\$ (20,723)	\$ 421,436	\$ 366,398	\$ 177,477	\$ 156,453
Special Revenue Funds					
Reserved.....	\$ 875,445	\$ 556,474	\$ 350,722	\$ 204,427	\$ 205,377
Unreserved, designated.....	344,509	50,082	336,826	165,328	128,640
Unreserved, undesignated.....	1,964,129	1,210,905	1,015,125	775,557	541,769
Total Special Revenue Funds.....	\$ 3,184,083	\$ 1,817,461	\$ 1,702,673	\$ 1,145,312	\$ 875,786

The reserved component of fund balance represents amounts legally required to be segregated and amounts that cannot be appropriated for future expenditure. The unreserved component of fund balance is computed as total fund balance less reserved amounts.

The designated portion of unreserved fund balance reflects tentative plans for future use of available financial resources. For 1997, 1998, and 2001 the General Fund's reserve requirements exceeded its total fund balance. This created a negative unreserved component of fund balance in the General Fund, even though the total fund balance was positive in 1997 and 1998. In these years and in 2001, the General Fund did not have an unreserved designated fund balance because it had no net financial resources to finance any tentative future spending plans.

At June 30, 1999, the State had tentative plans to use \$91.766 million of the fund balance in its Budgetary General Fund to pay for selected recurring and nonrecurring items. Of that amount, only \$31.360 million in net financial resources was available in the General Fund at June 30, 1999, to finance those tentative plans.

In June 2000, the State General Assembly approved a plan to appropriate \$96.914 million of the fund balance in its Budgetary General Fund in the 2000-2001 fiscal year to pay for certain recurring and nonrecurring items. Of that amount, only \$33.297 million in net financial resources was available in the General Fund at June 30, 2000, to finance those items. Had the Governor approved the plan in June 2000, the General Fund at June 30, 2000, would have had an unreserved, designated fund balance of \$33.297 million. However, the Governor delayed signing the bill until November 16, 2000, and as a result, the General Fund at June 30, 2000, had an unreserved, undesignated fund balance of \$33.297 million.

PROPRIETARY OPERATIONS

Primary Government

There are several proprietary segments of South Carolina's primary government. Significant segments among these include the State Housing Finance and Development Authority, which provides low-cost housing to the State's citizens by issuing bonds/notes and by administering Federal contracts and grants, and the Education Assistance Authority, which issues bonds for the purpose of making loans to eligible students.

Financial highlights of these segments (expressed in thousands) for the fiscal year ended June 30, 2001, are as follows:

	Housing Authority	Education Assistance Authority
Operating revenues....	\$ 53,720	\$ 49,973
Net income.....	14,717	10,869
Total assets.....	731,675	602,267
Total fund equity.....	200,243	108,770

Discretely Presented Proprietary Component Units

The State's two largest proprietary operations are discretely presented proprietary component units.

The Public Service Authority (Santee Cooper) is South Carolina's State-owned public power resource. The Public Service Authority (Santee Cooper) produces and sells electric power and wholesale water to individuals, businesses, electric cooperatives, and municipal power departments. The Public Service Authority (Santee Cooper) made payments to the State's General Fund of \$8.497 million during its fiscal year ended December 31, 2000. The distribution to the General Fund is based primarily on operating cash flows and mandatory reserve requirements.

The State Ports Authority develops and maintains State harbors and seaports and handles the commerce through these ports.

Highlights of segment financial information (expressed in thousands) for discretely presented proprietary component units for the fiscal year ended June 30, 2001, follow:

	Public Service Authority (Santee Cooper)	State Ports Authority
Operating revenues....	\$ 862,415	\$ 104,655
Net income.....	66,320	18,394
Total assets.....	3,563,812	543,261
Total fund equity.....	935,174	377,324

FIDUCIARY OPERATIONS

The most significant of the State's Fiduciary Funds are the four retirement plans administered by the South Carolina Retirement Systems. Those plans include: the South Carolina Retirement System, the Police Officers' Retirement System, the Retirement System for Members of the General Assembly, and the Retirement System for Judges and Solicitors. The State has funded all four of these plans in accordance with recommendations of the consulting actuaries, both in the current period and in past periods. The State has no pension liability for those plans at June 30, 2001.

The South Carolina Adjutant General's Office administers the National Guard Pension System. The State recorded a \$5.333 million pension liability for that plan in the General Long-Term Obligations Account Group at June 30, 2001. See Note 7, "Retirement Plans," in the Notes to the Financial Statements for more information.

DEBT ADMINISTRATION

The State finances many of its major capital needs by issuing bonds. Some of this debt is general obligation debt backed by the full faith, credit and taxing power of the State. Much of the debt, however, is revenue bonds and notes associated with specific State agencies and discretely presented component units. Specific revenue flows of particular agencies and discretely presented component units service revenue debt.

Moody's Investors Service has rated South Carolina's general obligation bonds as "Aaa," and Standard & Poor's and Fitch, Inc., rate these bonds as "AAA," the highest ratings that these services award. The Comptroller General's Office annually furnishes the State's Comprehensive Annual Financial Report and related information to the bond rating firms. This process is critical to ensuring that the State maintains its current high bond ratings.

During the fiscal year ended June 30, 2001, South Carolina issued \$786.587 million and retired \$125.813 million in general obligation bonds payable by governmental funds. The State budgets and pays principal and interest on capital improvement bonds and State school facilities bonds from current resources of the Budgetary General Fund. The Department of Transportation Special Revenue Fund pays the debt service on highway bonds. At June 30, 2001, the Higher Education Funds reported State institution general obligation bonds outstanding of \$96.310 million.

State law limits annual debt service expenditures rather than directly limiting the amount of outstanding debt for general obligation bonds and notes. The annual debt service margin at June 30, 2001, was \$9.878 million in total for all institution bonds, \$21.496 million for highway bonds and \$52.753 million for general obligation bonds excluding institution and highway bonds.

Net general obligation bonds/notes outstanding per capita (which excludes general obligation bonds payable from Higher Education Funds) is an indicator of the State's debt position that citizens, investors, and management may find useful. The following table shows this amount at June 30 for the last three years:

	<u>2001</u>	<u>2000</u>	<u>1999</u>
Net general obligation bonds/notes outstanding.....	\$2.055 billion	\$1.394 billion	\$1.141 billion
Net general obligation bonds/notes outstanding per capita.....	\$512	\$347	\$294

The General Services Fund, an Internal Service Fund, had \$34.003 million of limited obligation lease revenue bonds outstanding at June 30, 2001.

The primary government had revenue, Tobacco Authority, and Infrastructure Bank bonds, notes, and certificates of participation of \$3.253 billion outstanding on June 30, 2001. Revenue, Tobacco Authority, and Infrastructure Bank bonds, notes, and certificates of participation outstanding (expressed in thousands) by agency were:

South Carolina Housing Authority.....	\$ 505,506
South Carolina Education Assistance Authority.....	426,220
Tobacco Authority bonds.....	934,530
Transportation Infrastructure Bank bonds.....	832,575
Various higher education institutions.....	547,419
Other State agencies.....	7,178
Total—primary government.....	<u>\$ 3,253,428</u>

During the fiscal year ended June 30, 2001, the Education Assistance Authority advance refunded \$19.200 million in revenue bonds to gain flexibilities provided by the 1993 bond resolution. For additional details on this refunding, see Note 10 in the Notes to the Financial Statements.

In addition, discretely presented proprietary component units had the following amounts of bonds and notes outstanding (expressed in thousands) at June 30, 2001:

South Carolina Public Service Authority (Santee Cooper).....	\$ 1,992,561
South Carolina State Ports Authority.....	151,563
Connector 2000 Association, Inc.....	222,353
Total—discretely presented component units.....	<u>\$ 2,366,477</u>

CASH MANAGEMENT

State law requires full collateralization of all State Treasurer bank balances. Agencies and component units may have collateralization policies that differ from those of the State Treasurer.

Legally authorized investments vary by fund, but generally include obligations of the United States and certain agencies of the United States, obligations of the State of South Carolina and certain of its political subdivisions, certificates of deposit, collateralized repurchase agreements and certain obligations of United States corporations. Under State law, the State Retirement Systems Investment Panel may make limited investments in equity securities for the State's Pension Trust Funds. For additional details, see Note 1g in the Notes to the Financial Statements.

As provided by law, the State Treasurer deposits money in a general deposit account. The State records earnings of the general deposit account as revenue of the General Fund. The Treasurer deposits other monies into various special deposit accounts, each of which retains its own earnings.

State agencies that issue their own checks participate in pooled bank accounts. These agencies issue checks against the pooled bank accounts. Meanwhile, the State Treasurer invests account balances until the checks clear.

The State participates in a securities lending program to generate additional investment income. At June 30, 2001, the fair value of the State's securities on loan under this program was \$1.916 billion. For additional details on the securities lending program, see Note 4d in the Notes to the Financial Statements.

Investment income for the General Fund totaled \$114.151 million for the fiscal year ended June 30, 2001. This income includes realized and unrealized gains and losses.

RISK MANAGEMENT

The State generally does not purchase commercial insurance for the risks of loss to which it is exposed. Instead, State management believes it is more economical to manage its risk internally. Accordingly, the State sets aside assets for claim settlement in its Internal Service Funds—specifically, in the Insurance Reserve Fund (IRF), the Health and Disability Insurance Fund, and the State Accident Fund.

The IRF services claims for many of the risks of loss to which the State is exposed, including the following: property insurance on government-owned buildings, the contents of such buildings, equipment, and automobiles; automobile liability insurance on government-owned vehicles and school buses; tort liability insurance for government premises and operations; and medical professional liability for hospitals. The IRF purchases aircraft and ocean marine insurance, areas in which the IRF has limited expertise. Further, the IRF purchases reinsurance to limit losses in the areas of property, boiler and machinery, automobile liability, and medical professional liability. Reinsurance permits partial recovery of losses from reinsurers; but the IRF, as direct insurer of the risks, remains primarily liable.

The Health and Disability Insurance Fund was established to provide health and dental insurance coverage for eligible employees and retirees of State agencies and school districts and group life and long term disability insurance coverage to eligible active State and public school employees. The State, the predominant participant, retains the risk of loss. Under the health insurance program, participants elect coverage through either a health maintenance organization or the State's self-insured plan. All dental, group life, and long-term disability coverage for which the State retains the risk of loss is handled through the State's self-insured plan.

Section 42-7-10 of the South Carolina Code of Laws, as amended, established the State Accident Fund to provide a program of workers' compensation insurance coverage to State entities. The State assumes the full risk for covered claims. The Fund purchases reinsurance to reduce its exposure to catastrophic losses on insured events; however, as direct insurer of the risk, the Fund remains primarily liable.

The State conducts various risk control programs to help minimize losses. For example, the health insurance program conducts extensive wellness education programs for covered employees that promote development and maintenance of healthful lifestyles.

The State also administers the Patients' Compensation Fund, an insurance enterprise, which provides medical malpractice insurance to participating licensed health care providers within the State of South Carolina.

AUDIT

An independent audit of the general purpose financial statements was performed jointly by the State Auditor and the independent certified public accounting firm of Deloitte & Touche LLP. This report for the fiscal year ended June 30, 2001, includes an unqualified opinion, the best possible result of the audit process.

The audit described above is not intended to meet the requirements of the Federal Single Audit Act as amended. The Single Audit reports for the State are issued separately.

CERTIFICATE OF ACHIEVEMENT

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the State of South Carolina for its comprehensive annual financial report (CAFR) for the fiscal year ended June 30, 2000. In order to be awarded a Certificate of Achievement, a government must publish an easily readable and efficiently organized CAFR whose contents conform to rigorous program standards. Such reports must satisfy both generally accepted accounting principles and applicable legal requirements. A Certificate of Achievement is valid for a period of one year only.

The State of South Carolina has received a Certificate of Achievement for the last thirteen consecutive years (the 1987-1988 through 1999-2000 fiscal years). Again this year, the State will submit its CAFR to the Certificate of Achievement for Excellence in Financial Reporting program of the GFOA. I firmly believe that South Carolina's report for the fiscal year ended June 30, 2001, meets the requirements to receive the Certificate of Achievement.

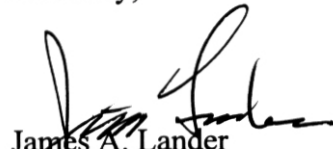
ACKNOWLEDGMENTS

Production of this report would not have been possible without the support of all State agencies and component units that supplied GAAP closing data on a timely basis. As we strive to produce this report in future years and to improve its quality and content, continued support of these parties is essential.

We extend special appreciation to Mr. Bryan Stone, staff photographer for the South Carolina Office of the Governor, for providing the cover photographs and several other images that appear in the report. The South Carolina Office of

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Sincerely,



James A. Lander
Comptroller General