



State of South Carolina
Office of Comptroller General

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November 12, 2008

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

I am pleased 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, 2008. The report provides financial information about the State's operations during the year and describes its financial position at the end of the year. 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 that we recently received for our report as of June 30, 2007; a list of State officials; and an organizational chart of State government.
- The Financial Section, including the report of the independent auditors, management's discussion and analysis, government-wide financial statements, fund financial statements, required supplementary information, other combining financial statements, and schedules.
- The Statistical Section, presenting comparative financial data and other non-financial data.

Management assumes full responsibility for the completeness and reliability of the information contained in this report, based upon a comprehensive framework of internal controls that was established for this purpose. Because the cost of internal controls should not exceed the anticipated benefits, the objective is to provide reasonable, rather than absolute, assurance that the financial statements are free of any material misstatements.

The State Auditor and Clifton Gunderson LLP, an independent certified public accounting firm, jointly performed an independent audit of the State's basic financial statements for the fiscal year ended June 30, 2008. The auditors have issued an unqualified opinion, the most favorable outcome of the audit process.

This letter of transmittal is designed to complement management's discussion and analysis that immediately follows the report of the independent auditors.

PROFILE OF THE GOVERNMENT

South Carolina extends from the Atlantic Ocean westward to the Blue Ridge Mountains, containing over 30,000 square miles. Fortieth in geographic area among the fifty states, South Carolina ranks twenty-fourth in population with approximately 4.4 million citizens.

As shown in the organization chart on page 15, State government is divided into three separate branches: legislative, executive, and judicial. The State's citizens elect the legislative and executive branch officials. The General Assembly elects certain members of the judicial branch, including the Supreme Court. The principal State officials currently in office are listed on page 14.

State government provides a full range of services to South Carolina's citizens including educational, health, social/human, transportation, public safety, regulatory, and conservation/natural resources services. In addition, the State provides grants and loans to assist local governments, including school districts, within its borders.

Certain legally separate entities are included in these financial statements because they function, in essence, as part of State government. The Governor appoints the governing boards for the Public Service Authority, a public utility company, and the State Ports Authority. The Connector 2000 Association, Inc. assists the State's Department of Transportation on a toll road project. The Lottery Commission transfers its net proceeds to the State for educational programs. Other entities benefit and support institutions of higher education, provide medical malpractice insurance, and address medical and educational needs of South Carolina's children. Additional information on these legally separate entities can be found in the notes to the financial statements.

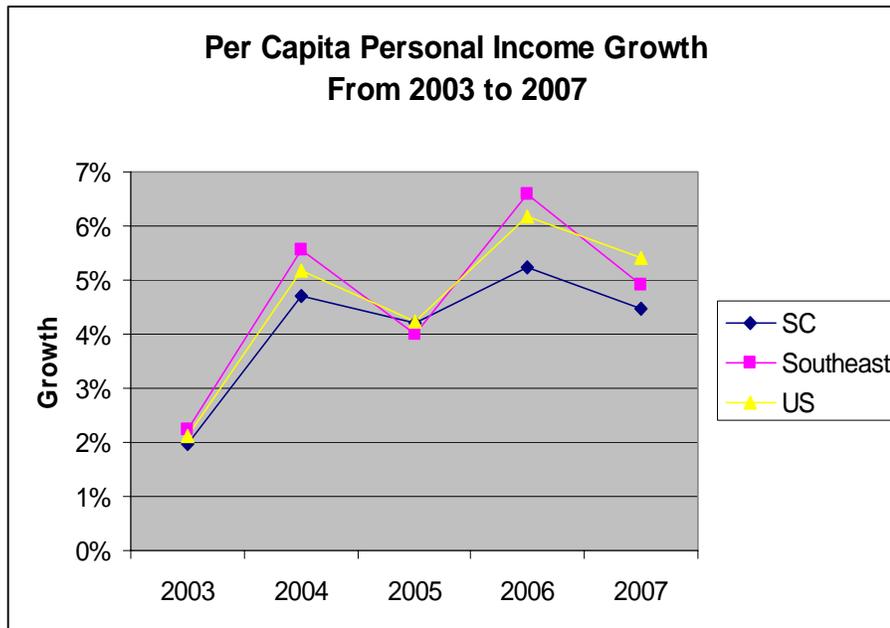
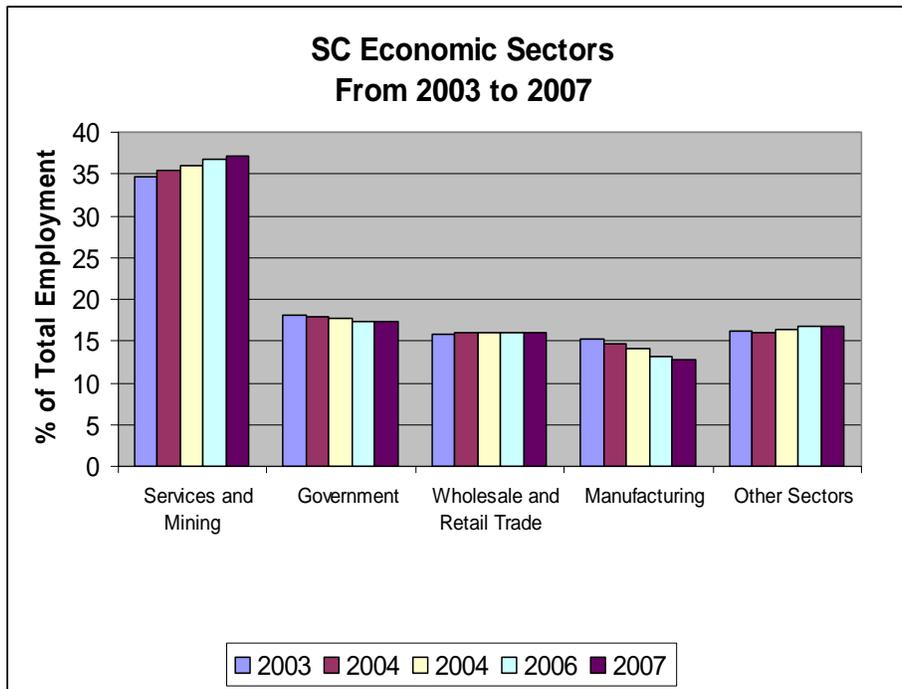
South Carolina's annual Appropriations Act includes legally adopted budgets for the Budgetary General Fund and for Total Funds. The initial budget appears in the annual Appropriations Act. After the budget year begins, the State Budget and Control Board, comprised of five key executive and legislative officials, may order spending cuts if revenue collections fail to reach predicted levels. Departments and agencies may request transfers of appropriations among programs if the transfer request does not exceed 20% of the program budget. The Budget and Control Board has the authority to approve additional transfers of appropriations between personal service and other operating expense accounts. For additional information, see the notes to the required supplementary information - budgetary.

STATE ECONOMY

South Carolina has a diverse economic base, including manufacturing, trade, health care, services, and leisure and hospitality. 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, and accessibility to markets, and in recent years, substantial tax incentives.

Overall, South Carolina has suffered by the national soaring gas prices and stagnant economy but has seen a slight increase in job growth with total employment up 4,500 jobs, a gain of less than 1% over the last twelve months. The State experienced losses of 13,900 in construction and 5,000 in manufacturing from June 2007. The strongest employment gains have been in the State's service sector which has risen from 34% of total employment to 37% during the past five years. This sector, fueled by tourism, educational, and healthcare industries has contributed to a more diversified overall employment base and improved income levels. During fiscal year 2007-2008, average hourly earnings have increased by 3.4% and average weekly earnings have risen by 2.8%.

Although the State's unemployment rate of 5.9% continues to be 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 has fallen a half a percent from calendar year 2006. The State's unemployment rate as of September 2008 has increased to 7.3% based on the recent crisis in the financial markets.



South Carolina’s per capita income for 2007 increased to \$31,013, or 4.5% over 2006. Although the 2007 increase was below the national (5.4%) and southeastern states (4.9%) growth rates, it ranked as the highest per capita personal income growth rate for the State in the last five years.

South Carolina’s population at July 1, 2007, was 4.4 million. The State’s rate of population growth is presently the eleventh fastest in the nation.

The South Carolina Department of Commerce was involved in recruiting 15,666 jobs and \$4.05 billion in new capital investment to the state in 2007. This showed large job creation levels in

non-urban areas, new companies choosing to invest heavily in South Carolina and diversity in investments.

LONG-TERM FINANCIAL PLANNING

State law requires agencies receiving 1% or more of the total annual General Fund appropriations to provide an estimate of their general fund expenditures for the next three fiscal years. The State Budget Office combines these expenditure estimates with long-term revenue estimates made by the State's *Board of Economic Advisors* (BEA) to create a three-year financial plan. The three-year financial plan assists the State in strategically assessing its future financial commitments. The plan is updated annually and provided to the State's Budget and Control Board, the Speaker of the House of Representatives, and the President Pro Tempore of the Senate during the second quarter of each fiscal year.

Principal financial challenges facing state government include anticipated future spending increases for Medicaid, State retirement and health benefits (including post employment benefits), and elementary and secondary education.

The State's long-term financial management practices include a five-year capital improvement plan, which requires funding to be in place before beginning construction on any capital improvement projects.

RELEVANT FINANCIAL POLICIES

The State's legislature is required to adopt a balanced budget annually based on revenue projections provided by the BEA. State law requires the BEA to meet at least quarterly to review how actual revenue collections compare with its earlier projections, and to adjust its projections if necessary. If the BEA reduces revenue projections significantly once the budget year begins, the State's Budget and Control Board is responsible for taking appropriate action to keep the State's budget in balance. If the Board anticipates a year-end operating deficit as a result of the BEA reducing its revenue projections, it must first reduce amounts set-aside in the Annual Appropriations Act for the 2% Capital Reserve. If the anticipated deficit is greater than the 2% Capital Reserve, then the Board must reduce most agency appropriations evenly across-the-board. The State also is required to maintain a 3% General Reserve that can be used only for eliminating a year-end operating deficit. If the State's budgetary General Fund subsequently experiences a year-end operating deficit even after applying all the actions described above, the Board is required to meet within sixty days of August 31 to adopt a plan to liquidate the deficit.

Legislation also exists directing that in closing the books each year the Comptroller General shall suspend, to the extent necessary, any budgetary surplus appropriations in a general or supplemental act or Capital Reserve appropriations, if the State's GAAP-basis General Fund reports a negative unreserved fund balance.

The State's General Fund experienced a budgetary operating deficit and a negative GAAP unreserved fund balance for the fiscal year ended June 30, 2008. The State applied the entire Capital Reserve Fund of \$125 million, \$73 million of the General Reserve Fund, and \$34 million of fiscal year 2007 surpluses that had been carried over for spending in fiscal year 2008 to cover the budgetary operating deficit.

MAJOR INITIATIVES

Finance and Budgeting

The General Assembly approved provisions for guaranteed two percent annual cost of living adjustment (COLA) for beneficiaries within the South Carolina Retirement System and the South Carolina Police Officers Retirement System. The legislation provides that in years when the

Consumer Price Index, which is used to measure inflation, increases by no more than two percent, retirees within these systems are awarded a two percent cost of living adjustment. In years when the Consumer Price Index increase by more than two percent, the legislation establishes conditions that must be met before these retirees may be awarded a cost of living adjustment beyond two percent up to the total percentage increase in the Consumer Price Index or four percent, whichever is less.

The 2008-2009 Appropriations Act includes a 1% pay raise for state employees and funded teacher's salaries at \$300 over the Southeastern average.

Reforms

The General Assembly approved the "South Carolina Illegal Immigration Reform Act." This comprehensive legislation provides criminal penalties for harboring and transporting illegal aliens as well as for the possession for certain fraudulent documents. The legislation employment eligibility verification; prohibits the employment of unauthorized aliens; and authorizes a civil right of action for wrongful termination. Among other things, the legislation places new restrictions on receiving public benefits; establishes a mechanism for the recording and reporting of immigration law violations; requires the enforcement of standards of ethics in the profession of immigration assistance by private individuals who are not lawyers; and prohibits the development of "sanctuary cities" in South Carolina by requiring local officials to adhere to State law.

Responding to the large numbers of alcohol and drug related traffic collisions, the General Assembly revised driving under the influence (DUI) laws this session. The legislation approved by the General Assembly enhances penalties for the offenses of driving under the influence and driving with an unlawful alcohol concentration and structures these penalties so that they are increased according to the offender's level of intoxication. Individuals convicted of drunk driving offenses are required to complete drug and alcohol treatment plans.

Business and Economic Development

The South Carolina Educational Broadband Service Commission was established to evaluate business proposals for leasing the excess spectrum capacity licensed to the South Carolina Educational Television Network that will become available following the federally required conversion to digital broadcasting.

The General Assembly approved the "South Carolina Residential Improvement District Act" to provide a new option for financing infrastructure and other improvements needed to facilitate development. Under the legislation, the owners of real property may request the governing body of a county or municipality to create a district consisting of their property and impose assessments within that district. A local government is authorized to issue bonds secured against the revenue from these assessments in order to fund proposed improvements such as roads, sidewalks, parks, playgrounds, recreational facilities, parking, facade redevelopment, storm water drainage projects, utilities, and school construction or renovation.

Education

The 2008-2009 Appropriations Act provides an additional \$94.5 million to fully fund the Education Finance Act. Other important legislation in support of education includes comprehensive legislation revising the Education Accountability Act of 1998 which replaces the Palmetto Achievement Challenge Test (PACT) with a new accountability test. Also, the South Carolina LightRail Consortium was created to manage access to a high speed, high bandwidth fiber optic communications network for research and clinical work conducted by the State's institutions of higher learning and their research partners.

Energy Conservation

The General Assembly approved a bill establishing incentives for energy efficient manufactured homes. The legislation establishes the Energy Efficient Manufactured Homes Incentive Program to allow an individual who purchases a manufactured home that meets energy saving efficiency standards to receive an income tax credit equal to seven hundred fifty dollars.

Also, legislation was passed for a Fleet Management Program that seeks to improve environmental quality in this state by decreasing the discharge of pollutants. In addition the legislation outlines that a preference in purchasing state motor vehicles must be given to hybrid, plug-in hybrid, bio-diesel, hydrogen, fuel cell, or flex-fuel vehicles when the performance, quality and anticipated life-cycle costs are comparable to other available motor vehicles.

AWARDS AND ACKNOWLEDGMENTS

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, 2007. This was the twentieth consecutive year that the State of South Carolina has achieved this recognition. In order to be awarded a Certificate of Achievement, a government must publish a timely, easily readable, and efficiently organized CAFR. The CAFR must comply with both generally accepted accounting principles and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. We believe that our current CAFR continues to meet the Certificate of Achievement Program's requirements and we are submitting it to the GFOA to determine its eligibility for another certificate.

Production of the CAFR was made possible only by the support of all State agencies and component units that supplied financial data to our office on a timely basis. We extend special appreciation to Mr. Larry Pearce, Director of Publications and Printing at the University of South Carolina, for providing the CAFR's attractive cover.

Sincerely,



Richard Eckstrom, CPA
Comptroller General