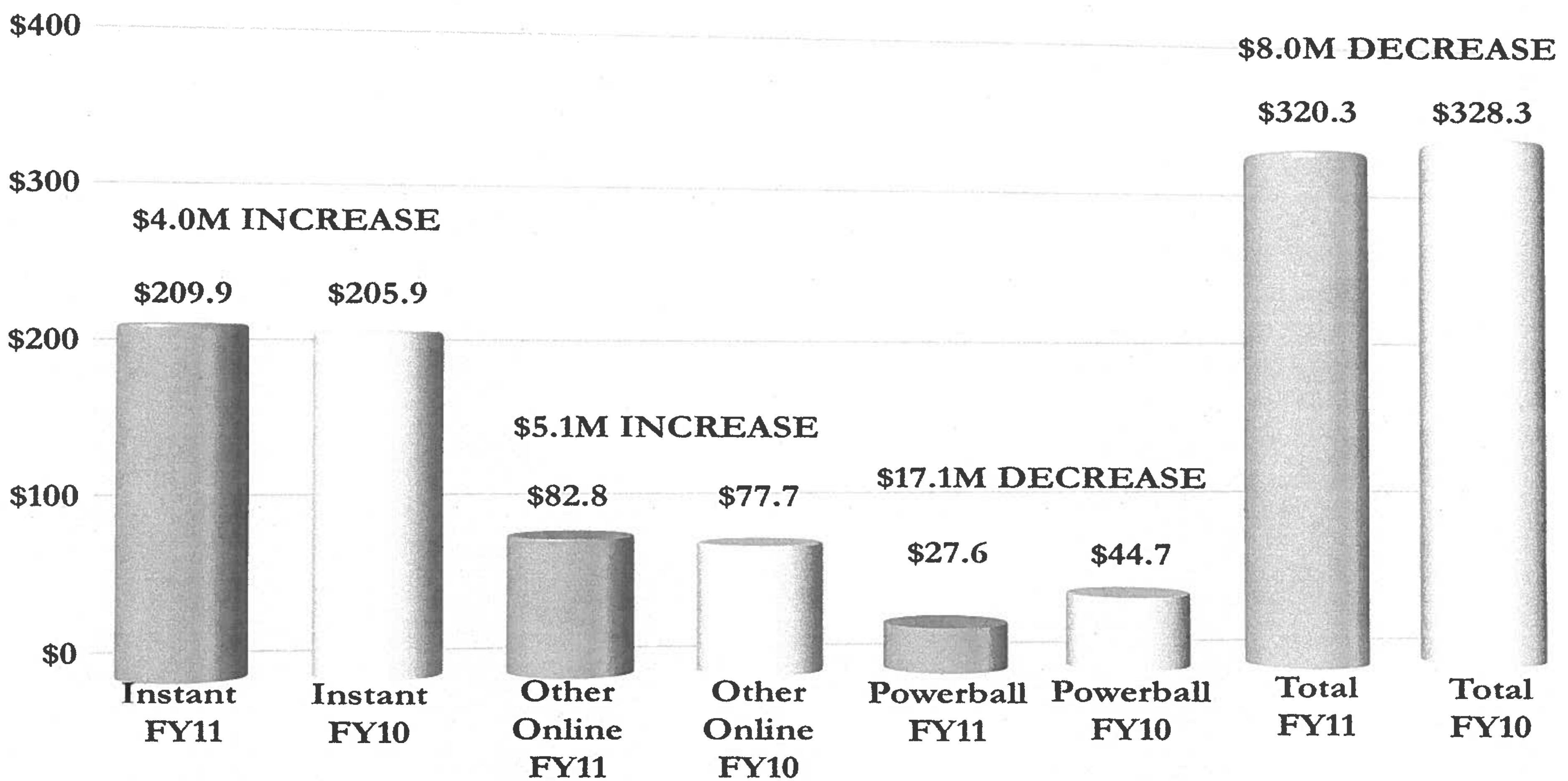
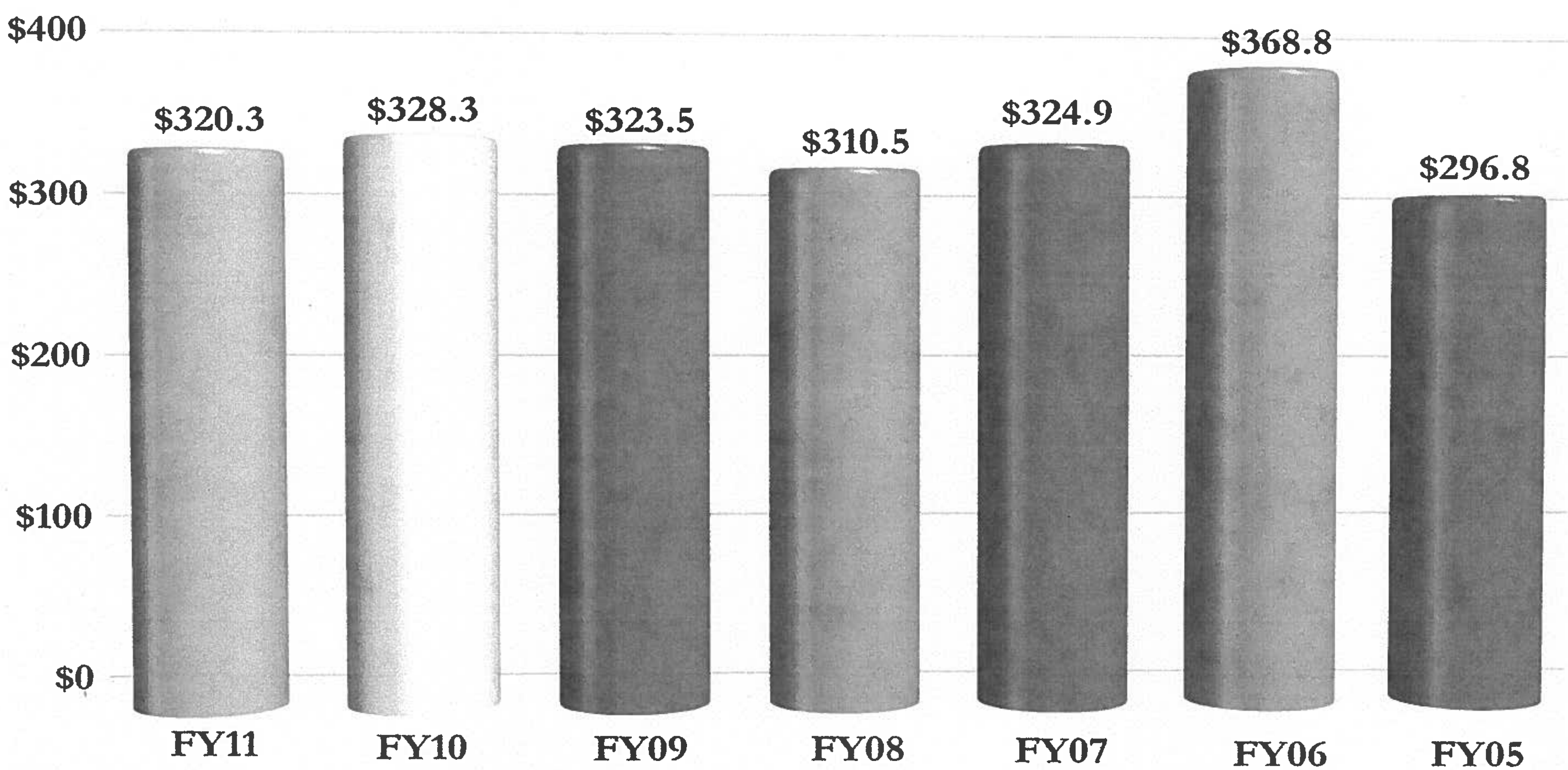
South Carolina Education Lottery
Presentation to
Ways & Means Committee
The House of Representatives
November 18, 2010

Instant and Online Sales – July - October – FY11 & FY10 ($M)



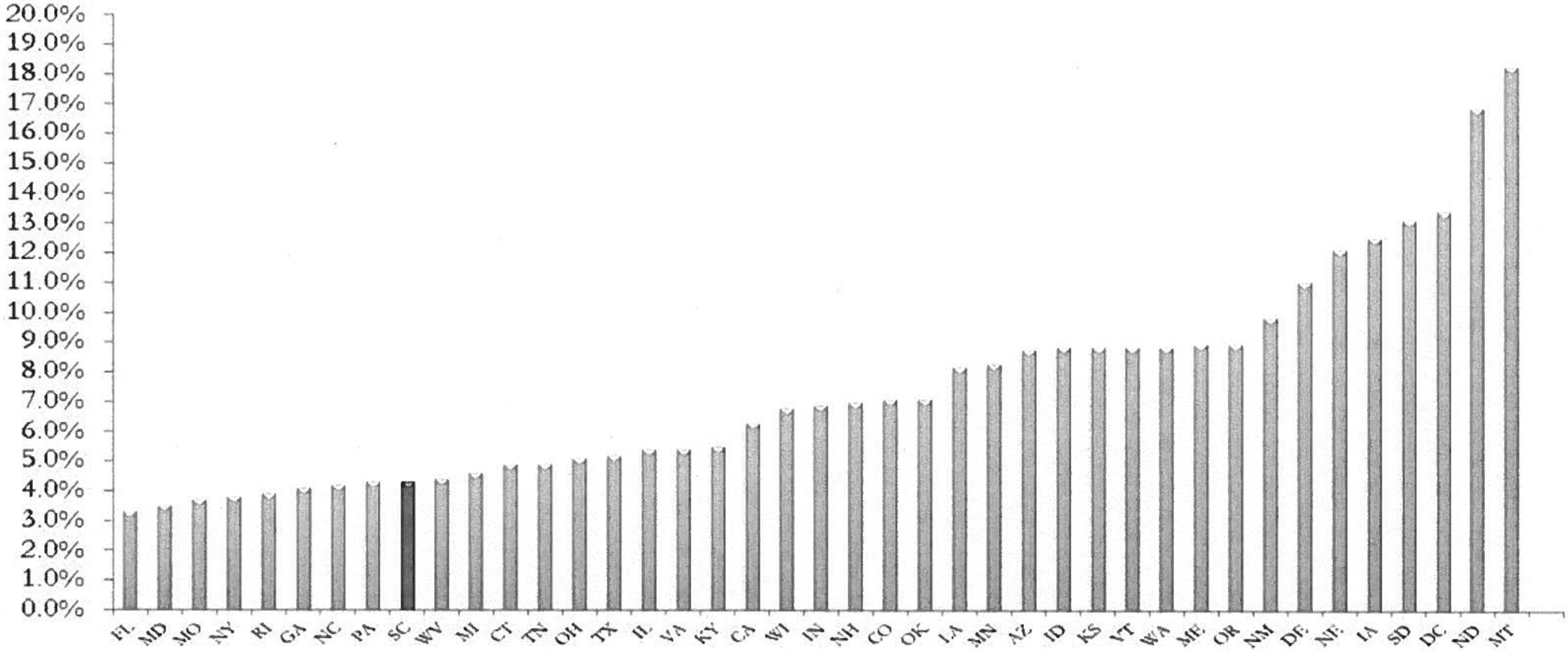
South Carolina Education Lottery®

Sales Revenue ($M) – July - October



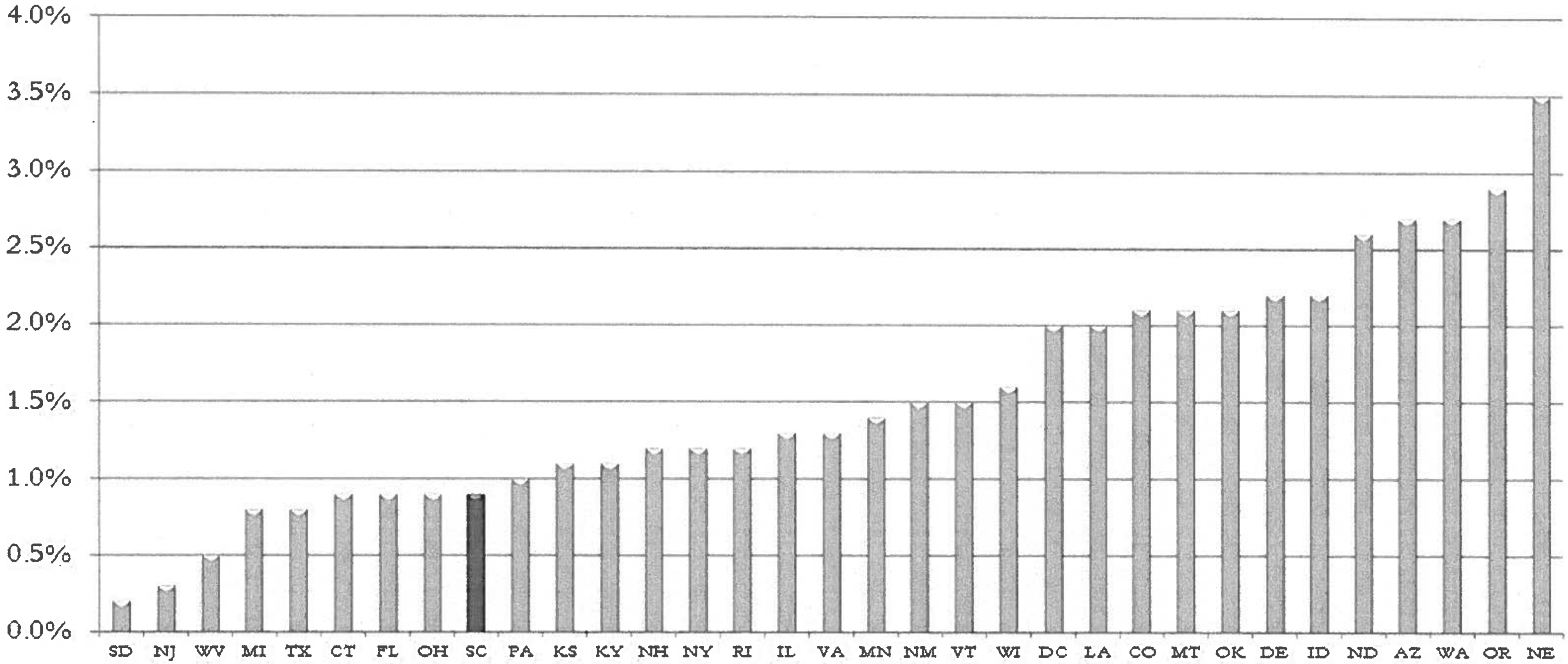
South Carolina Education Lottery®

Administrative Expense as % of Gross Sales (FY09)



South Carolina Education Lottery®

Advertising as % Sales (FY10 Budget)



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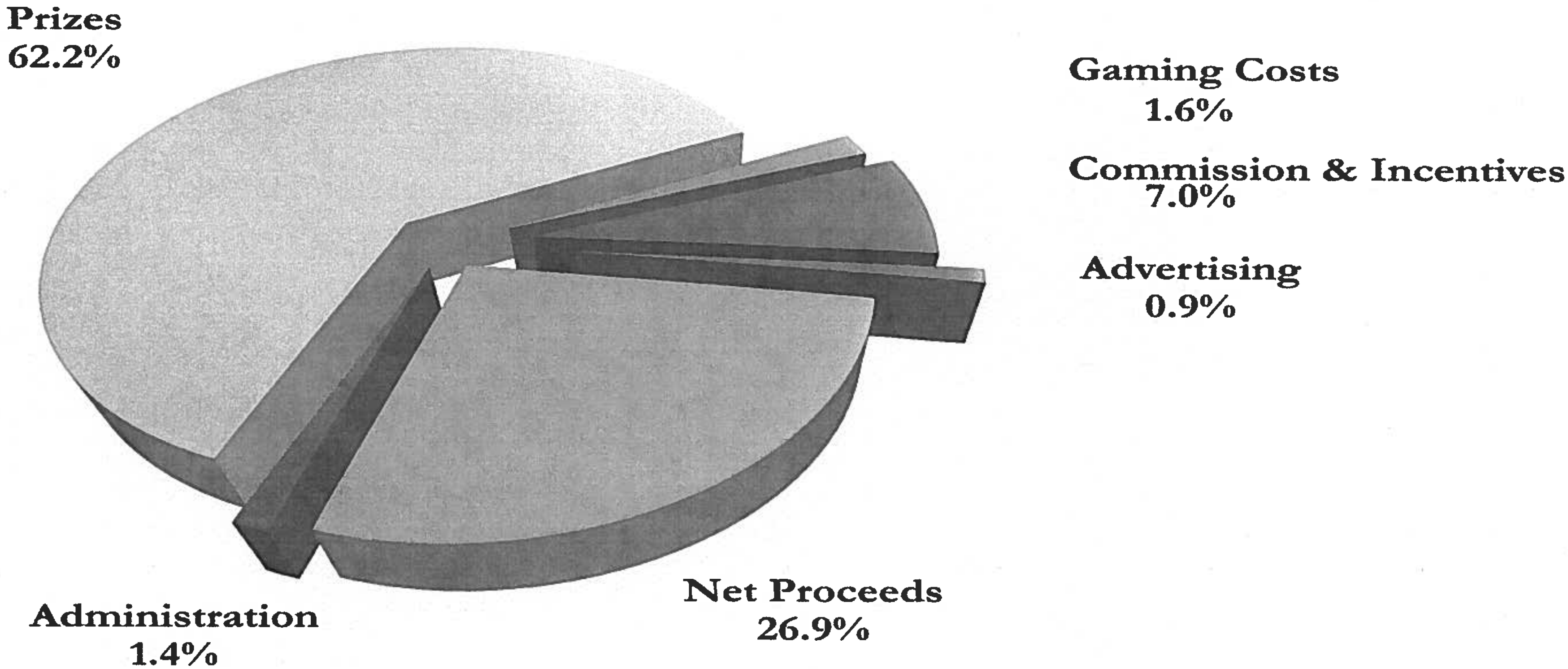
Percent of Total Revenue FY10



FY11 SALES FORECAST =		$955M
× BUDGETED OPERATING MARGIN	×	26.5%
= FORECAST NET INCOME		$253.1M
STATE ESTIMATE		$252.4M

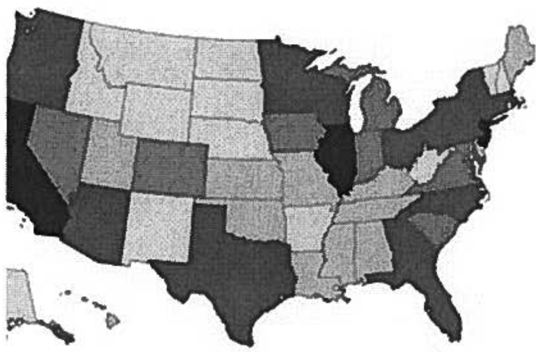
The Wall Street Journal Wed. November 17, 2010

States Offer Washington Lesson in Belt Tightening

The U.S. government is now borrowing $5 billion every business day and has done nothing more than talk about a plan to reduce its debt. State governments don't have that luxury.

States in the Red

Most states have addressed or still face gaps in their budgets, while tax revenue declined.



From Sacramento to Austin to Albany, the day of fiscal reckoning is here. At one point this spring, financial markets were demanding more to insure investors against defaults by Illinois, New Jersey, New York and Michigan than to insure the debt of Ireland and Portugal, the flailing economies of Europe.

Federal aid cushioned states from some of the drop in revenues during the recession, but that's running out. With all statehouses unable to borrow as readily as Washington and nearly all constitutionally required to balance their budgets, they can't ignore gaps between revenue and spending.

On Monday, Pennsylvania's house of representatives passed a bill, already approved by the state senate, that raises the retirement age for

Illinois lawmakers met Tuesday to debate options for addressing their troubled state budget, including a major gambling expansion, an income-tax increase and borrowing $4 billion to make pension payments.

After learning that California faces a deficit next year of $25.4 billion, twice the size of previous forecasts, California Gov. Arnold Schwarzenegger last week called for legislators to meet Dec. 6 in a special session to make midyear budget cuts.

State governments—battered by the downturn and generous pension promises to their employees—have cut spending and raised taxes, while Washington has been spending more to prop up the sagging economy and cutting taxes.

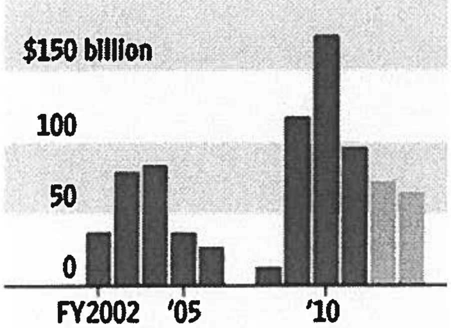
In the past three years, 29 states have raised fees on, or cut services for, the elderly and people with disabilities, says the Center on Budget and Policy Priorities, a liberal-leaning research group. Fifteen states raised sales or income taxes in 2009 or 2010, according to the Tax Foundation, a conservative-leaning Washington research outfit.

At some point, Congress and the president will have to grapple with the gap between revenue and spending. Despite a tough proposal last week from the leaders of a deficit-reduction panel appointed by the White House, the recent congressional elections left many deficit hawks dispirited.

Too many Republicans, the hawks say, have persuaded themselves they can reduce the deficit significantly by cutting only unpopular spending and rejecting tax increases. And Democrats, they worry, are digging in to protect spending on health and retirement benefits, which drive future deficits, and on education and infrastructure—and to insist on higher taxes. Polls suggest the public is divided, and sometimes simply inconsistent.

Big Holes

Tax increases, spending cuts and other measures required to close state budget gaps



Notes: For fiscal years ending June 30. 2012 and 2013 are projections.
Source: National Conference of State Legislatures

There are many reasons, of course, that state governments and the national one have to manage their finances differently. Washington is expected to run big deficits during recessions; states can't. Washington issues debt deemed the safest in the world; states have to worry about credit ratings and the prospect of someday being shut out of markets.

Yet in significant ways, state governments offer a hint of what lies ahead for Washington.

One popular state tactic has obvious—and ironic—national implications. New Jersey, Indiana and Minnesota, among others, have trimmed state spending by sending less money to local governments. That pushes onto local officials politically tough decisions about raising taxes, cutting spending or finding major money-saving efficiencies. In the past, Republicans in Washington have proposed shrinking and removing strings from various federal-state programs and letting states figure out how to do the job with less.

In other states, notably Illinois and California, the political system has done little more than lurch to the end of the fiscal year. California voters took a step toward alleviating gridlock, approving a referendum that reduces the legislative votes needed to approve a budget to a simple majority, from the current two-thirds. It will still take two-thirds to raise taxes or fees, however.

There are political lessons to be gleaned from what is happening in some states. In Indiana, Mississippi and New Jersey, Republican governors appear to be maintaining their popularity while cutting spending. New Jersey's Chris Christie has cut pensions for future state and local employees, vetoed a tax increase on income over $1 million and cut $1.26 billion in aid to schools and municipalities, which local officials said would drive up property taxes. Among New Jersey residents, 51% approved of the job Mr. Christie was doing, versus 37% who

But, just as Washington has been reluctant to cut Social Security and health benefits, most states have yet to tackle their biggest fiscal issue: the trillions of dollars in pension and health benefits promised to state employees, for which states haven't set aside enough money.

Tolerance for state tax increases may be fading. Twelve of the newly elected governors—11 Republicans plus New York Democrat Andrew Cuomo—have ruled out tax hikes to cure deficits, according to a tally by Stateline.org, a website published by the Pew Center on the States. In Washington state, voters recently undid higher taxes on candy, bottled water and soda that the legislature had enacted, and they rejected a proposed income tax that would have hit only high-wage earners.

In Indiana, Gov. Mitch Daniels, a second-term Republican and the former White House budget director for President George W. Bush, moved the state from deficit to surplus by paring spending in good times. Indiana swung from a nearly $200 million deficit in 2004, the year Mr. Daniels was first elected, to a $1.3 billion surplus last year. It was not without controversy: On his second day in office, Mr. Daniels issued an executive order that ended collective-bargaining rights for state employees.

The Daniels approach wasn't tax-free. He increased the state cigarette tax to help pay for a new health-care program.

Indiana eliminated roughly half its nearly $1 billion deficit for its latest fiscal year by drawing down rainy-day funds it had built up in good times. The rest came from spending cuts, large and small. In April, Mr. Daniels directed state agencies to reduce spending 5% for the current fiscal year, on top of a 10% cut ordered earlier. He cut $150 million in aid to state colleges and universities, suspended a $15 biweekly matching contribution to public-employee retirement accounts and reduced the number of state-owned vehicles.

Some of the state's most-vulnerable citizens have been affected. In October, the state ended a grocery subsidy for more than 400 developmentally disabled people. Officials said the program was misused. Nonprofits serving the disabled say some are turning to food banks.

In January, foster parents won an injunction blocking Mr. Daniels' proposed 10% cut in state aid to them. On Nov. 4, Mr. Daniels proposed cutting unemployment benefits, despite the state's 10.1% unemployment rate. Indiana has borrowed nearly $2 billion from the federal government to shore up its unemployment-compensation fund. Next year, the state intends to begin charging businesses more to replenish the coffers.

The state's fiscal cushion is getting thinner. By June 2011, the state will have less than $200 million in its rainy-day fund, forcing it to rely mainly on spending cuts or revenue increases to address a projected $1.2 billion shortfall. Earlier this month, the governor said he is opposed to any tax increase.

Indiana voters appear to prefer reduced services to higher taxes, at least higher property taxes, which are levied by local governments. On Nov. 2, 72% approved putting property-tax caps into the state constitution, making it difficult for future lawmakers to change them. "We put the caps there so [local-government] units could not find a way to raise property taxes back to a level we had just found intolerable," Mr. Daniels said in a recent interview.

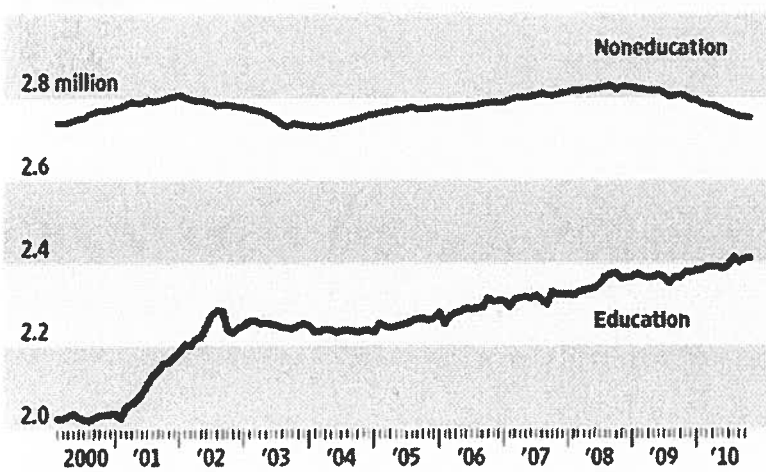
Mr. Daniels remains popular. He was re-elected by an 18-point margin in 2008, and his approval rating hovers around 65% now.

In May, Minnesota lawmakers approved a budget widely seen as a victory for outgoing Republican Gov. Tim Pawlenty, because it ratified spending cuts he had made unilaterally and it didn't raise taxes. The deal, which eliminated a $3 billion deficit, gave the governor or his successor—the election results aren't yet final—power to shift thousands of low-income Minnesotans from a state-funded health plan to the state-federal Medicaid plan. Lawmakers balanced this year's budget, mainly by delaying $1.9 billion in payments that had been promised to K-12 schools by June 2011, setting aside nothing to make payments later.

Part of Mr. Pawlenty's budget-balance strategy has been reducing state aid to cities and counties. In the fiscal year that ends in June 2011, state contributions will represent 16% of local-government revenue, excepting school funding, down from 25% eight years earlier, according to Minnesota 2020, a left-leaning St. Paul think tank. The state provided 64% of local school revenue this year, down 10 percentage points from 2003.

Cutting the Budget

State-government employment, education and noneducation employees



Source: Bureau of Labor Statistics

The result: Local governments have to choose between raising taxes and cutting services.

In Indiana, for example, local governments increased property taxes, which provoked a backlash. Gov. Daniels backed a 2008 state law that limited property taxes to 1% of the assessed value for homes, 2% for rental properties and farms, and 3% for businesses.

To shore up school budgets, Indiana then raised the sales tax to 7%, from 6%. But as residents cut back on spending, sales-tax revenue fell. Mr. Daniels told school districts in January to cut budgets 3.5%. When parents, teachers and administrators protested, he offered a "Citizens'

Checklist" of ways to cut budgets without teacher layoffs. Sample suggestion: "Examine and reduce all fringe benefits of school-board members and administration..."

In Muncie, Republican Mayor Sharon McShurley, who supports the property-tax cap, has cut, among other things, the firefighting budget, angering the Democratic-controlled city council. As part of $464,000 in budget cuts for the coming year, the council eliminated funding for the leased copier and printer in the mayor's office. She is seeking donations to replace the equipment.

Indiana's nonpartisan Legislative Services Agency said the caps will cost cities and towns—and save property owners—$474.6 million this year, nearly 10% of potential total property-tax revenues. State auditors warn that tax caps could push the city of Gary into insolvency.

Illinois is a case study in the cost of delay. With revenue falling and payments due to state-employee pension funds, Illinois faces a deficit for the fiscal year beginning July 1, 2011, that could reach $15 billion—more than half the state's general-fund budget. Because the state hasn't made any pension payments for four months, the pension funds have been selling assets.

The state's backlog of unpaid bills reached $5.5 billion at the end of September, $2 billion of which must be paid by Dec. 31. "The ability of the state to maintain any reasonable level of education and social-service funding—and just as importantly, to pay for those services on a timely basis—will be severely jeopardized," Comptroller Daniel Hynes has warned.

Companies that provide foam food trays for prison meals and bullets to train prison guards stopped delivering because they weren't being paid. Social-service agencies have cut staff, reduced caseloads, and, in some instances, closed altogether, as they wait for the state to pay bills.

Earlier this year, Democratic Gov. Pat Quinn, who kept his job by a narrow margin on Nov. 2, proposed a one percentage point increase in the state income tax, to 4%, dubbing it "1% for education." But the Democratic-controlled House balked. His Republican opponent for governor, state Sen. Bill Brady, advocated cutting taxes, saying that would boost the state's economy, as well as cutting spending "a dime for every dollar." Neither candidate laid out a plan to balance the budget.

So far, Illinois hasn't had difficulty borrowing, but it is paying more to do so. Its Moody's bond rating is the lowest of any state.

—Lisa Fleisher contributed to this article.