

Lieutenant Governor Michels, Mr. Speaker, members of the legislature, Chief Justice Gilbertson, Justices of the Supreme Court, constitutional officers and fellow South Dakotans... *(slowly)* Thank you very, very much for giving me the enormous challenge and the wonderful opportunity to be your Governor.

(pause for applause)

It is my privilege today to offer my thoughts on the state of our state. To do this, one must first ask the question: against what standards do we measure ourselves. I believe we should look to the citizens of South Dakota for the answer. Over the last year, most of us were involved in political campaigns. We visited with thousands and thousands of South Dakotans. They told us what they want from their government.

They want balanced budgets,
They want the deficit eliminated,
They want fewer and simpler regulations,
They want more and better jobs,
They want to be protected from crime,
They want help for those who need education or training to become self-reliant,
They want care for those who have no one else to care for them, and
They want more opportunities and better lives for themselves, their children and grandchildren.

In short, the people want a strong foundation for our state. That's where we must focus our energy. That's why the people elected us.

PRAISE FOR GOVERNOR ROUNDS

I am grateful for the opportunity we will all have to work toward this goal.

I am also very grateful for the hard work that was done over the past eight years by the state legislature and by Governor Mike Rounds. Our state is in a much stronger financial condition than almost any other state because of decisions Governor Rounds and the legislature made.

Even after the national recession, South Dakota has more jobs now than when Governor Rounds took office. We have made improvements in our gross domestic product, visitor spending, and capital investment. Our unemployment rate is among the lowest in the nation. We have made substantial increases in ethanol production and wind energy. Our schools receive \$109 million more than they did eight years ago. We have record enrollments and dramatically more research at our state universities. And we have secured the future of Ellsworth and continued the development of the Homestake Lab.

All of this happened because of the hard work of the people of South Dakota, our state legislators, and... Governor Mike Rounds. Please join me in thanking Governor Rounds and all those who served over the past eight years for their service to South Dakota. *(pause for applause)*

CREATING JOBS AND GROWING THE ECONOMY

The dominant challenge of THIS legislative session will be the state budget. I have asked legislative leaders to convene a Joint Session on January 19 – eight days from now – to receive my budget proposal.

The budget will present tough choices. But much of this challenge emerges from the national recession, which has caused revenues to fall and the demand for services to rise. That is why my number one priority as governor is to create jobs and grow the economy – it is the best long-term solution to solving our budget problem.

During the campaign, I released an economic development plan entitled “Building a Stronger South Dakota.” This is my goal. It must be the goal for us all: To create a state with more jobs, more wealth, and more opportunities for our young people.

It is a four-year plan, not a one-year plan, and I am always open to improving this plan or adding to it as circumstances change. But I will act vigorously to implement this plan, starting today.

I propose to elevate the Governor's Office of Economic Development to cabinet level, reporting directly to me as Governor. I plan to be personally involved, every day, in our state's economic development efforts. I am proud to have Pat Costello as Commissioner of GOED. Pat has practiced as a CPA, run a business, and served his community as a civic leader. He will be a great partner to me in leading our economic development efforts.

I intend to be South Dakota's Number One salesman. Often, a governor is called upon to be a "deal-closer," and that is an important role. I will also be a "door-opener," and I will use my office to seek out new opportunities for our state.

Our economic development efforts will use a three-pronged approach: invite, increase, and innovate.

First: **Invite**. We should continue to invite businesses from high-tax, over-regulated states to come to South Dakota.

Second: **Increase**. We should encourage those businesses that are already here to increase their production and the number of people they employ in our state. We need to help them find orders and contracts. We need to help them add new lines to their businesses.

Third: **Innovate**. We should foster innovation and entrepreneurship, because some of our best businesses – the ones who are most likely to expand here and stay here – are the businesses that are started in South Dakota by South Dakotans. That's why we need to keep expanding research efforts at the universities, and strengthen our efforts to bring researchers together with entrepreneurs so that new knowledge can lead to new businesses.

REDI FUND AND ETHANOL INCENTIVES BILL

Another economic development goal I set during my campaign is to revamp the Revolving Economic Development Initiative or "REDI" Fund.

An important first step is to increase the total value of the fund. I'm proud to announce today an innovative and forward-thinking partnership with our state's ethanol industry that will refocus state ethanol incentives and provide an extra \$10 million for the REDI Fund over the next five years.

Currently, our state provides \$7 million a year in incentives to ethanol plants operating in South Dakota. I will be introducing a bill that to save the state \$13.5 million over the next five years by spreading out the current ethanol incentives over an additional two years. \$3.5 million of that savings will be used to install even more ethanol blender pumps in South Dakota, allowing our citizens to use higher blends of ethanol in their vehicles. The extra \$10 million in savings will be deposited in the REDI Fund over five years.

This approach is a “win-win-win.” First, our economic development efforts will have more money to invest in South Dakota business. Second, our ethanol industry will get an investment in blender pumps – the infrastructure needed to expand ethanol markets. And third, we will do this at no additional cost to our budget. I want to recognize the vision the ethanol industry has shown in working with me to craft this innovative plan. They are redeploying millions of short-term-incentive dollars to expand their markets and strengthen their industry in the long term.

SMALL TOWNS

I appreciate that the ethanol industry has brought jobs and wealth to the rural areas of our state. South Dakota is a state with many small towns, and they must be an important component of our economic development efforts. We will work with local and regional economic development organizations, and non-profits, to identify and train “small town specialists” who can work with local leaders to make contacts, create plans and goals, and promote themselves to businesses.

I will revamp our MicroLOAN program, which provides loans to small businesses for capital assets. This program is underutilized because it is too bureaucratic. Some are reluctant to apply because of the burdensome application process. That is government at its worst. I will ask the Office of Economic Development to streamline the application paperwork and approval process. I will also prioritize loans to aid in the sale of small businesses. In many small town businesses, the value of a business’s inventory is so high that banks are hesitant to finance a potential purchaser. This can lead an aging shopkeeper to shut down, for lack of an available buyer. We can use the MicroLOAN program to help younger owners purchase these businesses and keep our small town businesses open.

AGRICULTURE

Of course, our small towns rely heavily on the ag economy. Agriculture is our state's number one industry and the foundation of our economy. Over the past few years, Mother Nature has provided some challenges--heavy rains, hailstorms, blizzards, and outbreaks of grasshopper and mountain pine beetle--but our producers have still enjoyed strong financial returns. Our robust ag economy is the principal reason that South Dakota's personal income growth is among the best in the nation. And a strong ag economy not only helps our farmers and ranchers, but also the numerous ag-based businesses on Main Streets across the state.

I will aggressively pursue opportunities to expand value-added agriculture, like the Dakota Provisions plant in Huron and the beef plant in Aberdeen. And I will host an annual Governor's Forum on Agriculture, in conjunction with the second annual Governor's Ag Development Summit, to discuss the future of ag with every commodity group and stakeholder. I want to open the lines of communication to ensure that state government is always acting in the best interests of farmers and ranchers. My door will always be open.

TOURISM

Just as we focus on our largest industry, so too must we continue to promote our second-largest industry, Tourism. The visitor industry in South Dakota has enjoyed great success over the past several years, and I expect to announce another strong total for 2010 at the Tourism conference next week. While the recession caused visitor spending to fall in much of the nation, we have held strong in South Dakota.

We need to build upon that success. I will be elevating Tourism back into the cabinet to give this industry a strong voice. And I will be bringing a bill to retain the extra half-cent tax that the visitor industry placed upon itself in 2009. That tax is set to expire, but these revenues are important to continue to provide for our very successful tourism promotion efforts. South Dakota is a great place to visit, and we must continue to tell our story and to invite people from all over the world to enjoy our state.

LARGE PROJECT REFUND PROGRAM

I will also be introducing a bill reforming the Large Project Refund Program. This program, which was a topic of much discussion last year, was created to encourage investment in large projects in South Dakota. It has worked. Ethanol plants, ag processing plants, and wind power projects have all been built in South Dakota in part because of this tax incentive program. However, this program has also been used by some projects that would likely have been built in South Dakota anyway. We should reform this program so that it only attracts new projects without giving tax refunds to projects that would have been undertaken anyway.

As you know, this program is scheduled to sunset at the end of 2012. It would be a mistake to let this program expire and lose this important economic development tool. I will be asking the legislature to reform this program to provide that refunds only be given to those projects that would not otherwise be undertaken, and to give discretion to determine when a project meets that standard. There is no way to write a law that perfectly anticipates every situation. It makes more sense to allow for discretion in awarding the tax rebates, so that loopholes cannot be used to secure unneeded rebates. I would ask that you would provide this authority so that South Dakota can be protected from unnecessary tax giveaways.

HOMESTAKE LABORATORY

I would like to update you for a moment on developments at the Sanford Underground Laboratory at Homestake. Biology and geology experiments are already being conducted at the lab and nearly all of our state universities are participating. More experiments are preparing to commence this year.

Under a preliminary agreement, the original plan was for the National Science Foundation to build the facility and for the Department of Energy to pay for the excavation of large cavities. But recently, the National Science Board has taken the position that the Department of Energy should own and build the facility and that the National Science Foundation should pay for only experiments. Therefore, \$29 million in funding is being withheld by the National Science Board and has not been released to Homestake.

Over the past several weeks, Governor Rounds and I worked closely with the NSF, the Department of Energy, and our congressional delegation to secure short-term funding to continue this important project. Although this is a challenging situation, I will keep working to secure this funding so the lab can continue to operate while a new agreement is reached. I hope this can be accomplished very soon.

Everyone in South Dakota should be proud of the commitment that Governor Rounds, the State Legislature, and every citizen has made toward securing the deep underground lab for our state and our nation. I will work hard to ensure that the setback suffered in the past few weeks does not undermine the work of the past several years.

ELLSWORTH AFB AND AVIATION LIABILITY BILL

Just as Homestake has great potential to transform the economy of the Black Hills, Ellsworth Air Force Base is already an important economic driver. I was proud as Lieutenant Governor to help create the Ellsworth Development Authority, which encourages development that complements the Base. Aviation is an industry that would fit well near Ellsworth, and I will be proposing legislation that will make South Dakota more attractive to the aviation industry. I will ask you to reform South Dakota's product liability law for aviation manufacturers based in our state to protect manufacturers from claims arising years after the aircraft is manufactured. This bill is based on the state law of Kansas, which is home to many large aviation manufacturing operations, such as for Boeing. Just as we acted in the past to attract the financial services industry, we can change this law to give the aviation industry a reason to look at South Dakota.

NO NEW TAXES AND RED TAPE EFFORTS

These are some of the initiatives I will be undertaking in the next year to create jobs and grow our state's economy. But we cannot forget the important advantages we already have. We have the best business climate in the nation, and I intend to keep it that way.

Our first advantage is our low tax burden. I am proud that South Dakota has the lowest per capita tax burden in the nation. I said many times during the campaign that I will not raise taxes, except in the case of an emergency like a blizzard or a flood. And I mean it. A recession is the worst time to raise taxes – and if you send me a bill to raise taxes, I will veto it.

Our second advantage is our reasonable, predictable, and simple regulations. But this second advantage can be improved. It is the nature of government, over time, to become more regulatory, and we must be deliberate about resisting and reversing this.

Over the next year, we must undertake a comprehensive review of regulations in every agency of government. We must repeal the regulations that we don't need, and simplify those that are too complex. We must also seek the input of our customers – those who are regulated – to find ways to make government more streamlined and sensible.

EDUCATION

As we discuss economic development, we must remember that the foundation of our economy is an educated workforce. Every year, education is one of the dominant issues of the legislative session, but too often, the discussion is only about funding. That is an important discussion – and certainly one we will have this year. But we should not measure our schools by how much money they receive or spend. We should measure them by the success of our students.

By many measures, South Dakota students are succeeding. Eighty-nine percent of our high school freshmen complete high school – one of the best rates in the nation. Seventy-two percent of our graduates go on to college or technical school – also one of the best rates in the nation. And among states that test at least half of their students, our average ACT score is near the top of the list.

I believe our students and schools are successful because of good parenting that sends most SD kids to school ready to learn. They are met there by hard-working and committed educators who cause that learning to occur. My wife, Linda, worked for years as a teacher, school librarian, and coach.

These professionals dedicate their careers to our young people. It is because of committed teachers and administrators, hard-working students, and involved families that our schools achieve at the high level that they do.

Can we do better? Of course. I am firmly committed to ensuring every student who wants to go to college is fully prepared to enter and graduate. I am also committed to expand technical education opportunities, through partnerships with our tech schools and private businesses, so that high school students can have exposure to skilled, technical fields. I will also be sponsoring a bill to increase the bonding capacity of our post-secondary tech schools, to allow them to continue to expand their campuses and add new programs in technical fields.

We also must do a better job in the fields of science, technology, engineering, and mathematics. South Dakota does relatively well in these fields when compared to other states, but our children are not competing against Iowa and Minnesota. They are competing against India and China. Over the next year, I will begin to work toward new approaches to strengthen education in these important areas.

I want to use my office to promote new approaches in education and help schools implement them. But I also want to allow local school boards and school administrators to run their own districts. That is why I will be sponsoring bills this year to repeal the 100 student minimum for state aid to school districts, and to remove the cap on school district reserve fund balances. We must trust local officials to make the best decisions for their districts. And if they fail, we must trust local voters to find new local officials.

HEALTH CARE

Our system of education is the source of tomorrow's workforce, and we have no greater workforce need over the next ten years than in Health Care. By 2014, South Dakota will require an additional 13,000 health care workers. Partnering with health systems, professional organizations, educational institutions, and local governments, we must increase efforts to encourage our students to consider careers in health care. We should encourage local school districts to give high

school credit toward graduation for training in fields like EMT, dietetics, or nursing assistants.

We must also continue to promote the privately-funded DakotaCorps scholarship. Governor Rounds created this program, without state funding, with generous support from corporate and foundation donors. I have already begun conversations toward continued private support to DakotaCorps because this program rewards young people who commit to staying in our state and to entering into health care and other high-need fields.

My administration will also be working to comply with the new requirements that Congress has imposed on us as a part of federal health care reform. At the same time, however, I am going to continue to support the efforts begun by Governor Rounds and Attorney General Jackley to challenge the federal health care reform law in court. I will also support efforts in Congress to repeal this bill or reform its worst provisions. Over ninety percent of South Dakotans have health insurance. Here, our most serious problem is cost. Yet, the federal law focuses almost entirely on getting coverage for the few without insurance, and does little to control rising costs for the many already insured. This is a law that doesn't make sense for South Dakota.

INFANT MORTALITY

The federal health care law is frequent topic of debate. Likewise, Economic Development and Education are often discussed in the political arena, and rightly so. But another important issue in our state has not received as much attention – infant mortality.

Over the past decade, 113,517 babies have been born in South Dakota. 794 of them died before their first birthday. That is an average of 79 deaths each year. South Dakota's infant mortality rate is significantly higher than in North Dakota, Minnesota, Iowa, Nebraska, or Montana. And although we saw dramatic improvements from the 1960s to the 1990s, over the past decade our infant mortality rate has exhibited a worsening trend.

In the last several years, infant mortality among Native Americans in our state has improved, but is still higher than in most places. In the rest of South Dakota, the mortality trend has worsened.

It has been said that the infant mortality rate is the gold standard for measuring the health of a population. I will make it a priority to face this problem, head-on. We already know many of the factors that contribute to infant deaths. Too many mothers in our state – almost 20 percent – use tobacco products while they are pregnant. In one-third of South Dakota counties, over 30 percent of mothers don't seek prenatal care during the first trimester. And more young parents need to learn about safe sleep positions and other important infant care tips.

One tool our state has to combat infant mortality is the Bright Start home visitation program. Nurses visit expectant mothers in Sioux Falls, Rapid City, and Pine Ridge to educate them about healthy behaviors, during pregnancy and after their baby is born. I'm pleased to announce that the state has been awarded a \$645,000 grant to expand the Bright Start program to more communities.

But there is more to do. I'm going to ask doctors, hospitals, parents, and state and tribal leaders to come together to face this problem. Each of us has a role to play. We all want more South Dakota infants to reach their first birthdays.

TRIBAL RELATIONS

Infant mortality is one of many issues that will encourage close cooperation between state and tribal leaders. Our reservations are our integral parts of our state, and I do not view any challenges they face as solely tribal problems. They are South Dakota problems.

As Governor, I am going to work very hard to build positive working relationships between the state and each of our nine tribes. I want to base these relationships on two principles. First, I will always remember that the nine tribes are nine separate sovereign nations, each with their own set of circumstances. They should not be subject to a "one-size-fits-all" approach. Second, I want to be respectful of the wishes of tribal leaders. My first question to them will be "What challenges and opportunities do you face?" And my second question will be "How can we work together?"

I am creating a cabinet-level Secretary of Tribal Relations to help me build these relationships and hold these conversations. I want every tribal leader to know that I am serious about working with them to Build a Stronger South Dakota. I'm not looking to attend more meetings as window-dressing. I want to build real relationships that can lead to positive results for all South Dakotans who live on reservations.

EXECUTIVE REORGANIZATION ORDER

In addition to the bills and other proposed changes I've described already, I will be recommending several organizational changes. This week, I will be submitting an Executive Reorganization Order for your consideration.

I have already mentioned that I will be abolishing the Department of Tourism and State Development, and elevating into the cabinet the Governor's Office of Economic Development, the Department of Tourism, and the Department of Tribal Relations. Each of these interests deserves a seat at the cabinet table.

In addition, I will be moving most of the business regulatory functions from the current Department of Revenue and Regulation into the Department of Labor. I believe that these regulatory functions, such as Banking, Insurance, and Securities, fit more closely with the current Labor Department, which already includes workers compensation, unemployment, and many professional boards and commissions. Making this change will also allow the Department of Revenue to be more focused upon its core function of collecting tax dollars owed to our state.

I will also be moving the three behavioral health divisions from the Department of Human Services to the Department of Social Services. These three divisions are funded heavily by Medicaid, which is administered by Social Services. I am hopeful that this realignment will allow Social Services to work with these agencies to find efficiencies and save Medicaid dollars.

Finally, I will be splitting the current Department of Military and Veterans' Affairs into two cabinet-level departments. The Department of the Military will be led by the Adjutant General and will oversee the South Dakota National Guard. The Department of Veterans Affairs will oversee our Veterans benefits and programs, including the state veterans' home.

Creating separate Departments for the Military and for Veterans Affairs will allow the Adjutant General to focus on leading an increasingly active National Guard, while allowing the Secretary of Veterans Affairs to ensure that we always meet our obligations to our veterans.

Over the past few years, it has been my honor to serve on the board of the South Dakota Honor Flight program. This program charters planes to fly South Dakota's WWII veterans to Washington DC to see their memorial. It was a privilege to be associated with Honor Flight and to meet many of these heroes, now in the twilight of their lives, who fought so valiantly to protect our world from Fascism and Communism. Today's foreign struggles are creating a new generation of heroes, who have put their lives on the line to protect our freedoms. We owe them our thanks and our strong support. **Please join me in thanking them at this time.**

REORGANIZATION OF THE GOVERNOR'S OFFICE

Beyond the cabinet changes, I have also reorganized the Governor's Office. In most governors' offices, in South Dakota and around the nation, the governor employs a single Chief of Staff. I have opted instead to have six officials reporting directly to me as an Executive Committee. These six people will divide up the traditional duties of the Chief of Staff, and will also assume many other responsibilities.

One key member of that team is our lieutenant governor. Matt Michels is one of the most impressive people I've ever met. He came from a single-parent home and worked his way through school. He served his country in the United States Navy. He graduated from law school and is one of our state's leading attorneys in healthcare law. He was a brilliant legislator and a two-term Speaker of the House. And most importantly, Matt is a family man with a great wife and son.

Having Matt Michels as a full-time Lieutenant Governor is a great asset for the people of South Dakota. He will be working with me, every day, to make our state a better place. And if something happens to me, Matt will be ready to lead our state as Governor.

The elevation of the lieutenant governor to full-time, and other organizational changes I have made, does not add “another layer of bureaucracy.” These changes have not added additional expense or employees. My governor’s office will have the same number of positions as the previous administration. But by reshuffling duties and personnel dollars, we have cut the Governor’s Office payroll by more than ten percent, effective yesterday.

STATE BUDGET

I would like to say a few words about the state budget. I will be introducing several bills on behalf of the Bureau of Finance and Management that are necessary to implement my budget proposal. This will include special appropriations bills to fund the omnibus water bill and our obligations under the physician tuition reimbursement program. There will also be a number of other, more technical bills that I will discuss with you next week.

Beyond legislation, I will be working with my cabinet this year to find ways to make government more efficient and to save money. One area that I would like to revisit is state travel – the motor fleet and the airplane fleet. I know that studies have been done in the past, but austerity measures currently in place have limited the amount of travel that is being done. I will be asking the Department of Transportation to undertake a comprehensive study of usage, both of our auto fleet and our airplane fleet, to determine whether we need all we have.

As my last words about the budget today, I would like to say something about the principles that guided me as I crafted the budget proposal I will present next week. As a first principle, I am committed to eliminating the structural deficit. A structural deficit exists when ongoing spending exceeds ongoing revenue. Let me emphasize that definition, because clear communication depends upon a mutual understanding of language. A structural deficit exists when ongoing spending exceeds ongoing revenue. One-time revenue items do not enter into the calculation. Neither do one-time expenses.

Over the past few years, we have had an increasing structural deficit, not because of mismanagement, but because of the national recession. Our ongoing revenues fell in FY09, fell further in FY10 and although they are now turning around, ongoing revenues for this fiscal year, ending in June, are still expected to be below Fiscal Year 2008 ongoing revenues. Even as our ongoing revenues were falling, our ongoing expenses were growing. To fill the gap, the federal government gave us money, but as a condition, we were forbidden to cut spending in most areas. This denied us the freedom to address our structural deficit in a meaningful way. That money will be gone in FY12, and we must now confront our condition. I am committed to eliminating the structural deficit.

As a second principle, we must not use one-time dollars to perpetuate overspending – because that only “kicks the can down the road.” It defers the problem to another year. One-time money should be used only for one-time costs. Reserves should be used only for unexpected needs.

The budget I propose next week will meet our goals within these principles. My budget proposal will clearly demonstrate, to you and to the people of South Dakota, that if we truly want to balance our budget without raising taxes, as I do, we must be prepared to make some very difficult decisions.

I intend to lead by example. The agencies under the control of the governor will be cut by at least ten percent. The governor’s office will be cut ten percent overall. Every member of my cabinet has agreed to cut his or her salary by at least ten percent. And I will be cutting my own salary by fifteen percent.

It is my duty as Governor to begin the budget discussion with a proposal. I do not claim that my proposal is **THE** plan. It is **A** plan. I look forward to an open and honest dialogue – with you and with the people of South Dakota – about this proposal. I am willing to reconsider the details of the budget I present – but I am committed to the principle goal of a structurally balanced budget.

During session, the halls of our Capitol are filled with those who represent the many interest groups of our state. These are good people and they have a job to do – to advocate for their employers. It is important that someone fills that role.

But we who have been elected must remember that there is another interest group who is not so well-organized. They are the taxpayers who elected us to come to Pierre. We are here to represent all of South Dakota – the tax-PAYERS as well as the tax-SPENDERS. The taxpayers ask that we look at the big picture – that we take the long view – and that we spend their hard-earned tax dollars responsibly and provide government services efficiently. As Governor, I will put taxpayers first, and I will make sure that their voice is never forgotten.

CONCLUSION

Let me close, now, with a little history. Every year, our legislature opens its session by inviting the Governor to report on the State of the State. It was exactly 100 years ago last week, on January 3, 1911, that the legislature convened for the very first time in the brand-new State Capitol Building to listen to the Governor's State of the State address. The governor that day discussed many of the same issues that we still debate and discuss: the budget, education, agriculture, state institutions, law enforcement, and transportation.

This governor had been elected in 1908 and had won his second term by a margin of more than twenty percent. Yet, I would venture to guess that almost no one in this state, myself included, would be able to recall the name of that Governor if asked.

And, you see, that's the point. A century from now, Governor Dennis Daugaard will be as forgotten as Governor Robert S. Vessey. Let us seek to be remembered for our deeds, not our names.

We all stand on the shoulders of those who came before us. I invite all of you to join me this year as we seek to Build a Stronger South Dakota. There will be times when we disagree, but if we can agree on the facts and set politics aside, there is much that we can accomplish. It is amazing what you can do if you don't care who gets the credit. Let us stand tall, together, so that the generations who follow us may live in a stronger, freer, better South Dakota.

Thank you so much.