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It's longer than I was thinking it would be, but if nothing else, it's a decent primer on what's actually in this thing.

CLS

December 19, 2012

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

South Carolina is on the move. Our unemployment rate is now 8.6%, down from 10.6% when I took office nearly two years ago. We've also created **XX,XXX** new jobs together. But you don't have to take my word for it – at the University of South Carolina's Economic Outlook Conference last week, Professor Doug Woodward said, when it comes to foreign and domestic business investment, "We look the best of all states going into 2013." I couldn't agree more.

Manufacturing is growing again in the Palmetto State, and we're seeing a rise in housing prices, along with a dramatic increase in building permits. This means construction jobs, too.

We're back on track, but what's happening in Washington threatens to derail us. Congress and President Obama have less than two weeks left to resolve their differences before we're thrown over the fiscal cliff, to face higher taxes and reduced federal support for many programs. Higher taxes are the last thing we need when we're trying to create jobs. The threatened cuts to our armed forces could also have a serious impact on South Carolina's economy, where we have critical military installations that are at the very heart of our communities. For this reason, my budget recommends additional funding for the Military Base Task Force that Comptroller General Richard Eckstrom chairs.

The rising cost of healthcare continues to be the greatest challenge we must confront as we fight to rein-in spending. Even if we opt-out of Medicaid expansion, the Affordable Care Act will cost us \$67.4 million in the upcoming year. Every dollar that Washington forces us to spend on this program is a dollar we can't put into our schools, into our roads and infrastructure, or back into the pockets of those who work hard every day to earn that money in the first place. Furthermore, the costs associated with public employees' pensions and health benefits will cost the General Fund nearly \$80 million more in the 2013-14 fiscal year, crowding out nearly all other programs.

While the fight over Medicaid expansion has put the spotlight on the Department of Health and Human Services, other state healthcare agencies are also being affected by new rules from Washington. An appreciable fraction of the nearly \$5 million recommended for the Department of Disabilities and Special Needs is to respond to changing federal reimbursement guidelines. The budget recommends that \$600,000 of this increase be used to implement the Supports Intensity Scale, which is a widely respected assessment tool used to determine what level of support a client needs in order to live independently. This instrument is critical to the development of valid treatment plans, but also, the equitable allocation of the state's funds for those with special needs.

The Executive Budget also steps-up state support for the Department of Mental Health's telepsychiatry initiative, which is a true public-private partnership that includes the Duke Endowment, the South Carolina Hospital Association, and various hospitals and universities across the state. This cost-saving program allows providers to support patients in underserved areas in real-time, even outside of regular hours.

Turning to education, the budget I am presenting to you today maintains Base Student Cost, while increasing funding for both teacher supplies and instructional materials. Although my children attend public schools, I continue to believe that parents deserve a choice – especially those who live in communities where public schools aren't making the grade. For this reason, I

am recommending an additional \$5 million for charter schools next year.

Choice is not a silver bullet, though. Building better schools will require new methods of teaching, but will also require a greater degree of accountability for our teachers and administrators. Teach For America's winning approach has won it countless awards all across the country. Last year, I recommended and the General Assembly graciously approved \$2 million for this exceptional program. This year, I ask for \$1 million more, to help TFA expand into more schools. I also applaud Superintendent Mick Zais for receiving a waiver from the federal government under the Elementary and Secondary Education Act. The flexibility granted through this action will enable us to more meaningfully evaluate our schools and educators, and subsequently take the necessary steps to improve performance.

With affordable tuition and a keen eye for the skills needed by our state's businesses, South Carolina's Technical College System continues to be a nationally-recognized model. My budget recommends more than \$7.5 million in non-recurring funds to honor the job-training commitments we have made under the "readySC" program. This would be supplemented by an additional one-time allocation of \$2.5 million for laboratory improvements and the replacement of associated equipment, plus a \$2.5 million increase in General Fund support for the Technical College System's educational offerings.

To more fairly and effectively allocate the state's scarce resources, I have proposed – and will pursue again in the upcoming legislative session – a model of Accountability-Based Funding for higher education. This initiative, which was passed by the Senate in 2012, will ensure that public investments both follow our in-state students and also reward those institutions that offer quality instruction as they help their enrollees graduate on-time, and at a reasonable cost.

Our public colleges and universities are centers of innovation and economic development; I am therefore recommending support for Clemson University's Center for Energy Systems, to build upon their highly respected efforts in this important, job-creating field. This budget also embraces the University of South Carolina's Palmetto College, which makes a high-quality education more accessible for students – such as working professionals and members of the military – who can't attend class on a more traditional schedule. In addition to funding these programs, the Executive Budget recommends that \$24 million from the Capital Reserve Fund be allocated for the deferred maintenance needs of our public higher education institutions, based upon their respective shares of in-state undergraduate students.

The current year's budget made significant investments in law enforcement, especially within the State Law Enforcement Division. The FY 2013-14 Executive Budget recommends additional personnel and equipment for SLED's investigative services, forensics, and information technology units, among others. The budget also calls for 18 new Highway Patrol officers in the Department of Public Safety, plus 10 law enforcement officers in the Department of Natural Resources.

In June, inmates briefly took control of a dormitory at Lee Correctional Institution. Although order was restored within hours, the event underscored the need to better provide for the safety of those who protect us each day. For this reason, my budget recommends that non-recurring funds be used to construct two towers at Lee and to purchase metal detectors, wands, cameras, and other protective equipment for our most dangerous facilities.

The proposed budget also contains funds for new parole agents, to improve offender supervision ratios, along with more staff and improved technology to help us deploy evidence-based practices in our probation and parole system. Recommended increases for the Department of Juvenile Justice would largely replace dried-up funding streams or cash balances that have been depleted. Like many agencies in our criminal justice system that receive a significant portion of their funding from fines, DJJ's revenues have been affected by offenders' lack of resources with which to pay penalties.

More than 1,000 of South Carolina's bridges are structurally deficient; hundreds are in such poor condition that they are now load-restricted. The condition of our infrastructure is deteriorating to the point where it is limiting economic growth. Some have called for a higher gas tax, but I disagree. Instead, let's start by having more of the gas tax we already collect go to our bridges and highways.

Millions of dollars of gas taxes and related fees are currently being diverted to other uses. In this budget, I recommend that the General Fund take on the cost of supporting both the Department of Natural Resources' Water Resources Fund and also the Department of Agriculture's petroleum inspection program. These changes will make \$4.3 million available each year for transportation needs. I am also asking that \$10 million be allocated from the Capital Reserve Fund in the upcoming year, to be distributed using the criteria specified under Act 114.

Although the budget I have proposed funds all essential services within the General Fund revenues projected by the Board of Economic Advisors last month, if the past is any indication, those projections will rise as the budget bill makes its way through the General Assembly. When the BEA does ultimately raise its estimate, I suggest that the legislature pass a bill to eliminate the 6% individual income tax bracket and instead let that income be taxed at the 5% level. This action would reduce future General Fund revenues by roughly \$26 million and would help citizens offset any increases in income or Social Security taxes

that may be coming from Washington next month. After paying for this relief, any additional General Fund revenues should be dedicated to transportation.

Finally, the proposed budget contains more than \$20 million to repay the loan authorized by the Budget and Control Board for costs associated with the data breach at the Department of Revenue. In my Executive Budget last year, I fully funded the remainder of the South Carolina Integrated Tax System project, to replace our outdated systems with a modern one that can process returns more swiftly and provide improved reporting and service at a lower cost. The General Assembly approved a fraction of this request, but those funds ultimately failed to materialize after revenues fell short of the target.

This year, I am again recommending that SCITS be funded out of available non-recurring revenues, along with several other IT security projects in other agencies. These steps will help to secure our electronic systems and records, but as the initial reports on the data breach show, a serious approach to technology requires that we take an enterprise-wide perspective. The inescapable conclusion, as countless good-government advocates and editorial page-writers have observed in the past decade, is that it's time for a Department of Administration.

I respectfully submit the Executive Budget for Fiscal Year 2013-14 and look forward to working with you on this and other important initiatives in the coming year.

My very best,

Nikki R. Haley

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