



VIRGINIA DEPARTMENT OF EDUCATION

BRIEFING

STATUS REPORT ON THE LITERARY FUND

PRESENTED TO
SENATE FINANCE
SUBCOMMITTEE ON EDUCATION

JANUARY 25, 2007

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Background

- The Literary Fund is a permanent and perpetual school fund that began in 1810 and was later established in the Constitution of Virginia.

- Revenues to the Literary Fund are derived primarily from criminal fines, fees, and forfeitures, unclaimed and escheated property, and repayments of prior Literary Fund loans. The most recent addition to the sources of Literary Fund revenues is the transfer of unclaimed lottery winnings.

- In fiscal year 2006, total revenues were \$219.3 million. The revenue sources were:
 - \$69.2 million from fines, fees, and forfeitures
 - \$44.8 million from Literary Fund repayments
 - \$85.0 million from unclaimed property
 - \$13.2 million from unclaimed lottery winnings
 - \$ 7.1 million in interest earnings

- The Literary Fund has typically been used to provide low-interest loans for school construction, grants under the interest rate subsidy program, debt service for technology notes funding, and to support the state's share of teacher retirement required by the Standards of Quality.

Terms of a Literary Fund Loan

- Current Board of Education regulations and statutory provisions provide that:
 - Literary Fund loans may be offered as a source of low-interest loans for the purpose of erecting, altering, or enlarging school buildings;
 - the maximum loan amount available for a single project is \$7.5 million;
 - the minimum loan amount is \$50,000;
 - the length of the loan may run from five to 20 years, but the majority of loans are made for 20 years;
 - the interest rate is based on the school division's composite index of local ability-to-pay.

- The interest rates are as follows:

<u>Composite Index</u>	<u>Interest Rate on Loan</u>
0.2999 and below	2%
From 0.3000 to 0.3999	3%
From 0.4000 to 0.4999	4%
From 0.5000 to 0.5999	5%
0.6000 and above	6%

- Loan applications are placed on a Literary Fund Waiting List in priority order.

Direct Literary Fund Loans Released by Fiscal Year

- Since fiscal year 1983, a total of \$916.4 million has been provided in direct Literary Fund loans to local school divisions. The chart below reflects the release of these loans by fiscal year.

Fiscal Year	Projects Funded
1983	\$41,917,922
1984	13,090,500
1985	40,425,600
1986	32,768,391
1987	64,951,999
1988	36,212,656
1989	68,865,889
1990	22,158,479
1991	16,374,400
1992	-0-
1993	-0-
1994	-0-
1995	23,186,074
1996	48,888,628
1997	67,163,679
1998	78,254,001
1999	111,271,391
2000	99,576,079
2001	117,794,506
2002	-0-
2003	-0-
2004	-0-
2005	-0-
2006	-0-
2007	33,500,000 ¹

¹Released by the Board of Education at the January 10, 2007, board meeting.

Literary Fund Transfers

The Constitution provides that, “*But so long as the principal of the Fund totals as much as eighty million dollars, the General Assembly may set aside all or any part of additional moneys received into its principal for public school purposes, including the teachers retirement fund.*”

- As of June 30, 2006, the principal of the Literary Fund was approximately \$466.3 million:
 - Cash and Investments - \$119.5 million
 - Outstanding Loans - \$346.8 million

- Transferring revenue from the Literary Fund for teacher retirement payments has been a standard practice at least since 1973. This action reduces the general fund appropriations needed for teacher retirement and thus makes the general fund revenues available for other purposes.

- Transfers from the Literary Fund for teacher retirement increased steadily over time with increases in Literary Fund revenue itself, reaching more than \$100 million in fiscal year 1992.

- With nearly 90% of all Literary Fund revenues transferred to teacher retirement in fiscal years 1992, 1993, and 1994, many projects waited more than two years to receive funding.

- No direct loans were made from the Literary Fund from January 1991 until April 1995.

Literary Fund Transfers (continued)

- Transfers for teacher retirement diminished in the last half of the 1990s and were eliminated in fiscal years 2000 and 2001.

- Since fiscal year 2002, the majority of the Literary Fund revenues have been transferred to pay teacher retirement in order to reduce the pressure placed on the general fund by growing costs in public education.

- In fiscal year 1999, a new type of transfer began when \$9.0 million was designated in the appropriation act for transfer from the Literary Fund to the School Construction Grants Program.

- This transfer amount was based on the estimated revenue from the unclaimed lottery prizes.

- The actual transfer in fiscal year 1999 was \$8.4 million.

- After fiscal year 1999, the following transfers were made:
 - Fiscal year 2000 - \$10.2 million
 - Fiscal year 2001 - \$ 8.2 million
 - Fiscal year 2002 - \$ 9.2 million

- These transfers were discontinued in the 2002-2004 biennium.

Literary Fund Transfer History - Since 1980

Since 1980, approximately \$1.6 billion (or 49.1%) has been transferred from Literary Fund revenues for teacher retirement or school construction.

(\$ in millions)

Fiscal Year	Total Revenues	Teacher Retirement Transfer	School Construction Transfer	Total Percent Transferred
1980	\$33.2	\$1.5		4.5%
1981	\$34.1	\$3.3		9.7%
1982	\$41.3	\$8.4		20.3%
1983	\$45.7	\$31.7		69.4%
1984	\$48.4	\$44.4		91.7%
1985	\$51.1	\$10.0		19.6%
1986	\$58.8	\$22.0		37.4%
1987	\$64.4	\$15.0		23.3%
1988	\$67.8	\$32.1		47.3%
1989	\$80.1	\$10.0		12.5%
1990	\$85.1	\$60.0		70.5%
1991	\$102.1	\$36.8		36.0%
1992	\$102.8	\$101.1		98.3%
1993	\$100.9	\$84.5		83.7%
1994	\$101.5	\$93.9		92.5%
1995	\$119.0	\$82.3		69.2%
1996	\$108.6	\$35.0		32.2%
1997	\$124.1	\$41.1		33.1%
1998	\$127.0	\$15.5		12.2%
1999	\$140.3	\$7.8	\$8.4	11.5%
2000	\$138.6	\$0	\$10.2	7.4%
2001	\$162.0	\$0	\$8.2	5.1%
2002	\$154.2	\$110.0	\$9.2	77.3%
2003	\$166.5	\$112.8		67.7%
2004	\$209.1	\$118.5		56.7%
2005	\$215.7	\$131.9		61.1%
2006	\$219.3	\$125.9		57.4%
2007 - estimate	\$200.2	\$115.9		57.9%
2008 - estimate	\$187.0	\$115.9		62.0%

Literary Funds Used for Technology

- Beginning in 1988, Literary Fund revenues were used as a mechanism to finance the purchase of computers and related technology.

- Technology initiatives have been funded and/or authorized through the issuance of equipment notes through the Virginia Public School Authority with the debt service paid by the Literary Fund.
 - The 1988 initiative focused on computers to assist with remediation instruction in middle schools and distance learning equipment.

 - The 1990 initiative continued implementation of remediation and distance learning efforts at the middle school level and provided funding for statewide administrative computing efforts.

 - The 1995 initiative provided a core level of computer capabilities and access to information in every elementary school (complementing efforts at the middle and high school levels funded in the prior session from the general fund) and began networking efforts.

 - Throughout most of the late 1990s, initiatives have focused on three main components of the Six-Year Plan for Technology: (1) retrofitting and upgrading existing school buildings to use educational technology; (2) providing net-work ready multimedia microcomputers for use at the classroom level; and (3) providing a 5 to 1 ratio of pupils to network-ready computers.

Literary Funds Used for Technology (continued)

- The 1999 General Assembly authorized a Literary Fund notes program to replace the outdated administrative and student information software that was being used by many school divisions.
- Most recently, the notes issues since fiscal year 2001 have been dedicated to, "...improve the instructional, remedial, and testing capabilities of the Standards of Learning for local school divisions."
- To date, approximately \$335.4 million in VPSA bonds have been issued to support this most recent initiative. During the current fiscal year (2007), approximately \$58.7 million in additional notes proceeds will be made available to school divisions for this initiative.

Interest Rate Subsidy Program

- Given the level of transfers for teacher retirement, the General Assembly authorized a program of “interest rate subsidies” in order to provide maximum funding for school construction projects beginning in fiscal year 1989.
- The purpose of the program is to fund construction loan projects that are currently on the Literary Fund’s First Priority Waiting List through the Virginia Public School Authority.
- Funds are granted from the Literary Fund for each project to reduce the principal amount of debt financed in a manner that produces debt service payments equivalent to what the school division would have paid for a direct Literary Fund loan.
- Based on the level of market rates at the time of a subsidy sale and the rate of interest charged to localities through the Literary Fund, subsidy programs have funded an average of \$5.80 of projects for every \$1 of Literary Fund revenue paid as grants. As grants, the subsidy payments are not paid back to the Literary Fund.

Interest Rate Subsidy Program (continued)

The following is a summary of the total projects funded and costs to the Literary Fund for the subsidy program.

Fall of Calendar Year	Value of Projects Funded	Total Cost to the Literary Fund	Ratio of Projects Funded to Literary Fund Cost
1988	\$23,757,500	\$8,446,500	2.8
1990	43,405,770	11,033,560	3.9
1991	106,806,799	27,898,774	3.8
1992	42,872,037	10,611,971	4.0
1994	40,689,574	10,069,683	4.0
1995	64,733,441	12,266,988	5.3
1996	43,675,000	8,652,972	5.0
1997	59,795,100	9,963,749	6.0
1998	42,978,700	5,596,579	7.7
1999	51,811,589	9,967,509	5.2
2000	102,923,607	18,824,375	5.5
2001	104,628,220	11,324,309	9.2
2002	51,082,187	5,000,000	10.2
2003	35,253,087	2,921,438	12.1
2004	37,352,634	4,870,341	7.7
2005	133,084,594	14,889,363	8.9
2006	105,733,159	14,524,145	7.3
Total	\$1,090,582,998	\$186,862,256	
		Average Ratio	5.8

Current Status of the Literary Fund

- As of January 2007, the First Priority Waiting List consisted of 30 projects totaling \$131.6 million (see Attachment A).
- The project that has been on the First Priority Waiting List for the longest period of time was placed there in January 2005.
- In fiscal year 2007, revenues are estimated to be \$200.2 million. These revenues will be added to \$107.4 million of unspent revenues from fiscal year 2006.
- These funds are programmed to be used in the following manner pursuant to the provisions of the appropriation act:
 - \$115.9 million will be transferred for teacher retirement;
 - \$62.6 million will be used to pay debt service on the technology equipment notes;
 - \$14.5 million was used for an interest rate subsidy program; and,
 - \$33.5 million will be available to issue direct loans.
 - Total = \$226.5 million

Current Status of the Literary Fund (continued)

- In fiscal year 2008, revenues are estimated to be \$187.0 million. These revenues will be added to \$81.1 million of anticipated unspent revenues from fiscal year 2007.

- These funds are programmed to be used in the following manner pursuant to the provisions of the appropriation act:
 - \$115.9 million will be transferred for teacher retirement;

 - \$63.8 million will be used to pay debt service on the technology equipment notes; and,

 - \$20.0 million will be used for an interest rate subsidy program.

 - Total = \$199.7 million

- It is not anticipated that any funds will be available to issue direct loans in fiscal year 2008 because planned expenditures exceed projected revenue in fiscal year 2008 by approximately \$13 million. Maintaining expenditures from the Literary Fund at current levels over the next several years would exceed projected revenues each year and reduce the principal balance of the fund.

Proposed Budget Language Amendments

- The Governor's introduced amendments to the 2006-2008 biennial budget (SB 750) include the following two language amendments impacting the Literary Fund:
 - Flexibility in Seasonality Requirements of the Literary Fund Interest Rate Subsidy Program - This language amendment eliminates the seasonality requirements for the interest rate subsidy sale and allows for a fall and spring subsidy sale to utilize any balance in the annual subsidy appropriation remaining after the fall subsidy sale.
 - Allow Participation of Literary Fund Second Priority Waiting List Projects in the Literary Fund Interest Rate Subsidy Program - This language amendment would allow projects on the Literary Fund Second Priority Waiting List to participate in the Literary Fund Interest Rate Subsidy Program if unused subsidy appropriation remains once the participation of projects on the Literary Fund First Priority Waiting List is confirmed.

(Applications placed on the Literary Fund Second Priority Waiting List represent school divisions having a composite index of .6000 or above, or an outstanding indebtedness [including the application considered for release of funds by the Board] to the Literary Fund greater than \$20 million.)

2007 Literary Fund Legislation

- **HB 2350** - Amends or deletes various sections of the *Code of Virginia* to streamline the process for applying and obtaining approval for a Literary Fund loan, and to secure governing body concurrence with incurring the loan debt.
 - Governing Body Sign-off - Requires school board applications for a Literary Fund loan to be signed by the chairman of the governing body and the chairman of the school board. The chairman of the governing body would be required to sign the loan incurring the debt along with the chairman of the school board.
 - Restrictions Upon Loans - Eliminates language requiring the Board of Education to determine whether the debt service on a requested Literary Fund loan would entail too heavy a charge upon the revenues of the locality and eliminates the requirement to record a memorandum of lien with the circuit court.
 - Examination of Title, Certification of Title, Approval by Attorney General, Lien Requirement - The following sections of the Code are recommended for deletion:
 - Section 22.1-154 - Requires the title to the real estate on which the building has been or will be erected to be examined and approved by the appropriate attorney.
 - Section 22.1-155 - Requires loan applications to include a certification by the clerk of the circuit court indicating where the title deed to the property is recorded, that the title has been examined and approved in writing by an attorney, and that the certificate of the attorney shows that the school board or governing body has a good and sufficient title in fee simple to the real estate.
 - Section 22.1-156 - Requires that the attorney's certification of title along with the application for the loan be submitted to the Attorney General for approval before the Board approves a loan.

2007 Literary Fund Legislation (continued)

Section 22.1-157 - States that a loan from the Literary Fund constitutes a lien on the building and additions for which the loan was made as well as the lots where the buildings are situated.

- Governing Body Approval - Adds language prohibiting the Board from disbursing any proceeds of an approved loan before its receipt of “the concurrent approval of the governing body at the time of initial disbursement...”
 - Bond Counsel Opinion - Eliminates the requirement for a bond council opinion on the tax-exempt status of the interest on Literary Fund loans under federal income tax laws. This change is proposed because currently there is no need to determine the tax-exempt status of Literary Fund loans in order for the Commonwealth to “securitize” its portfolio of Literary Fund loans in the market. A local bond counsel opinion on each Literary Fund loan would enable the state to ensure that the portfolio remains tax-exempt. However, there are currently no state financing programs in place or under consideration that would securitize the portfolio of Literary Fund loans.
 - General Obligation Debt - Specifically states that Literary Fund loans are general obligation debt of the governing body and are subject to state aid intercept (default recovery mechanism) and to provisions in the Public Finance Act stating that voter approval is not required to issue bonds which are sold to the Literary Fund.
- **HB 2473** - Amends § 22.1-147 of the *Code of Virginia* to raise the maximum limit for any loan from the Literary Fund from \$7.5 million to \$12 million.

2007 Literary Fund Legislation (continued)

- **SB 1075** - Increases the loan amount available to a school division that consolidates two or more existing schools into one new school building. It would permit the Board of Education to release a separate loan for each school being consolidated if a school division consolidates two or more existing schools into one new school building.

The current maximum limit for any loan from the Literary Fund is \$7.5 million. The proposed legislation would permit a school division to receive up to \$15 million if two existing schools were consolidated into one new building or more than \$15 million (multiples of up to \$7.5 million) if more than two existing schools were consolidated into one.

VIRGINIA BOARD OF EDUCATION - FIRST PRIORITY WAITING LIST

The following projects have been placed or are recommended for placement on the First Priority Waiting List with the actions as indicated in the last column. Projects recommended for action at this meeting are presented in italics.

Priority	Date Placed on Waiting List	School Division	School	Interest Rate	Amount	Cumulative Total	Action/Status
1	January, 2005	Campbell County	Yellow Branch Elementary ¹	2%	7,500,000	7,500,000	Funding Deferred
2	June, 2005	Staunton City	A. R. Ware Elem ¹	3%	7,500,000	15,000,000	Funding Deferred
3	June, 2005	Staunton City	T. C. McSwain Elem ¹	3%	7,500,000	22,500,000	Funding Deferred
4	June, 2005	Warren County	West Warren High ¹	3%	7,500,000	30,000,000	Funding Deferred
5	June, 2005	Warren County	East Warren High ¹	3%	7,500,000	37,500,000	Funding Deferred
6	March, 2006	Martinsville City	Patrick Henry Elementary ¹	2%	2,500,000	40,000,000	Funding Deferred
7	March, 2006	Waynesboro City	Kate Collins Middle	3%	7,500,000	47,500,000	Funding Deferred
8	March, 2006	Culpeper County	Culpeper County High ¹	3%	7,500,000	55,000,000	Funding Deferred
9	March, 2006	Augusta County	Stuarts Draft High School	3%	7,500,000	62,500,000	Funding Deferred
10	March, 2006	Augusta County	Wilson Memorial High School	3%	7,500,000	70,000,000	Funding Deferred
11	June, 2006	Dinwiddie County	New High School ¹	2%	7,500,000	77,500,000	Funding Deferred
12	June, 2006	Dinwiddie County	New Elementary School ¹	2%	7,500,000	85,000,000	Funding Deferred
13	June, 2006	Nottoway County	Nottoway Intermediate and Middle School ¹	2%	3,000,000	88,000,000	Funding Deferred
14	June, 2006	King George County	New High School ¹	3%	7,500,000	95,500,000	Funding Deferred
15	September, 2006	Caroline County	Ladysmith Elementary ¹	3%	7,500,000	103,000,000	Funding Deferred
16	September, 2006	Hanover County	Hanover Elementary ¹	4%	7,500,000	110,500,000	Funding Deferred

New projects to be added with funding deferred until funds are approved for release by separate action by the Board of Education

17	January, 2007	Washington County	Abingdon Elementary ¹	3%	1,211,924	111,711,924	Add / Funding Deferred
18	January, 2007	Washington County	High Point Elem ¹	3%	986,356	112,698,280	Add / Funding Deferred
19	January, 2007	Washington County	Valley Institute Elementary ¹	3%	735,613	113,433,893	Add / Funding Deferred
20	January, 2007	Washington County	E. B. Stanley Middle ¹	3%	931,273	114,365,166	Add / Funding Deferred
21	January, 2007	Essex County	Essex Intermediate School ¹	4%	7,500,000	121,865,166	Add / Funding Deferred
22	January, 2007	Patrick County	Blue Ridge Elementary School ¹	2%	151,618	122,016,784	Add / Funding Deferred

VIRGINIA BOARD OF EDUCATION - FIRST PRIORITY WAITING LIST

The following projects have been placed or are recommended for placement on the First Priority Waiting List with the actions as indicated in the last column. Projects recommended for action at this meeting are presented in italics.

Priority	Date Placed on Waiting List	School Division	School	Interest Rate	Amount	Cumulative Total	Action/Status
23	<i>January, 2007</i>	<i>Patrick County</i>	<i>Hardin Reynolds Memorial School ¹</i>	2%	105,406	122,122,190	<i>Add / Funding Deferred</i>
24	<i>January, 2007</i>	<i>Patrick County</i>	<i>Meadows of Dan Elementary ¹</i>	2%	105,217	122,227,407	<i>Add / Funding Deferred</i>
25	<i>January, 2007</i>	<i>Patrick County</i>	<i>Patrick County High School ¹</i>	2%	275,324	122,502,731	<i>Add / Funding Deferred</i>
26	<i>January, 2007</i>	<i>Patrick County</i>	<i>Patrick Springs Primary ¹</i>	2%	195,976	122,698,707	<i>Add / Funding Deferred</i>
27	<i>January, 2007</i>	<i>Patrick County</i>	<i>Stuart Elementary School ¹</i>	2%	304,878	123,003,585	<i>Add / Funding Deferred</i>
28	<i>January, 2007</i>	<i>Patrick County</i>	<i>Woolwine Elementary School ¹</i>	2%	361,581	123,365,166	<i>Add / Funding Deferred</i>
29	<i>January, 2007</i>	<i>Galax City</i>	<i>Galax High School ¹</i>	2%	4,750,000	128,115,166	<i>Add / Funding Deferred</i>
30	<i>January, 2007</i>	<i>Henry County</i>	<i>Drewry Mason Elementary ¹</i>	2%	3,500,000	131,615,166	<i>Add / Funding Deferred</i>

¹ Pending approval by the Attorney General's Office
January, 2007