



VIRGINIA BOARD OF EDUCATION

AGENDA ITEM

Agenda Item: H

Date: September 15, 2022

Title: First Review of Guidelines for Implementing New Appropriation Act Provisions for Literary Fund School Construction Loans in the 2022-2024 Biennium

Presenter: Kent C. Dickey, Deputy Superintendent of Budget, Finance, and Operations

Email: kent.dickey@doe.virginia.gov

Phone: (804) 225-2025

Purpose of Presentation:

Action required by state or federal law or regulation

Executive Summary

The 2022 Appropriation Act (i.e., Chapter 2 budget) enacted for the 2022-2024 biennium includes substantial support for local school construction and renovation through two grant programs as well as authorization to issue school construction loans from the state's Literary Fund. The 2022-2024 appropriation act also includes several new budget language provisions impacting the application process and award of Literary Fund school construction loans. Item 137, Paragraph C.11 of the 2022 Appropriation Act for the 2022-2024 biennium, includes the following provisions related to Literary Fund school construction loans:

- Language authorizing the Board to offer up to \$200,000,000 in fiscal year (FY) 2023 and up to \$200,000,000 in FY 2024 from the Literary Fund for school construction loans, subject to the availability of funds. Amounts designated for school construction loans that are not obligated in FY 2023 may be obligated in FY 2024;
- Establishing an annual open enrollment process by which localities and school boards apply to the Literary Fund for school construction loans, in lieu of the First Priority and Second Priority waiting list process for awarding loans. Priority for loan funding is based on the local composite index of ability-to-pay (but the Board may consider other critical projects for priority);

- Establishing a maximum Literary Fund loan amount per project of \$25.0 million (from \$7.5 million currently authorized in the *Code of Virginia*);
- In consultation with the Department of the Treasury, establishing loan interest rates that are benchmarked to a market index interest rate on an annual basis, not to exceed 2.0 percent for the tier of localities with a school division local composite index of ability-to-pay between 0.0000 and 0.2999; and
- Language authorizing the Board to offer a loan add-on amount not to exceed \$5.0 million per loan for projects that will result in school consolidation and the net reduction of at least one existing school.

[Senate Bill 471](#) (McClellan), which was signed by the Governor on August 4th, includes similar provisions for Literary Fund loans as the 2022 Appropriation Act provisions listed above. However, there is a delayed enactment of SB471 of four months following the adjournment of 2022 Special Session I, which is still in session. SB471 also requires the Board to amend its Literary Fund regulations to implement the provisions of the bill.

As the Virginia Board of Education (Board) is responsible for management of the Literary Fund and awarding of school construction loans from the Fund, these proposed guidelines are intended to facilitate implementation of the new appropriation act provisions (and eventually the similar provisions in SB471) impacting the application for and awarding of Literary Fund school construction loans during the 2022-2024 biennium. The Virginia Department of the Treasury, which serves as accountant for the Literary Fund, was consulted in the development of the proposed guidelines. Treasury and VDOE staff collaborated on the overall content of the proposed guidelines, with Treasury staff providing specific recommendations for implementing a market index interest rate as a benchmark for establishing Literary Fund loan interest rates.

Notwithstanding the forthcoming enactment of SB471, if subsequent legislative action on the state budget during the 2022-2024 biennium results in substantive revisions to language provisions affecting Literary Fund loans, the guidelines will be updated accordingly and presented to the Board for review and approval. These guidelines will remain in effect initially for the 2022-2024 biennium, and then for future biennium if the new budget language provisions affecting Literary Fund school construction loans are continued in future biennial budgets.

This item aligns with Priority 1 of the Board's Comprehensive Plan: 2018-2023 to provide high-quality, effective learning environments for all students.

Action Requested:

Final review: Action requested at this meeting.

Superintendent's Recommendation

The Superintendent of Public Instruction recommends that the Board of Education waive First Review and approve the *Guidelines for Implementing New Appropriation Act Provisions for Literary Fund School Construction Loans in the 2022-2024 Biennium*.

Rationale for Action:

The 2022 Appropriation Act includes new budget language provisions impacting the application process for and award of Literary Fund school construction loans. The proposed guidelines are intended to facilitate implementation of these enacted appropriation act provisions. It is recommended that the Board waive first review and approve the proposed guidelines so that Department staff may proceed more quickly with implementing the new open enrollment application process for loans authorized in the current Chapter 2 budget.

Previous Review or Action:

No previous review or action.

Background Information and Statutory Authority:

The Literary Fund provides low-interest loans for school construction and renovation to help provide students with a safe and secure environment in which to learn. In accordance with [Section 22.1-142 of the Code of Virginia](#), the Board is responsible for the management of the Literary Fund.

The Literary Fund is authorized under [Article VIII, Section 8 of the Constitution of Virginia](#) as a permanent and perpetual school fund to be used for public school purposes. Certain revenue sources are dedicated to the Literary Fund, such as escheated property, property forfeited to the Commonwealth, fines for offenses committed against the Commonwealth, and annual interest on the Literary Fund. A minimum asset balance of \$80.0 million must be maintained in the Fund. [Title 22.1, Chapter 10 of the Code of Virginia](#), [Chapter 100 of the Virginia Administrative Code \(Regulations Governing Literary Loan Applications in Virginia\)](#), and provisions in the state appropriation act further govern the Literary Fund and its uses.

The *Code of Virginia* and Board regulations in the *Virginia Administrative Code* establish public school construction and renovation through revolving loans as a primary purpose of the Literary Fund. The state appropriation act further authorizes the Board to issue loans from the Literary Fund to local school boards that apply for loans, authorized by the locality and the school board, for the purposes of a) erecting, altering, or enlarging school buildings in local school divisions, or b) refinancing prior indebtedness incurred by a locality on behalf of a school division which has an application for a Literary Fund loan for an approved school project pending before the Board.

The Virginia Department of the Treasury, which serves as accountant for the Literary Fund, was consulted in the development of the proposed guidelines that are needed to help facilitate implementation of the new appropriation act provisions affecting school construction loans from the Literary Fund.

The provisions in SB 471 which are similar to those in the 2022 Appropriation Act will be effective once SB 471 is enacted (four months following adjournment of 2022 Special Session I). In addition, SB 471 requires the provisions of the bill to be implemented in regulation so a future regulatory action will need to be initiated.

Timetable for Further Review/Action:

If First Review is waived and the guidelines are approved, there will be no additional action required of the Board. Upon approval of the guidelines, the guidelines will be posted on the Town Hall website for a 30-day public comment period, pursuant to the Administrative Process Act. Any submitted public comments will be reviewed and considered for inclusion in the final guidelines. Subsequent to finalizing the guidelines document, a Superintendent’s Memorandum will be issued to communicate the guidelines to local school divisions, as well as the initial open enrollment application process to apply for a Literary Fund school construction loan from the Board.

Impact on Fiscal and Human Resources:

It is projected that completion and implementation of the guidelines can be absorbed with existing Department of Education fiscal and staff resources. It is projected that implementation of the guidelines by school divisions can also be absorbed with existing fiscal and staff resources.



Guidelines for Implementing New Appropriation Act Provisions for Literary Fund School Construction Loans in the 2022-2024 Biennium

PURSUANT TO ITEM 137, PARAGRAPH C.11.,
2022 APPROPRIATION ACT (i.e., CHAPTER 2)

VIRGINIA BOARD OF EDUCATION

BACKGROUND

The Literary Fund is authorized under Article VIII, Section 8 of the *Constitution of Virginia* as a permanent and perpetual school fund to be used for public school purposes. Certain revenue sources are dedicated to the Literary Fund, primarily escheated property, property forfeited to the Commonwealth, fines for offenses committed against the Commonwealth, and annual interest on the Literary Fund. A minimum asset balance of \$80.0 million must be maintained in the Fund. Title 22.1, Chapter 10, *Code of Virginia*, Chapter 100 of the *Virginia Administrative Code*, and provisions in the state appropriation act further govern the Literary Fund and its uses. The Board of Education (“Board”) is responsible for administering the Literary Fund; the Department of the Treasury serves as accountant for the Fund.

The *Code of Virginia* and regulations of the Board in the *Virginia Administrative Code* establish public school construction and renovation through revolving loans as a primary purpose of the Literary Fund. The state appropriation act further authorizes the Board to issue loans from the Literary Fund to the school boards of local school divisions that apply for loans, authorized by the locality and the school board, for the purposes of a) erecting, altering, or enlarging school buildings in local school divisions, or b) refinancing prior indebtedness or obligations incurred by a locality on behalf of a school division which has an application for a Literary Fund loan for an approved school project pending before the Board.

Several new budget language provisions impacting Literary Fund school construction loans were enacted in Item 137, Paragraph C.11 of the 2022 Appropriation Act (i.e., Chapter 2) for the 2022-2024 biennium, as follows:

- Language authorizing the Board to offer up to \$200,000,000 in fiscal year (FY) 2023 and up to \$200,000,000 in FY 2024 from the Literary Fund for school construction loans, subject to the availability of funds. Amounts designated for school construction loans that are not obligated in FY 2023 may be obligated in FY 2024;
- Establish an annual open enrollment process by which localities and school boards apply to the Literary Fund for school construction loans, replacing the First Priority and Second Priority waiting lists for awarding loans. Priority for loan funding is based on the local composite index of ability-to-pay (but the Board may consider other critical projects for priority);
- Establish a maximum Literary Fund loan amount per project of \$25.0 million (from \$7.5 million currently authorized in the *Code of Virginia*);
- In consultation with the Department of the Treasury, establish loan interest rates that are benchmarked to a market index interest rate on an annual basis, not to exceed 2.0 percent for the tier of localities with a school division local composite index of ability-to-pay between 0.0000 and 0.2999; and
- Language authorizing the Board to offer a loan add-on not to exceed \$5.0 million per loan for projects that will result in school consolidation and the net reduction of at least one existing school.

APPLICABILITY OF THE GUIDELINES

The new appropriation act provisions summarized above, and which are the basis for these guidelines, override any conflicting *Code of Virginia* and *Virginia Administrative Code* provisions related to Literary Fund school construction loans. Where there is no conflict, existing *Code of Virginia* and *Virginia Administrative Code* provisions related to Literary Fund school construction loans remain in effect.

These guidelines facilitate implementation of the new appropriation act provisions impacting Literary Fund school construction loans during the 2022-2024 biennium. If subsequent legislative action on the state budget during the biennium results in substantive revisions to language provisions affecting Literary Fund loans, the guidelines will be updated accordingly and presented to the Board for review and approval. These guidelines will remain in effect initially for the 2022-2024 biennium, and then for future biennium if the new budget language provisions affecting Literary Fund school construction loans are continued in future biennial appropriation acts.

GUIDELINES FOR IMPLEMENTING THE NEW 2022-2024 APPROPRIATION ACT PROVISIONS FOR LITERARY FUND SCHOOL CONSTRUCTION LOANS

FUNDS AVAILABILITY FOR LOANS

As authorized in the Chapter 2 budget, the Board may offer up to \$200,000,000 in FY 2023 and up to \$200,000,000 in FY 2024 from the Literary Fund for school construction loans, subject to the availability of funds. Amounts designated for school construction loans that are not obligated in FY 2023 may be obligated in FY 2024. Before any loan is awarded by the Board for an approved school project during FY 2023 or FY 2024, Department of Education (“Department”) staff will confirm the availability of unobligated balances in the Literary Fund sufficient to fund the approved loan request.

ANNUAL OPEN ENROLLMENT APPLICATION PROCESS

Localities and local school boards may submit applications for school construction loans from the Literary Fund during an annual open enrollment process. Effective July 1, 2022, the Literary Fund First Priority and Second Priority waiting lists are no longer used to prioritize award of loans for approved applications.

The annual open enrollment process is announced by the Department to school divisions through a Superintendent’s Memorandum at a time determined by the Department, including establishing the specific beginning and end dates of the open enrollment application period. Literary Fund loan applications not submitted by the established open enrollment period deadline may be disqualified from consideration. The Department will prioritize conducting the open enrollment process as early as possible each fiscal year. School divisions will use an online application form

to apply for loans during the open enrollment period, which may be downloaded from the Department's Literary Fund webpage at: [Literary Fund Application Form Webpage](#).

After the open enrollment application period has closed, approvable loan applications are considered by the Board for funding. All statutory and regulatory requirements must be met for an application to be considered for loan funding. Priority for funding is based primarily on the local composite index of ability-to-pay of the applying school divisions. After the Department review period is completed, a Board meeting agenda item is created identifying recommended applications for loan funding, subject to availability of funding. School construction loans are awarded by the Board through a Board action item at a monthly business meeting of the Board.

The Board may also consider other critical school projects submitted during the open enrollment process to receive priority for loan funding if the Board finds that a critical need exists related to the project and such prioritization is justified. Reasons for such prioritization may include, but are not limited to: (i) hazardous materials or substances containment or removal or other environmental health factors, (ii) significant building safety issues or structural defects, (iii) effects of natural disasters, and (iv) unique circumstances that may be detrimental to education in the absence of a Literary Fund loan. Such prioritization shall be acted on by the Board on an individual application basis when all requirements for release of a Literary Fund loan have been met by the school division.

MAXIMUM LOAN AMOUNT PER PROJECT

The maximum Literary Fund loan amount per project that may be applied for during the open enrollment period is \$25.0 million, subject to available funding and Board review and approval. The Board may reduce loan requests for final approval if the sum of approvable requests exceeds available funding or in order to provide equitable loan funding for projects with similar circumstances and needs.

BENCHMARKING LOAN RATES TO A MARKET INDEX

Department staff will consult with the Department of the Treasury staff to establish loan interest rates that are benchmarked to a market index on an annual basis, but not to exceed 2.0 percent interest for the tier of localities with a school division local composite index of ability-to-pay between 0.0000 and 0.2999.

Following Department staff consultation with the Department of the Treasury, the annual market index benchmark rate established is the 20-year BVAL Callable Municipal Curve ("BVAL Callable") rate (source: Bloomberg). This rate is based on callable AAA-rated securities in the municipal bond market. The 20-year BVAL Callable rate aligns to the 20-year term for most Literary Fund loans, and the use of callable securities (i.e., those that can be redeemed or paid off prior to their maturity date) in the benchmark aligns to the early payoff feature allowed for Literary Fund loans.

The 20-year BVAL Callable rate is produced and listed hourly. Since the Chapter 2 budget language directs that Literary Fund loan interest rates be "benchmarking to a market index on an annual basis," the latest 20-year BVAL Callable hourly rate practically available at the time the Superintendent's Memorandum announcing each open enrollment application period is posted

will be used as the annual market index benchmark rate for Literary Fund loans awarded and closed for that open enrollment application cycle.

The primary purpose of the Literary Fund is to provide accessible, low cost financing for public school construction and renovation projects based on local need and available resources. In addition, current Board regulations at 8VAC20-100-140 allow for interest rates on Literary Fund loans of between 2.0 and 6.0 percent based on the local composite index of ability-to-pay. Further, new appropriation act language specifically allows for a 2.0 percent interest rate cap on loans for localities with the lowest composite indices (i.e., up to 0.2999). These rate provisions are used in combination with the annual market index benchmark rate in establishing the interest rate structure to be used for awarded loans.

For Literary Fund loan applications submitted during the annual open enrollment process and approved by the Board to receive a loan, the interest rate on the loan is based on the lesser of the annual market index benchmark rate or the rates provided under current Board regulation as determined by the composite index of ability-to-pay, as shown below:

Locality Composite Index Range:	Eligible Interest Rate = <u>LESSER</u> of 20-year BVAL Callable Rate Used or:
Composite Index between 0.0000 and 0.2999	2.0 percent
Composite Index between 0.3000 and 0.3999	3.0 percent
Composite Index between 0.4000 and 0.4999	4.0 percent
Composite Index between 0.5000 and 0.5999	5.0 percent
Composite Index between 0.6000 and 0.8000	6.0 percent

In the event that the 20-year BVAL Callable rate is not available or is discontinued, the MMD AAA Curve (produced by Municipal Market Data, another municipal security-based rate) will serve as the secondary annual market index benchmark rate.

LOAN ADD-ON AMOUNT FOR SCHOOL CONSOLIDATIONS

Subject to available funding, the Board may offer a loan add-on not to exceed \$5.0 million per loan for projects that will result in school consolidation and the net reduction of at least one existing school. The Board may also approve loan amount add-ons for less than \$5.0 million. When such loan add-ons are approved, the Board may require subsequent reporting by school divisions to ensure that the school consolidation action resulting in at least one net school closure did occur as part of the funded project.