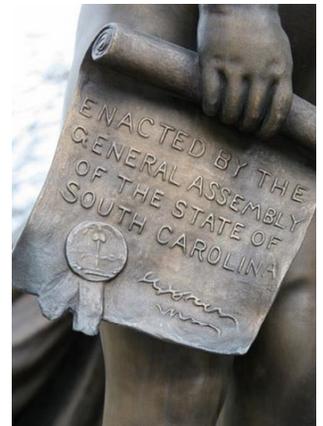


State of South Carolina

Popular Annual Financial Report
For the Year Ended June 30, 2008

Richard Eckstrom, CPA
Comptroller General



A Message from the Comptroller



RICHARD ECKSTROM, CPA
COMPTROLLER GENERAL

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Office of Comptroller General

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NATHAN KAMINSKI, JR., Esq.
CHIEF OF STAFF

January 27, 2009

It is my pleasure to provide this Popular Annual Financial Report ("PAFR") of the State of South Carolina for the fiscal year ended June 30, 2008. This convenient and easy-to-read report is intended to present a simplified, summary view of State government's finances. The State's 252-page Comprehensive Annual Financial Report, also available from my office and on the Internet at www.cg.sc.gov, provides a much more detailed analysis of the State's finances.

During fiscal year 2008, the State faced major fiscal challenges that included ending the year with a \$250 million budgetary deficit. Revenue collections were erratic and declining compared to corresponding collections in fiscal year 2007. In fact, for every month in fiscal year 2008 in which collections exceeded the corresponding monthly collections in fiscal year 2007 (4 months), there were twice as many months (8 months) that came in below. Overall collections in fiscal year 2008 were \$266 million less than they were in fiscal 2007, a decline of 4.0%. While revenue collections declined, unsustainable spending continued to grow as budgetary expenditures increased from \$6.6 billion to \$7.1 billion between fiscal years 2007 and 2008, an increase of 7.6%.

In short, State government continues to suffer through a financial crisis resulting from unsustainable spending and falling revenues. Since the end of fiscal year 2008, revenue collections have continued to decline, already requiring budget cuts four times, totaling \$918.6 million. Because of economic growth in previous years, State government had increased spending to levels it is unable to sustain now that revenues are falling.

As we begin a new legislative session, we look forward to new opportunities for needed change. I urge State leaders to recognize this golden opportunity to rethink the "spend it all" approach and exercise more effective financial discipline. We must all work together to restore the State's fiscal strength and integrity.

Sincerely,

A handwritten signature in cursive script that reads "Richard Eckstrom".

Richard Eckstrom

State Economy

South Carolina has a somewhat diverse economic base, including manufacturing, trade, health care, services, and leisure and hospitality. Businesses have migrated here from around the world to take advantage of the State's reliable labor force, competitive wages, lower-priced land, excellent port facilities, accessibility to markets, and in recent years, substantial tax incentives.

During fiscal year 2008, South Carolina suffered from the national soaring gas prices and stagnant economy but saw a slight increase in job growth with total employment up 4,500 jobs, a gain of less than 1%. The State experienced job losses of 13,900 in construction and 5,000 in manufacturing since June 2007. The strongest employment gains have occurred in the State's service sector which during the past five years has risen from 34% of total employment to 37%. This sector, fueled by the tourism, educational, and healthcare industries has contributed to a more diversified overall employment base and improved income levels. During fiscal year 2008, average hourly



Photograph by Deborah Farr

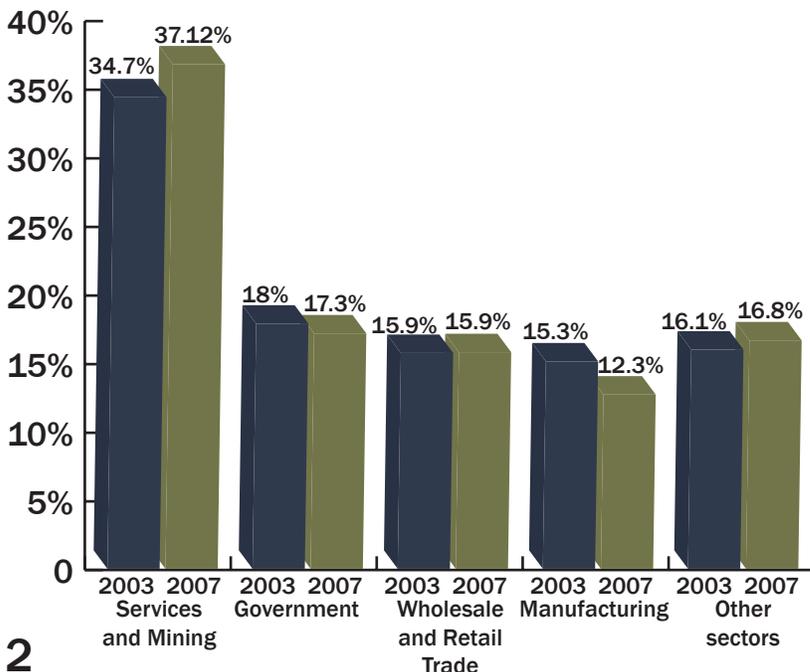
Scientist at the Department of Health and Environmental Control.

earnings increased by 3.4% and average weekly earnings rose by 2.8%.

Although the State experienced financial downfalls during fiscal year 2008, industry recruitment and job creation in South Carolina reached a record high. The South Carolina Department of Commerce was involved in recruiting more than 15,000 jobs and over \$4 billion in new capital investment to the State in calendar year 2007. This produced high job creation levels in non-urban areas (more than one-third of total jobs were created in rural areas), new companies choosing to invest heavily in South Carolina, and diversity in investments. During calendar year 2007, the State saw many new companies decide to locate in South Carolina and existing businesses commit to expand operations in the State.

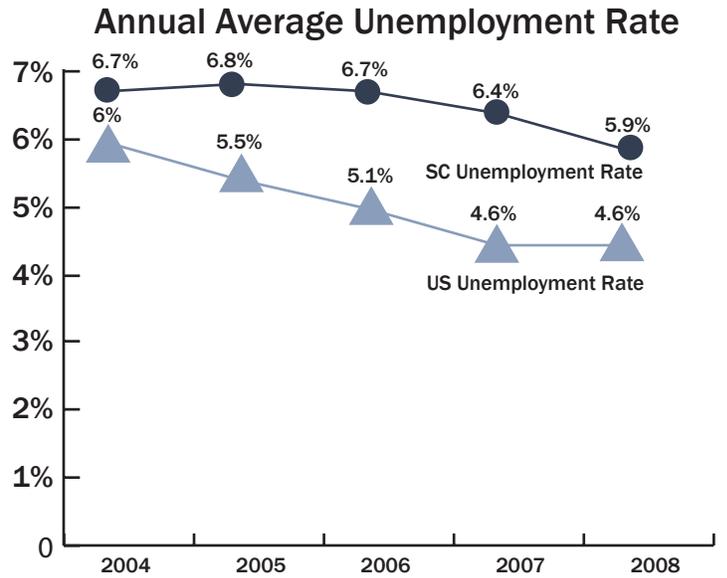
Additional capital investments and job growth have not been enough to keep pace with State government spending. Furthermore, State revenues have continued to decline in fiscal year 2009 and our national economy is being battered by the most severe financial crisis in decades. As a result, the State has already had to cut its fiscal year 2009 budget four times, as discussed in the Future Economic Challenges section on page 15 of this report.

SC Economic Sectors Comparison

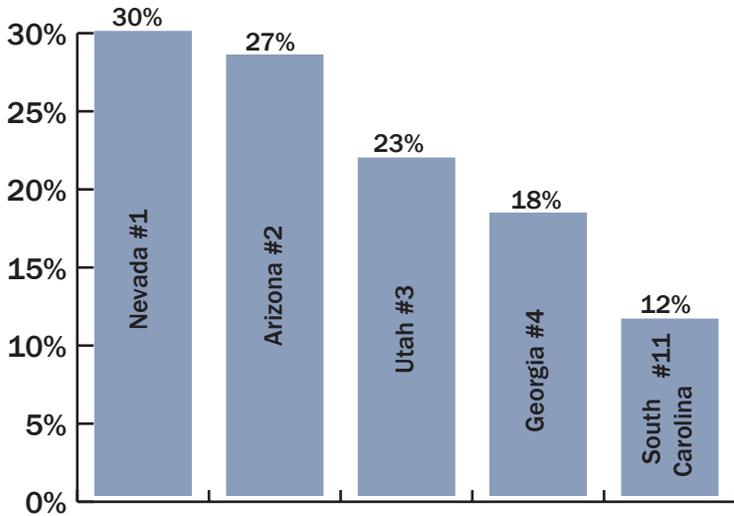


State Economy

Although the State's average unemployment rate for calendar year 2007 of 5.9% was higher than the national average rate of 4.6%, the State's economy has continued to generate jobs. During calendar year 2007, the jobless rate fell a half a percent from calendar year 2006. However, the State's unemployment rate for November 2008 has increased to 8.4% based on recent turbulence in the national economy.



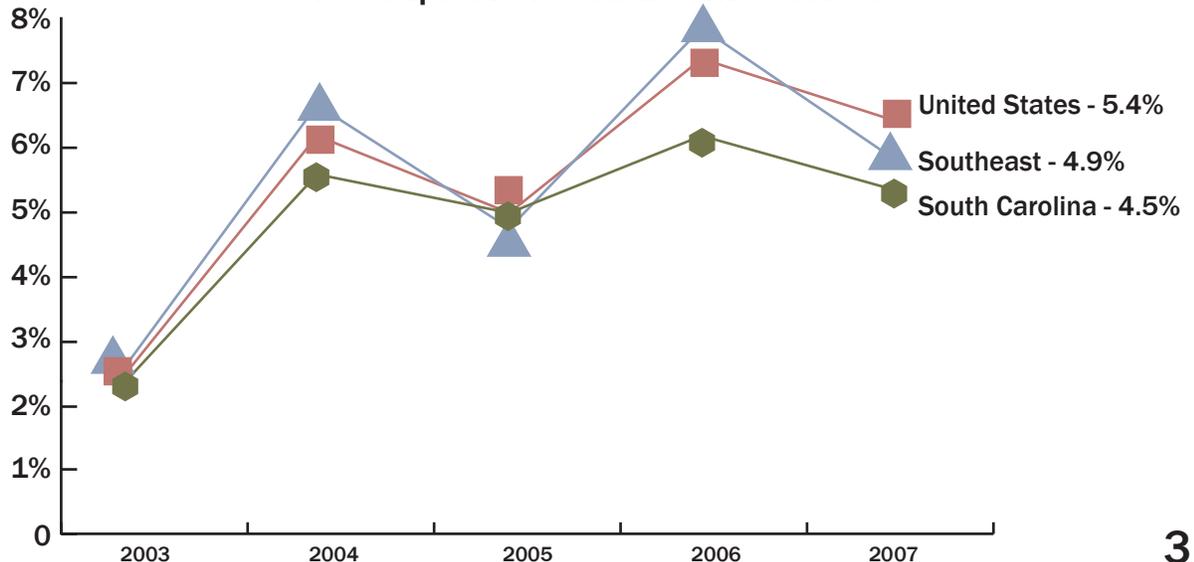
Population Growth Rankings



South Carolina's population at July 1, 2008, was 4.5 million. The State's rate of population growth is presently the eleventh fastest in the nation. The population is predicted to reach 5.6 million by 2035. Since Census 2000, South Carolina's population has increased by 468 thousand, or 12%.

South Carolina's per capita income for 2007 (most recent year available) increased to \$31,013, or 4.5% over 2006. 2007's increase was less than the national and southeastern states growth rates.

Per Capita Personal Income Growth



Financial Highlights

Government-wide Financials

The State of South Carolina's government-wide financial statements present a long-term view of the State's finances as a whole, using accrual basis accounting – the same accounting methods that most businesses use.

The government-wide statements present three different kinds of activities:

Governmental activities: Most of the State's basic services are included here, such as general government, education, health and environment, social services, administration of justice, and transportation. Taxes (primarily income and sales taxes) and federal grants finance most of these services.

Business-type activities: These activities usually recover all, or a significant portion, of the costs of their services or goods by charging fees to customers. Higher education (State-supported colleges and universities), unemployment compensation benefits, financing of housing facilities, and financing of student loans are the most significant of South Carolina's business-type activities.

Component units: Although component units are legally separate from the State, the State's elected officials are financially accountable for them. The Public Service Authority (Santee-Cooper, an electric utility company), the State Ports Authority, the Connector 2000 Association, Inc. (which operates the Southern Connector, a toll road), and the Lottery

Commission are the State's major component units.

To simplify the financial information provided below, component unit information is not included. You can obtain financial information for component units from the State's Comprehensive Annual Financial Report (CAFR) which can be obtained on the Comptroller General's Office website at www.cg.sc.gov.

The most significant changes (increases and decreases) in net assets occurred within current and other assets and current and long-term liabilities of governmental activities:

- \$ \$872.9 million decrease in cash due to increased spending, decreased collections as a result of elimination of certain taxes, and a bond defeasance.
- \$ \$168.4 million increase in accounts payable and \$185.3 million increase in intergovernmental payables due in part to timing of payments in the current and prior years. The increase in intergovernmental payables included \$56.7 million of sales tax revenues owed to counties. The newly established Homestead Exemption Fund provides property tax relief through an additional 1% sales tax.
- \$ The decrease in long-term liabilities included a \$549.9 million reduction in Tobacco Authority bonds payable resulting from a bond defeasance. In addition, the State did not issue general obligation debt during the year, while it continued to pay off previously issued bonds.

Capital assets of governmental and business-type activities also increased significantly by \$318.7 million and \$438.6 million, respectively. Additional information can be found in the Capital Assets section of this report on page 6.



The most significant changes in revenues and expenses were in governmental activities:

- \$ Operating grants and contributions increased by \$465.2 million primarily due to improved funding of public health and social services programs.

- \$ General tax revenues increased

	Governmental Activities		Business-type Activities	
	2008	2007	2008	2007
Assets				
Current and other assets.....	\$ 8,905	\$ 9,771	\$ 5,362	\$ 5,241
Capital assets.....	13,712	13,393	3,978	3,539
Total assets.....	22,617	23,164	9,340	8,780
Liabilities				
Current liabilities.....	4,681	4,123	1,002	887
Long-term liabilities.....	4,493	5,233	3,980	3,759
Total liabilities.....	9,174	9,356	4,982	4,646
Net Assets				
Invested in capital assets, net of debt.....	10,008	9,706	2,315	2,134
Restricted.....	3,597	3,498	1,387	1,406
Unrestricted.....	(162)	604	656	594
Total net assets.....	\$ 13,443	\$ 13,808	\$ 4,358	\$ 4,134

Financial Highlights

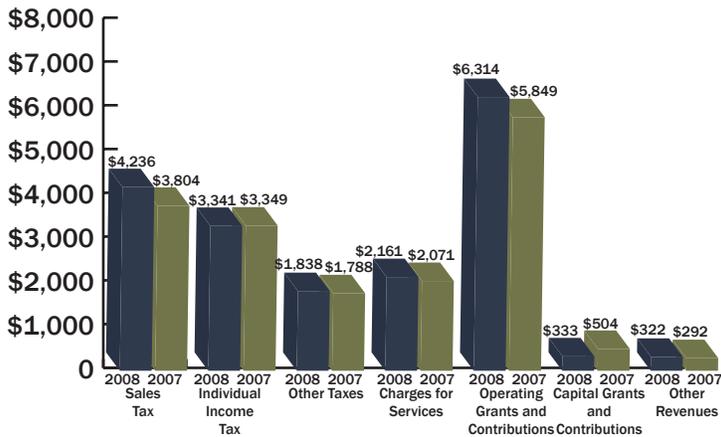
\$474.5 million over last year. Sales and use tax increased primarily due to the new property tax exemption program and additional accommodations and local option sales taxes.

General government expenses increased \$1.1 billion due in part to the increase of outflows to the new Homestead Exemption Act program, as well as

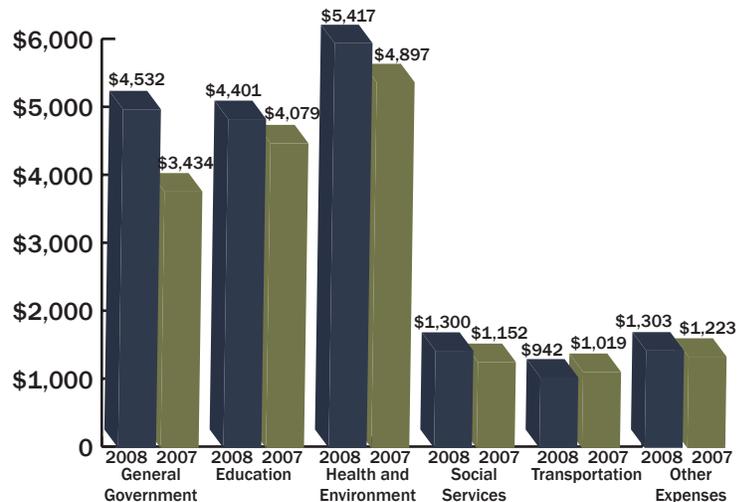
increased distributions of accommodations and local option sales taxes to participating counties.

Expenses for education increased \$322.2 million because of spending for early childhood programs for at-risk students, school bus replacement, and increased funding over prior year levels for other educational programs.

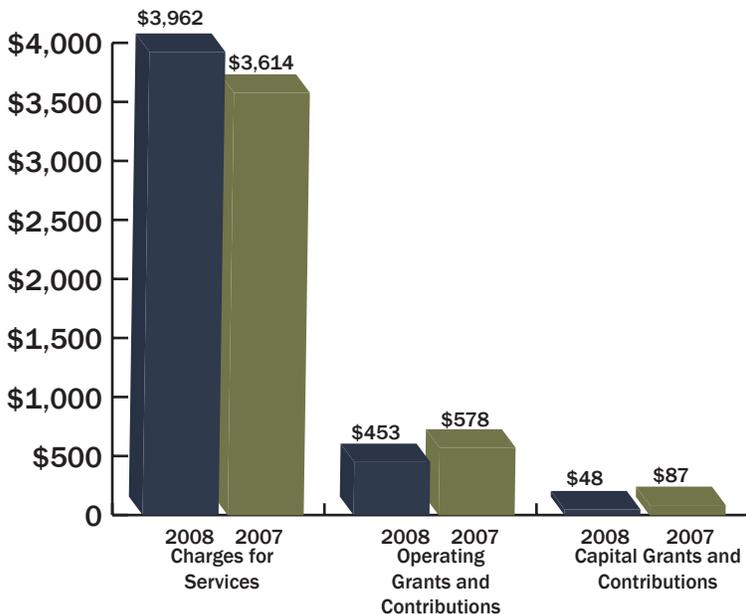
Governmental Activities – Revenues
Fiscal Years 2007 and 2008
(in millions)



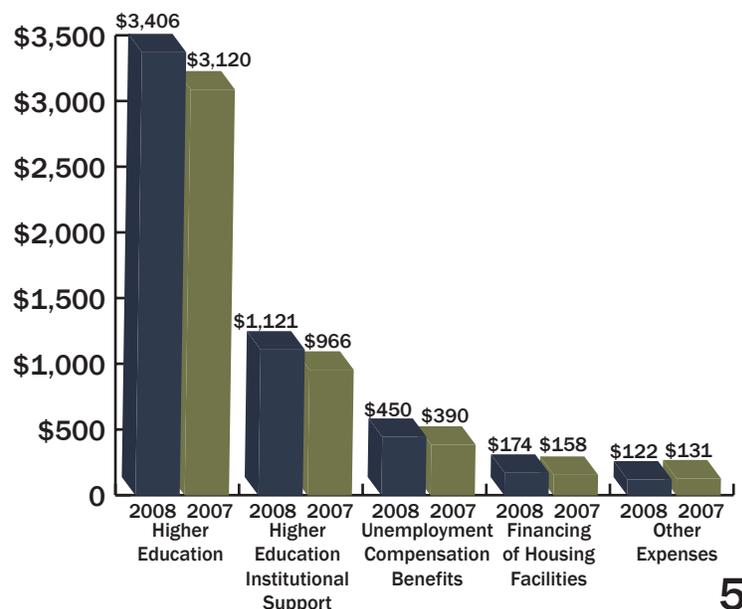
Governmental Activities – Expenses
Fiscal Years 2007 and 2008
(in millions)



Business-type Activities – Revenues
Fiscal Years 2007 and 2008
(in millions)



Business-type Activities – Expenses
Fiscal Years 2007 and 2008
(in millions)



Capital Assets



Dreher Island State Park.

At the end of fiscal year 2008, the State had \$17.7 billion invested in capital assets. This represented a net increase (including additions and deductions) of \$757.3 million, or 4.5%, over the previous fiscal year.

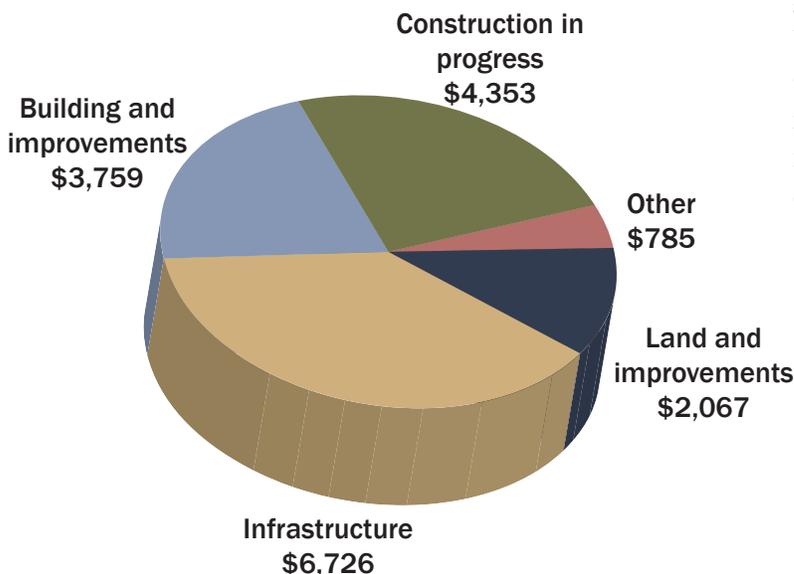
The State's investment in buildings and improvements increased significantly, primarily because of public colleges and universities expanding their campus facilities. The Medical University of South Carolina completed a cancer center expansion while MUSC Hospital Authority completed the first phase of replacement of its current patient care facilities.

The College of Charleston added a new campus building, residence hall, and athletic facility.

State vehicles increased significantly due to the Department of Education increasing its bus fleet by 530 vehicles and the Budget and Control Board upgrading the state fleet by 773 vehicles.

As in prior years, machinery and equipment increased significantly due, in large part, to acquisitions by public universities. Clemson University, The Medical University of South Carolina, and the University of South Carolina all made significant investments in computing, testing, medical, scientific, and laboratory equipment and equipping newly-established facilities.

**Primary Government Capital Assets
Net of Depreciation as of June 30, 2008
(in millions)**



Significant Increases in Capital Assets

- Fleet vehicles - 773
- School buses - 530
- Highway patrol vehicles - 798
- Higher education buildings - 12

Long-term Debt

South Carolina issues various types of general obligation debt including capital improvement bonds, highway bonds, school facilities bonds, higher education institution facilities bonds, and economic development bonds. General obligation bonds are backed by the full faith, credit, and taxing power of the State. Additionally, South Carolina issues revenue bonds, which are not backed by the full faith, credit, and taxing power of the State. Instead, the State pledges certain revenue streams for repaying this type of debt.

At June 30, 2008, the State had \$8.1 billion in total bonds and notes outstanding—a decrease of \$434.1 million, or 5.1%, over last year. Expressed in relation to the State’s population, the share of the State’s general obligation debt per capita at June 30, 2008 was \$528.

The reduction in debt reported in governmental activities resulted primarily from the defeasance of \$575.2 million of Tobacco Authority revenue bonds. The Tobacco Settlement Revenue Management Authority defeased the bonds with a portion of the proceeds of \$275.7 million in Tobacco Settlement Revenue Asset-Backed Refunding Bonds, along with funds transferred from the Tobacco Settlement Fund.

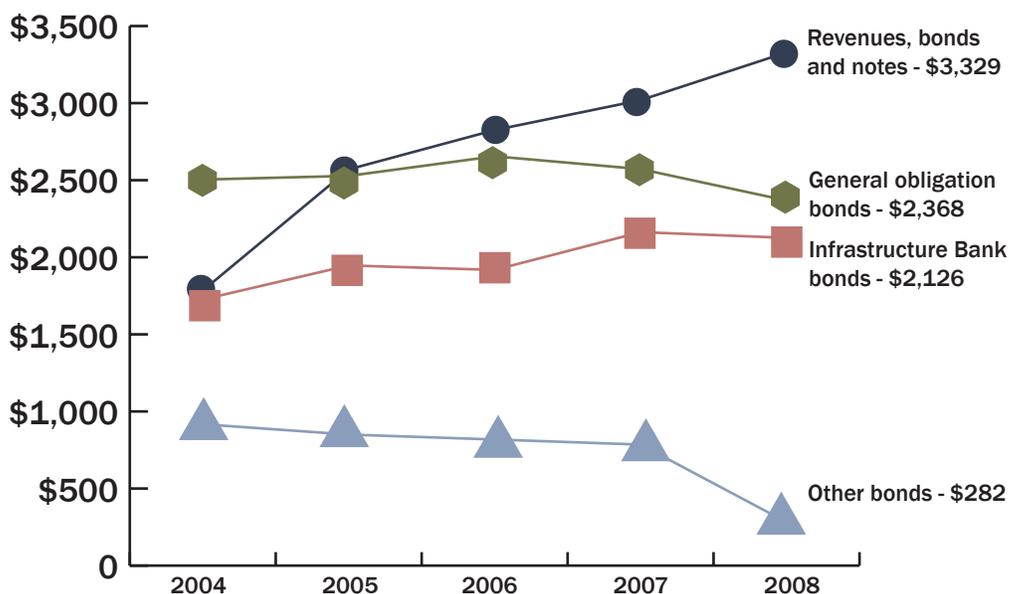
New debt reported in business-type activities resulted mainly from the issuance of revenue bonds by

the enterprise funds. The Housing Authority issued \$103.0 million in bonds for housing programs, the Education Assistance Authority issued \$131.7 million in bonds to provide financing for student loans, and the College of Charleston and the University of South Carolina issued \$95.9 million and \$94.2 million, respectively, in facilities revenue bonds. In addition, the Medical University of South Carolina drew down \$48.8 million on a note payable to finance the acquisition of equipment for a new hospital facility and issued \$30.0 million in short-term general obligation bond anticipation notes. The Housing Authority entered into a \$50.0 million mortgage revenue note payable.

National bond rating services assign ratings to bonds that the State backs with its own taxing authority (general obligation bonds). Fitch Ratings has rated these bonds as “AAA” and Moody’s Investors Service has rated them as “Aaa”, the highest ratings that these services assign. Standard & Poor’s has rated these same bonds as “AA+”.

To limit the overall amount of general obligation debt that can be issued, the State limits the amount of annual payments for principal and interest on general obligation debt. At June 30, 2008, the State had not reached its legal debt limits.

Primary Government Bonds and Notes Outstanding
Fiscal Year End Balances
(in millions)



General Fund Highlights



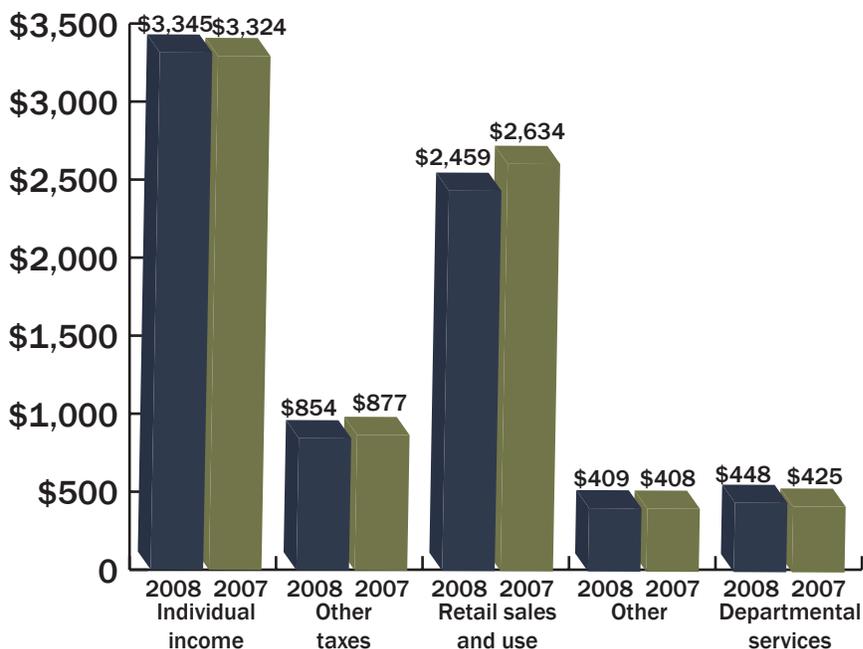
Golfer at Harbour Town Golf Links on Hilton Head Island.

The State's primary operating fund (or set of accounts) is called the General Fund. This fund includes resources that pay for the services that the State traditionally provides to its citizens. These resources, such as taxes, are accounted for in the General Fund unless State law requires them to be accounted for in another fund.

During fiscal year 2008, the net fund balance of the General Fund decreased \$828.9 million (75.8%) from the previous year. General Fund revenues declined overall by \$152.1 million (2.0%) due to significant decreases in sales and use tax collections coupled with smaller decreases in corporate taxes and increases in individual income taxes and interest earnings as presented below.

- Individual income taxes increased \$21.3 million (0.6%);
- Sales and use taxes decreased \$174.8 million (6.6%);
- Corporate and other taxes decreased \$22.6 million (2.5%);
- Interest earnings increased \$18.1 million (13.9%).

General Fund Revenues
Fiscal Year 2008 compared to 2007
(in millions)



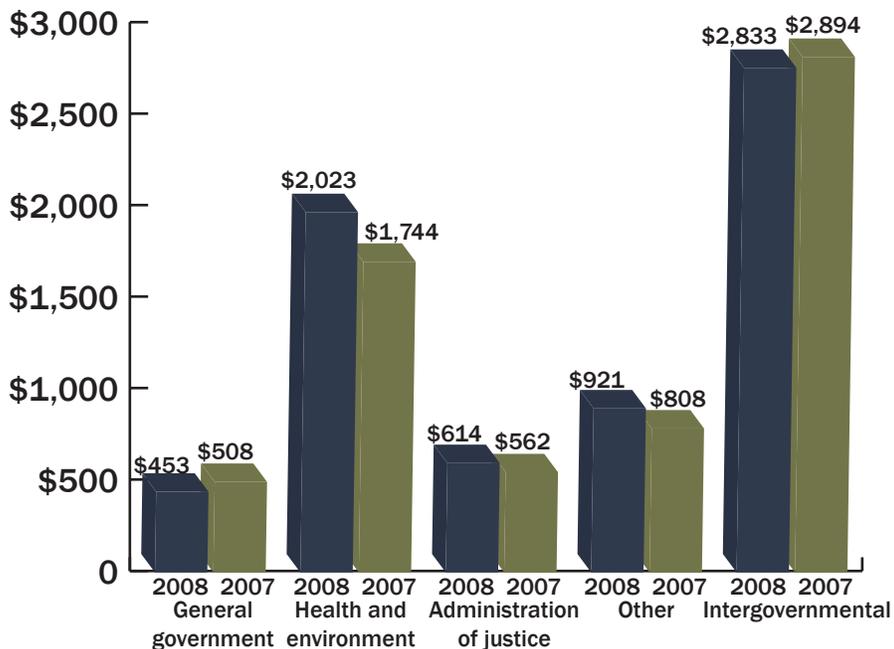
General Fund Highlights

General Fund expenditures increased \$327.9 million (5.0%) from last year. The most significant expenditure increase was attributable to Health and environment, which increased \$278.7 million (16.0%). Also contributing to the overall reduction of the total fund balance were increased operating transfers out of the General Fund in the amount of \$309.5 million (25.8%). This increase was attributable in part to transfers of tax revenues to the Homestead Exemption Fund for subsequent distribution for property tax relief.



Steeplechase races at Springdale Race Course in Camden are a national-level equestrian event.

General Fund Expenditures Fiscal Year 2008 compared to 2007 (in millions)



The “Rainy Day Account”

At June 30, 2008, the General Reserve Fund, sometimes called the “rainy day account”, contained \$95.1 million, which is \$91.7 million below the full funding requirement. The State’s Constitution requires restoration of the reserve to a level defined by formula within three years after a withdrawal. State law defines full funding for the reserve as 3% of the Budgetary General Fund’s revenues for the latest completed accounting year. The 2007-2008 Appropriations Act provided \$19.1 million to fully fund the rainy day account, however, \$91.7 million was drawn out to cover the 2007-2008 Budgetary General Fund deficit.

Operating Indicators

Significant Operating Indicators By Selected Function

	2007	2008
General government		
Individual income tax returns processed	2,273,202	2,421,786
Corporate income tax returns processed	164,855	166,237
Department of Motor Vehicles transactions	13,331,078	13,234,198
Education		
Public school enrollment	698,290	701,749
Average operating miles per school bus	16,000	15,651
Health and environment		
Medicaid eligible participants	902,308	669,507
Women, Infant and Children (WIC) program participants	112,467	124,033
Community mental health center clients	87,641	87,762
Social services		
Average food stamp households served per month	231,053	248,314
Child Protective Services investigations	18,168	18,553
Transportation		
Miles of surface repair	167,551	158,512
Miles of roadway inspections	332,559	342,981
Administration of justice		
Adult prison average daily population	23,437	23,958
Juvenile facility average daily population	985	910
Resources and economic development		
Department of Commerce capital investment projects	\$2.99 billion	\$4.05 billion
Higher education and higher education institution support		
Total headcount enrollment	176,415	180,479
Degrees awarded	26,063	26,237
Unemployment compensation benefits		
Initial claims	304,464	292,661
Financing of housing facilities		
Mortgage loans managed	15,815	17,734
Families receiving rental assistance	20,129	20,100

State Government Employees

Governmental Activities - 43,101
Business-type Activities - 27,285

State Ten Largest Employers

Bi-Lo, Inc.
Blue Cross/Blue Shield of South Carolina
Greenville County School District
Greenville Hospital System
Palmetto Health Alliance, Inc.
University of South Carolina
U.S. Department of Defense
U.S. Postal Service
Wal-Mart Associates, Inc.
Washington Savannah River Company

Agency Highlights

The following pages highlight eight of South Carolina's State agencies. These agencies receive the largest level of State appropriated funding, and as a result are the agencies hardest hit by the recent budget crisis. While all these agencies are operating with budget constraints, each managed to achieve important goals during the fiscal year.

Department of Education

The South Carolina Department of Education's (DOE) mission is to provide leadership and services to ensure a system of public education through which all students will become educated, responsible, and contributing citizens. South Carolina's schools face significant challenges in improving education, the greatest challenge being adequate funding, equitably distributed across school districts. Legislation that replaced locally generated property taxes with an additional state sales tax continues to create funding constraints, particularly in high-growth districts. The poorest districts struggle to meet the needs of students disadvantaged by poverty. Existing difficulties are worsened by shortfalls in state tax revenues.

Despite the funding challenges, DOE made numerous achievements during fiscal year 2008. South Carolina continues to grow in number of students

and schools, with 701,544 students enrolled in K-12 grades in 1,161 schools during 2008. The number of teachers earning certification by the National Board for Professional Teaching Standards continues to increase significantly each year. The number of certified teachers is now up to 5,770 in 2008. South Carolina has emerged as a leader in single-gender education with expanded curriculum choices within public schools. Nearly 250 South Carolina schools, more than any other state in the nation, are offering single-gender options during the 2008-09 school year, up from 70 at the start of the last school year. DOE completed the second year of its two-year Child Development Education Pilot Program (CDEPP), which provided full-day four-year-old pre-kindergarten programs for at-risk children in 37 districts.

Department of Health and Human Services

The mission of the South Carolina Department of Health and Human Services (DHHS) is to provide the best healthcare value for South Carolinians in need. South Carolina's Medicaid program, through a network of close to 30,000 healthcare professionals, provides healthcare services for approximately one million residents annually who are either poor, elderly, or disabled. DHHS has the important job of ensuring the State gets the best possible return on its healthcare investment by identifying and confronting the fundamental inefficiencies that drive up costs and hold down quality.

Some recent efforts to achieve the mission of the agency include implementation of Healthy Connections Kids (SCHIP), which allows coverage of uninsured children whose annual family income

does not exceed 200% of the federal poverty level; establishment of the South Carolina Health Information Exchange (SCHIE_x), which is a free, secure web-based platform that will give doctors a complete history of drugs and procedures paid for by Medicaid over the past decade to better help them diagnose diseases, adjust treatment methods, and educate patients on healthy lifestyles; and taking the initiative to be the first state in the nation to offer Health Opportunity Accounts (HOA's), which encourage preventive medical care, while discouraging unnecessary visits to the emergency room in that preventive care visits to the doctor are not deducted from the HOA while unnecessary emergency room visits merit a deduction.

Agency Highlights

Department of Corrections

The Department of Corrections (DOC) has twenty-eight institutions categorized into four distinct security levels: high security, medium security, minimum security, and community-based pre-release/work centers. Inmates are assigned to institutions according to their specific security, programming, medical, educational, and work requirements.

For fiscal year 2008, DOC operated at a deficit of \$3.9 million. Increased costs of food, utilities, transportation, and medical services coupled with a steadily increasing inmate population made it impossible to operate within the appropriated level of funding from the State. Despite these difficulties,

DOC took a proactive approach to identify cost savings by restructuring the internal education system for a savings of \$796 thousand; restructuring Prison Industries for an annual savings of \$400 thousand; reducing the time inmates spend in the Reception and Evaluation (R&E) facility for medical evaluation; implementing a system-wide smoke-free environment (employees and inmates) to minimize long-term health problems related to tobacco smoking and the related health costs; and designing successful safety programs that have contributed to further reductions in Workers' Compensation claims and premium rates.

Department of Mental Health

The mission of the South Carolina Department of Mental Health (DMH) is to support the recovery of people with mental illnesses and emotional disorders. DMH emphasizes respect for the individual, support for local care, and dedication to improved public awareness and knowledge. During the past fiscal year, DMH took a major initiative to increase public awareness about mental health issues by making presentations to civic clubs and other audiences around the State, driving home the key message about mental illnesses and how DMH strives to deliver quality

services efficiently and effectively. Other achievements included delivering services in the public school system with 282 school-based mental health counselors serving about 13,000 children, with increased service capability through a \$1.2 million grant from the Blue Cross Blue Shield of South Carolina Foundation; continuing to help people with mental illnesses find jobs and places to live; and solving the problem of people with mental illnesses coming to local hospital emergency rooms for treatment by providing more crisis and other services in the community mental health centers.

Department of Disabilities and Special Needs

The South Carolina Department of Disabilities and Special Needs (DDSN) has authority over all the State's services and programs for South Carolinians with severe lifelong disabilities, including mental retardation and related disabilities, autism, traumatic brain injury, and spinal cord injury and similar disabilities. DDSN currently serves over 29,000 people with mental retardation and related disabilities, autism, head injury, and spinal cord injury. Approximately 82% of those individuals live at home with their families, while the remaining 18% require 24-hour care provided

in community residential settings or in one of five state operated regional centers. As of June 30, 2008, DDSN has developed 449 new beds for individuals in need of residential services through new State funds appropriated in fiscal years 2006 and 2007. DDSN also expanded its in-home individual and family support services through new State funds as well as natural attrition, prioritizing the needs of individuals, improving the use of Medicaid reimbursements, and reducing administration.

Agency Highlights

Department of Health and Environmental Control

The South Carolina Department of Health and Environmental Control (DHEC) is charged with protecting the State's public health and the environment. DHEC is organized to serve the public under four broad areas: Environmental Quality Control, Health Services, Health Regulations, and Ocean and Coastal Resource Management.

Despite dealing with budget cuts, DHEC has made numerous achievements during the past fiscal year, a few of which include receiving the highest possible

ratings in all categories in a review by the U.S. Nuclear Regulatory Commission; implementing a five-year "Shoreline Change Initiative" in an effort to deal with shoreline erosion and sea level rise; holding "World Café" meetings with the public to solicit suggestions on how the agency can better interact with and engage the public in environmental issues; putting into place new solid waste program regulations; and partnering with the Department of Education to reduce diesel emissions from the State's aging fleet of school buses.

Department of Social Services

The mission of the Department of Social Services (DSS) is to ensure the health and safety of children and adults who cannot protect themselves and to assist families to achieve stability through food assistance, child support, and temporary benefits while transitioning into employment. Major programs administered by the agency include Child Welfare, Adult Protection, Child Support Enforcement, Family Nutrition, Child Care Services, and Temporary Assistance for Needy Families.

Like most agencies, DSS has seen its base budget reduced in recent years. Despite financial hardships,

the agency has been successful by achieving more than 500 finalized adoptions during fiscal year 2008, compared to averaging about 400 in the last five years; being recognized by the federal government for its innovative marketing campaign for its foster care recruitment program; selection by the National Governor's Association to participate with six states in a study designed to reduce the number of children coming into foster care; and placing clients into more than 11,500 jobs paying an average of almost \$8 per hour through the Family Independence Program.

Department of Juvenile Justice

The Department of Juvenile Justice (DJJ) administers South Carolina's juvenile justice system at the State and local levels. The mission of the agency is to protect the public while reclaiming juveniles through prevention, community programs, education, and rehabilitative services in the least restrictive environment. The agency administers an array of programs and services ranging from diversionary, early intervention, supervision, and specialized treatment in secure facilities.

During the fiscal year, DJJ completed construction of the Community Connections Center, a 10,000

square foot visitation and activity building for the Broad River Road complex funded entirely by private donations; completed the Girls Transition Home, which provides a home-like setting where females can master independent living skills; and replaced of dormitories for male residents that are designed to promote best practice behavior management, juvenile and staff safety, and treatment services. The agency's school district was named "Palmetto Gold" for the 6th year in a row, and its Birchwood School maintains accreditation through the Southern Association of Colleges and Schools.

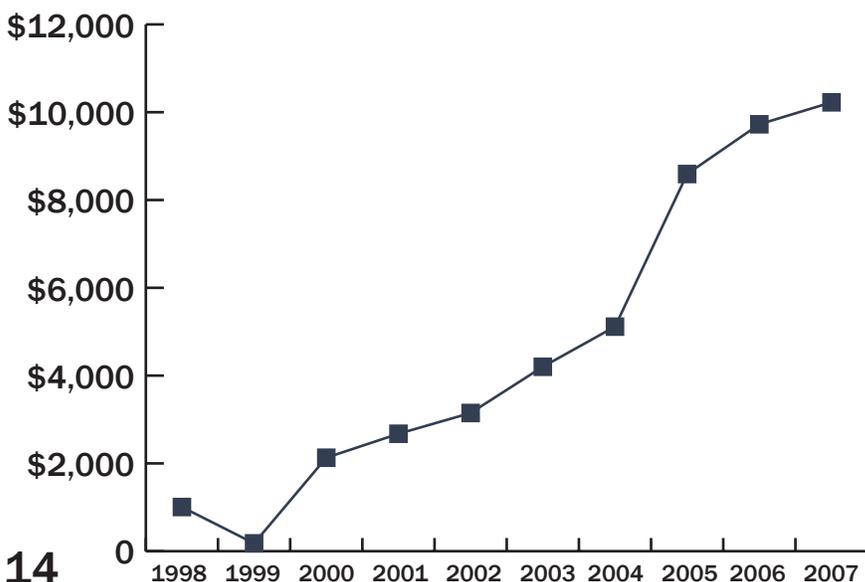
Retirement Plans and OPEB

State Retirement System — The South Carolina Retirement Systems is comprised of five defined benefit pension plans:

- *South Carolina Retirement System (SCRS)* – Covers state and municipal employees as well as public school districts;
- *Police Officers Retirement System (PORS)* – Covers state and local law enforcement personnel and firefighters;
- *The Retirement System for Members of the General Assembly (GARS)* – Covers members of the South Carolina General Assembly;
- *The Retirement System for Judges and Solicitors (JSRS)* – Covers judges, solicitors, and circuit public defenders; and
- *National Guard Retirement System (NGPS)* – Covers members of the South Carolina National Guard.

The General Assembly approved a plan (Act 311 of 2008) to provide state retirees an annual cost of living adjustment (COLA) of up to 2% and to accumulate money to cover these costs. This replaces the previous plan that provided retirees “ad hoc” COLA’s which were unfunded and were seriously eroding the economic health of the State Retirement System.

**Unfunded Accrued Liability
South Carolina Retirement System
(in Millions)**



The new plan provides an opportunity to reduce the Retirement System’s \$10.2 billion unfunded liability (similar to a 30 year mortgage that the State must pay) while still providing state retirees annual COLA’s.

Retirees’ Health Insurance — In accordance with new rules by the Governmental Accounting Standards Board to account for public employee health insurance benefits, effective May 1, 2008, the General Assembly established the South Carolina Retiree Health Insurance Trust Fund to accumulate sufficient funds to provide disability benefits and to provide post-employment health insurance benefits for retired State and school district employees. The Trust Fund received contributions of \$348.8 million, which included a transfer of \$248.7 million from the Employee Insurance Program reserves, along with \$63.5 million in State appropriations and \$36.6 million in employer contributions. The total contributions of \$348.8 million represent approximately 50% of the actuarially determined annual required contribution of \$692.7 million. These contributions also represent a reduction of the June 30, 2007 Unfunded Actuarial Accrued Liability of \$8.6 billion.

Long-term Disability Insurance—The General Assembly also established the Long-Term Disability Insurance Trust Fund, effective May 1, 2008, to accumulate sufficient funds to provide disability benefits for state employees, school district employees, and employees of participating local government entities. The Trust received contributions of \$28.6 million, which included a transfer of \$27.5 million from the Employee Insurance Program reserves and employer contributions of \$1.1 million. The total contributions represented 285% of the actuarially determined annual required contribution of \$10.0 million. The Actuarial Accrued Liability of \$28.0 million is nearly 100% funded.

Future Economic Challenges

South Carolina's current financial crisis is driven by both the State's tax policies and the national recession. The new fiscal year (FY09) has brought with it many challenges for maintaining a well-balanced budget. State officials forecasted that revenue collections would improve during the year and accordingly the spending budget was increased to \$7.2 billion, 5.0% over the FY08 final adjusted amount. However, sharply declining revenue collections have caused revenue projections to be adjusted downward four times totaling a decrease of \$918.6 million.

For the first six months of FY09, revenue collections have not met the expectations of anticipated growth. Overall, revenue collections are 4.9% below the prior year. Sales taxes and individual income taxes, the State's top two sources of revenue, have declined 8.7% and 2.5%, respectively, when compared to the same period last fiscal year. Because of the sagging tax collections and the expectation of climbing unemployment, the Budget and Control Board has ordered an immediate 7% (more than \$400 million) reduction in addition to the prior month's legislative action that trimmed \$488 million from the original budget passed for FY09.

The legislative action has created difficult financial burdens on State agencies, which have had to reduce spending through hiring freezes, eliminating positions, mandating employee furloughs, reducing travel, and other cost-saving methods. Coupled with the additional 7% reduction, State agencies will more than likely now have to further curtail services and broaden their reduction of employee payroll through lay-off and extended furlough programs. In addition, the State



Bennett's Point Road (SC 26), which intersects US 17 just south of the Ashepoo bridge.

Budget Office has requested agency budget writers to project a 15% budget spending cut to their 2009-10 budgets submitted to the legislature.

As one of the hardest hit agencies, the Department of Corrections (DOC) is projected to incur a budgetary deficit at the end of the year. DOC ended FY08 with an approximate \$4 million budgetary deficit. Current projections show that DOC is operating at a \$14.5 million deficit. Operating expenses including medical, food, and energy will continue to be impacted throughout the year by inflation possibly creating additional deficit spending. To offset some of the increases, DOC has taken steps to curtail spending and increase revenue through various initiatives such as increasing inmate medical co-pays to \$2 per incident, reducing free postage to indigent inmates, and raising canteen prices by 5%.

Based on these challenges and a continued bleak outlook for the rest of the year, State leaders need to work together to produce comprehensive solutions to restore the State's fiscal strength and integrity.

Outstanding Achievement Award

The Government Finance Officers Association of the United States and Canada (GFOA) has given an Award for Outstanding Achievement in Popular Annual Financial Reporting to the State of South Carolina for its Popular Annual Financial Report for the fiscal year ended June 30, 2007. The Award of Outstanding Achievement in Popular Annual Financial Reporting is a prestigious national award recognizing conformance with the highest standards for preparation of state and local government popular reports.

In order to receive an Award for Outstanding Achievement in Popular Annual Financial Reporting, a government unit must publish a Popular Annual Financial Report, the contents of which conform to program standards of creativity, presentation, understandability, and reader appeal.

An Award for Outstanding Achievement in Popular Annual Financial Reporting is valid for a period of one year only. We believe our current report continues to conform to the Popular Annual Financial Reporting requirements, and we are submitting it to the GFOA.

Sources and Acknowledgements

This report presents financial information using accounting principles generally accepted in the United States of America (GAAP). GAAP financial information is presented in a standardized manner that is comparable to that of other governmental entities. This report includes selected financial information for major funds, including the State's General Fund. It does not contain information for all funds, activities or component units as reported in the State's Comprehensive Annual Financial Report (CAFR). However, most of the information contained in this report is derived from the CAFR, produced by the Comptroller General's Office and independently audited. A more detailed and complete presentation of the State's GAAP financial information is presented in the CAFR.

The following sources were used to compile this report: South Carolina state agencies, US Census Bureau, and US Bureau of Labor Statistics. Photographs by SouthCarolinaParks.com, Sciway.net and Deborah Farr.

Award for Outstanding Achievement in Popular Annual Financial Reporting

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June 30, 2007

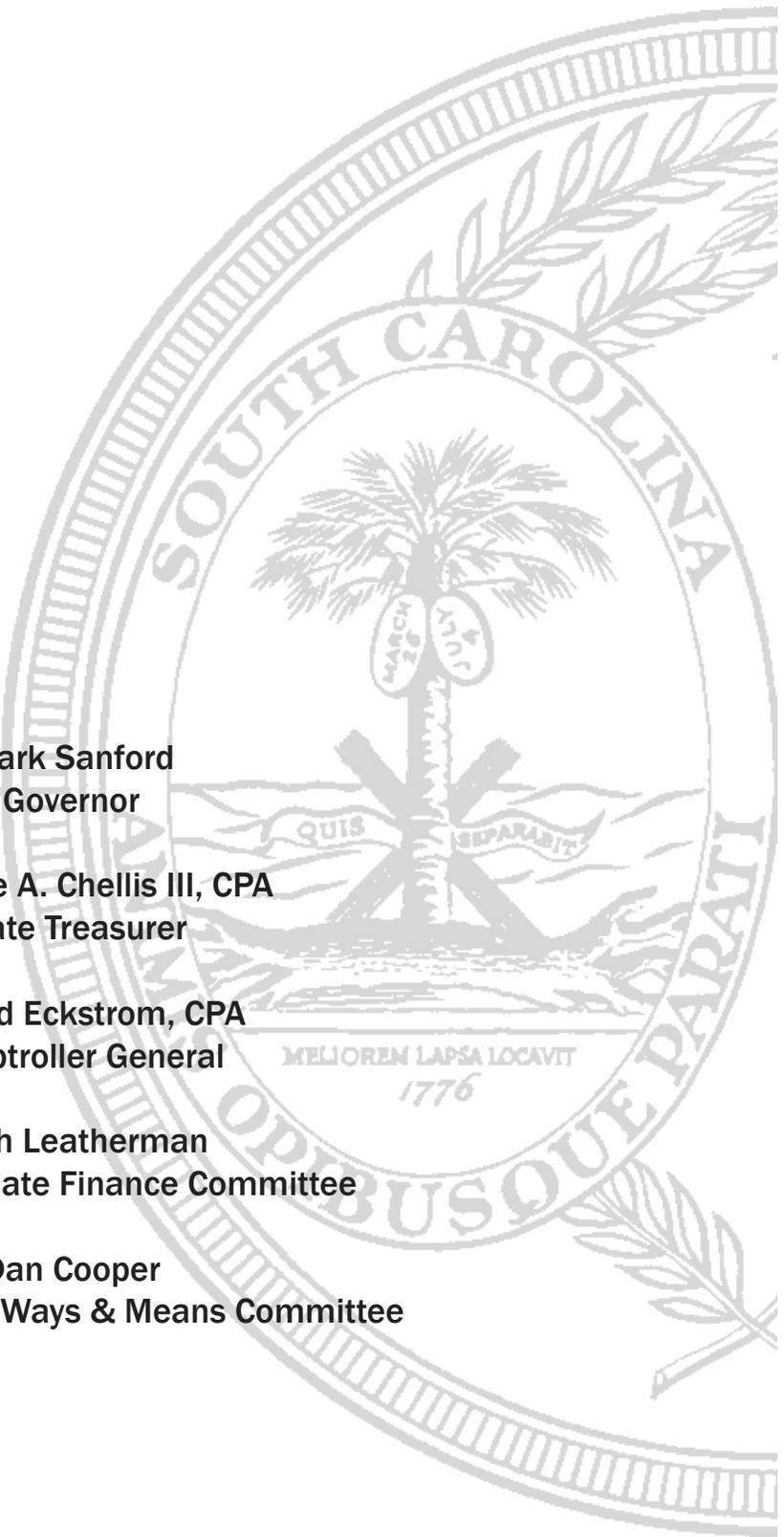


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The seal of the State of South Carolina is a large, faint watermark in the background. It features a central palmetto tree with two coconuts hanging from its trunk. The coconuts are inscribed with the dates 'MARCH 20' and 'JULY 4'. A banner draped across the base of the tree reads 'QUI PRO SEPARABIT'. Below the tree, the Latin motto 'MELIOREM LAPSA LOCAVIT' and the year '1776' are visible. The entire seal is encircled by the text 'SOUTH CAROLINA' at the top and 'ANNO DOMINI MDCCLXXVI' at the bottom, with a laurel wreath on the right side.

Mark Sanford
Governor

Converse A. Chellis III, CPA
State Treasurer

Richard Eckstrom, CPA
Comptroller General

Hugh Leatherman
Chairman Senate Finance Committee

Dan Cooper
Chairman House Ways & Means Committee