

Budget Transmittal Letter for Fiscal Year 2021-22

May 11, 2021

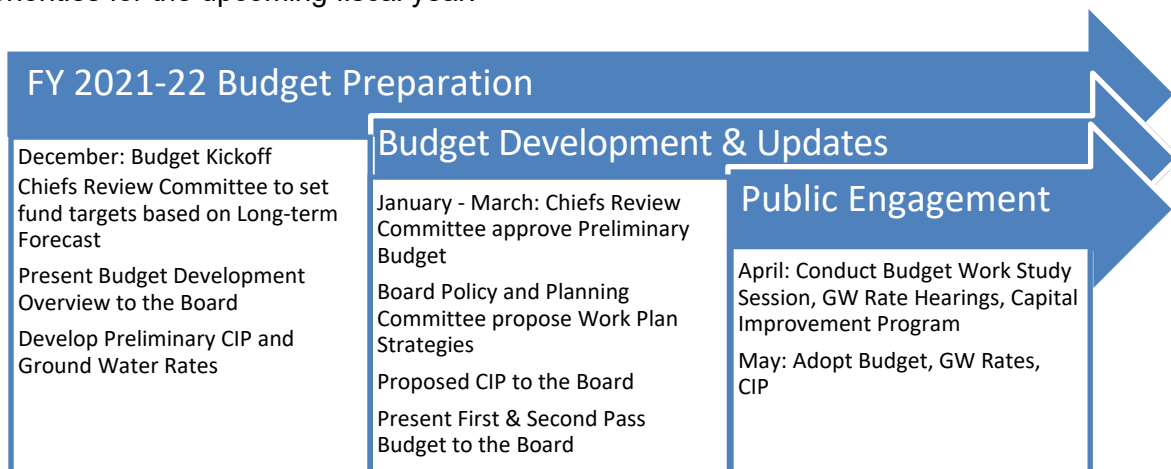
Honorable Members of the Board of Directors of the Santa Clara Valley Water District:

In accordance with Valley Water Policy, I am submitting the Fiscal Year 2021-22 (FY22) Budget for the Santa Clara Valley Water District (Valley Water). This budget represents Valley Water's mission of providing Silicon Valley safe, clean water for a healthy life, environment, and economy. This Budget also provides a comprehensive financial plan that includes a forecast of operating and non-operating revenues and expenditures; financing of long-term capital improvement plans to support infrastructure needs; and funding for the repayment of long-term debt. In FY22, Valley Water will focus on new water storage opportunities as well as advancing major water supply facilities such as Anderson Dam and leading efforts in recycled and purified water. Additionally, we will continue to promote water conservation as a way of life in Santa Clara County and equitably prioritize funding to protect and maintain our flood protection assets. In all focus areas we will continue to engage the community and not lose sight of our environmental stewardship goals such as a net positive impact on the environment. FY21 brought about unprecedented and challenging times but Valley Water will remain committed to providing Silicon Valley with safe, clean water for a healthy life, environment, and economy.

Financial Overview

The accounts of Valley Water are organized based on fund types and account groups. Each fund is an independent accounting entity with a self-balancing set of accounts comprised of its assets, liabilities, fund equity, revenue, and expenditures or expenses, as appropriate. Fund accounting allows government resources to be segregated and accounted for per their intended purposes, aiding management in demonstrating compliance with finance-related legal and contractual provisions.

The budget development process begins in December of each year and concludes on June 30, with the posting of the budget. The budget development process for FY 2021-22 includes several process improvements and numerous public hearings, as well as input from the Board on urgent priorities for the upcoming fiscal year.



Valley Water Priorities

In developing the budget, the Board directed its Board Policy and Planning Committee (Committee) to identify and summarize the Board's strategies. This budget is the culmination of the Committee's final recommendation, which ultimately resulted in Board action to accept and adopt the Committee's recommendation. In developing this budget, management identified where resources could shift and scrutinized additional funding requests that would help the organization achieve results.

This proposed budget demonstrates a fiscally responsible, balanced budget that meets the community's expectations of Valley Water. This budget was developed based on the Board's FY2021-22 Work Plan Strategies highlighted below:

1. Protect and maintain existing assets and infrastructure and advance new infrastructure projects
2. Pursue opportunities to improve internal capacity to acquire regulatory permits
3. Engage and educate the community, elected officials and staff on our management of water resources in Santa Clara County
4. Actively Pursue New Water Supply and Storage Opportunities
5. Actively Participate in decisions regarding the CA Delta Conveyance
6. Lead Recycled and Purified Water Efforts with committed partners
7. Advance Anderson Dam Seismic Retrofit Project
8. Promote Making Water Conservation a California Way of Life in Santa Clara County
9. Plan, design and maintain flood protection projects with multiple benefits, including protecting ecosystem functions and enhancing habitat
10. Provide flood protection equitably in all regions of the County, prioritizing disadvantaged communities
11. Attain net positive impact on the environment when implementing flood protection and water supply projects
12. Promote the protection of creeks, bay, and other aquatic ecosystems from threats of pollution and degradation
13. Continue the Fisheries and Aquatic Habitat Collaborative Effort (FAHCE)
14. Advance racial equity, diversity and inclusion
15. Maintain appropriate staffing levels and expertise and ensure the safety of our staff
16. Provide affordable and cost-effective level of services
17. Address future impacts of climate change to Valley Water's mission and operations

Valley Water is responding to these challenges in several ways, including expanded efforts possible with the proposed addition of 20 new positions and 1 fellowship discussed in detail in the following sections.

The organization will incorporate specific activities that address the Board's Work Plan Strategies and will periodically update the Board Policy and Planning Committee and the full Board throughout the fiscal year and bring adjustments back to the Board if needed.

Revenue

The FY 2021-22 Proposed Budget includes projected revenues of approximately \$539.4 million. These revenues are a net increase of \$32.8 million from the \$506.6 million included in the FY 2020-21 Adopted Budget. The increase is primarily derived from increases in water revenue (\$27.4 million), property taxes (\$15.5 million), benefit assessment revenues (\$1.1 million), special parcel tax (\$1.6 million), and offset by a decrease in capital reimbursement revenue (\$-8.5 million), and interest and other income (\$-4.3 million).

Appropriations/Outlays

Net total operating and capital outlays for the FY 2021-22 Proposed Budget is \$837.6 million, which includes \$71.3 million in debt service outlays. This figure does not include capital carry forward that was appropriated by the Board in prior years and is net of General Fund intra-district reimbursements and Internal Service Fund charges.

Net Operating Outlays

Net operating outlays for the FY 2021-22 Proposed Budget total \$354.2 million, an increase of \$42.3 million from the FY 2020-21 Adopted Budget. The increase in net outlays is primarily due to new essential worker positions, grants and partnerships funding, Conservation Program funding, purchase of additional water in response to emergency dry conditions, the cost to transfer water stored underground at the Semitropic Water Storage District in Central California to Santa Clara County, and initial implementation of a new partnership with Palo Alto and Mountain View to construct new recycled water facilities.

Net Capital Outlays

Net capital project appropriations total \$412.1 million in the FY 2021-22 Proposed Budget, an increase of \$176.3 million from the 2020-21 Adopted Budget. It is anticipated that \$52.1 million of the FY 2020-21 Adjusted Budget for capital projects also will carry forward into FY2021-22 at the close of the current fiscal year as most capital improvement projects will require multiple years to complete. The capital budget represents those projects that have been identified and prioritized in the Five-Year Capital Improvement Program (CIP).

Intra-district Reimbursements

The primary funding sources for the General Fund and Service Funds are intra-district reimbursements, totaling \$103.3 million in FY 2021-22. Intra-district charges reimburse the General Fund and Service Funds for functions such as finance, accounting, payroll, human resources, information technology, facilities, organizational leadership, and fleet management.

Other Financing Sources/Uses

Other financing sources include debt financing proceeds to fund capital projects. For FY 2021-22, Valley Water anticipates issuing approximately \$259.3 million in debt proceeds, of which \$159.3 million is to finance the Water Utility system infrastructure improvements and \$100 million is for Safe, Clean Water (SCW) capital projects.

Reserves

Valley Water reserves are comprised of Restricted Fund Balance reserves, Committed Fund Balance reserves and Assigned Fund Balance reserves. Within these categories are budgeted reserves and special purpose reserves, further detail is found in the FY 2021-22 Operating and Capital Budget document beginning on page 3–48. Overall, budgeted reserves for Fiscal Year 2021-22 are expected to decrease \$12.9 million to a total of \$336.3 million. The decrease is primarily due to increased capital project appropriations in FY2021-22.

(\$ in Thousands)	Budgetary Basis Actual 2019-20	Adopted Budget 2020-21	Projected	Proposed	Change from 2020-21	
			Year End	Budget	\$ Diff	% Diff
			2020-21	2021-22		
Restricted Reserves						
Safe, Clean Water & Natural Flood Protection Fund	153,384	80,381	105,177	123,854	43,473	54%↑
Water Enterprise Funds	81,582	59,126	63,770	60,107	981	2%↑
Subtotal	234,966	139,507	168,947	183,961	44,454	32%↑

Committed Reserves

General Fund	8,235	5,733	5,794	6,576	843	15%↑
Watershed Stream Stewardship Fund	161,629	115,513	92,591	74,324	(41,189)	(36%)↓
Water Enterprise Funds	86,770	71,380	141,122	56,730	(14,650)	(21%)↓
Internal Service Funds	27,020	17,035	18,826	14,714	(2,321)	(14%)↓
Subtotal	283,654	209,661	258,333	152,344	(57,317)	(27%)↓
Grand Total	518,620	349,168	427,280	336,305	(12,863)	(4%)↓

Debt Overview

The FY 2021-22 debt portfolio total outstanding principal of \$746.9 million includes \$87 million for Watersheds and \$659.9 million for the Water Utility Enterprise. Annual debt service budget of \$71.3 million includes repayment of principal, interest and various banking and legal fees for the debt portfolio.

The long-term strategy is to issue short-term debt to provide just-in-time funding for eligible capital projects as actual expenditures are incurred. As the outstanding short-term debt obligations reach the program capacity, the outstanding short-term debt will be refunded with long-term debt to be repaid over 30 years. For the Water Utility Program, the issuance of long-term debt helps keep water charges stable over the long-term while ensuring inter-generational equity by matching the timing of the debt service repayment to the useful life of the asset and allowing for the completion of capital projects in a timely manner. The February 2021 Protection and Augmentation of Water Supplies report shows that Water Utility finances will be healthy despite the issuance of debt, assuming that forecasted water charge increases are implemented.

For the Safe, Clean Water Program, issuing debt allows the projects to be completed earlier as it bridges the timing difference between when the voter approved special parcel tax revenues are collected versus the desired project delivery schedule based on the Board approved CIP.

The Safe, Clean Water special parcel tax, approved by voters on November 3, 2020, authorized Valley Water to levy the special parcel tax with periodic Board review of the amount necessary to fund ongoing operations, maintenance and capital project costs planned under the SCW program.

The Santa Clara Valley Water District proactively manages its debt portfolio to ensure access to the public finance credit markets at the lowest available borrowing cost, preserve strong credit ratings, fulfill its fiduciary responsibility to its customers, and provide high quality water service, stream stewardship and flood protection at the lowest possible cost.

Bond Ratings

The bond ratings for Valley Water’s outstanding debt reflect high grade investment quality debt. They are based on Valley Waters positive fiscal policy and financial strengths. The bond ratings are either the highest for a water related governmental entity in the State of California or among the highest. Bonds issued at this credit rating result in lower interest rates and corresponding lower debt service payments.

Please see table below for ratings going into FY 2021-22.

	Water Utility		Watershed Debt
	Senior Debt	Parity Debt	
Moody's	Aa1	Aa1	Aa1
Standard & Poor's	AA-	N/A	AAA
Fitch	N/A	AA+	AA+

Staffing

The FY 2021-22 Proposed Budget includes 892 positions including, 879 regular positions, 8 limited term positions, and 5 fellowships. This includes funding for 20 new positions and one new fellowship. For a comprehensive schedule of district-wide salaries and benefits, please refer to the salaries & benefits in the “Financial Overview” section.

Regular Position Count by Organization Area

	Adjusted Budget 2019-20 ²	Adjusted Budget 2020-21 ³	Proposed Budget 2021-22	Change from 2020-21
Board Appointed Officers ¹	77	73	73	0
Office of Integrated Water Management	-	38	39	1
External Affairs	39	42	45	3
IT & Administrative Services	160	159	162	3
Water Utility	309	293	296	3
Watersheds	274	254	264	10
Districtwide	859	859	879	20

¹ Board Appointed Officers Include: Office of Chief Executive Office, District Counsel and Clerk of the Board.

² During FY 2019-20, the Board approved additional 17 positions to help strengthen critical core business functions.

³ In FY 2020-21, A new Office of Integrated Water Management was created. A new Racial Equity, Diversity and Inclusion Unit was created in External Affairs.

Future Outlook

The Governor of the State of California recently proclaimed a state of emergency due to severe drought conditions, that continue to worsen, in the state. At this point in time, California is in a more dire situation as compared to this point in time last year. Valley Water will continue to prioritize drought response and preparedness resources, increase resilience of our water supplies and systems, and ensure that the potential impacts of drought on communities are anticipated and proactively addressed. At the same time, it is important to maintain a long-term outlook given the major infrastructure investments planned for the next 10 years, such as Anderson Dam. Valley Water continues its ambitious capital program to help ensure a reliable and safe water supply. It is prudent fiscal policy to start planning for the future by acting now and prioritizing projects for future unknowns like drought and other natural disasters. Valley Water will remain committed to providing Silicon Valley with safe, clean water for a healthy life, environment, and economy.

Sincerely,

A handwritten signature in black ink, appearing to read "Rick Callender", with a long horizontal flourish extending to the right.

Rick Callender
Chief Executive Officer