

Budget Transmittal Letter for 2018-19

May 8, 2018

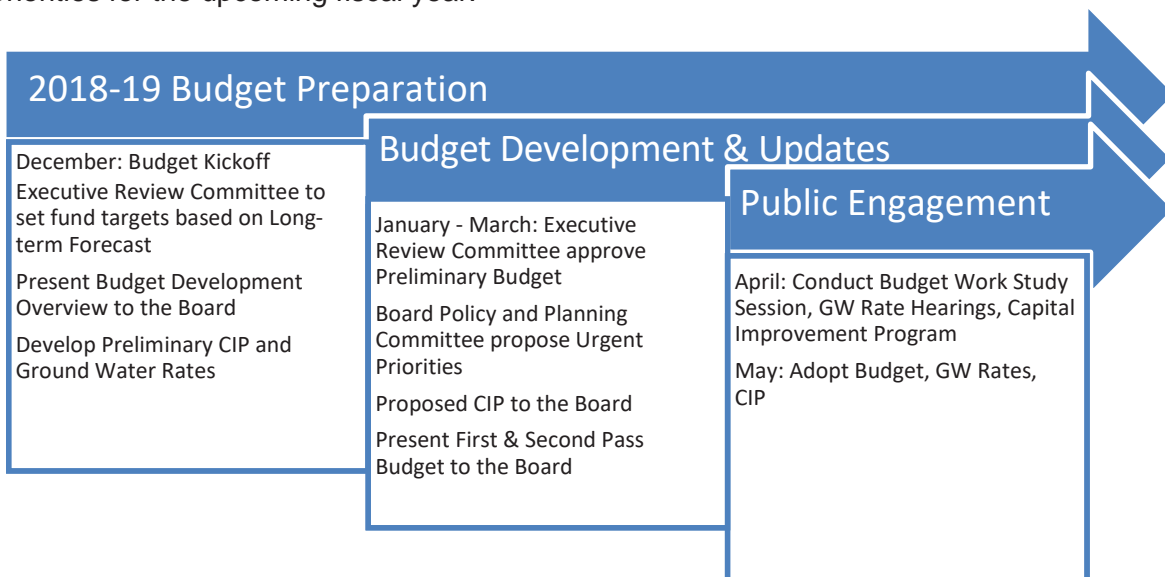
Honorable Members of the Board of Directors of the Santa Clara Valley Water District:

In accordance with the District Policy, I am submitting the 2018-19 Adopted Budget for the Santa Clara Valley Water District (District). This budget represents the District's mission of providing Silicon Valley safe, clean water for a healthy life, environment, and economy. It 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.

Financial Overview

The accounts of the District 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 2018-19 included several process improvements and numerous public hearings, as well as input from the Board on urgent priorities for the upcoming fiscal year.



District Priorities

In developing the budget, the Board directed its Board Policy and Planning Committee (Committee) to identify and summarize the Board's priorities. 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 help the organization achieve results toward the identified priorities as a part of the budget process.

This budget demonstrates a fiscally responsible, balanced budget that meets the community's expectations of the District. This budget focuses on 9 priorities, and these are not in order of priority.

1. Make key decisions regarding the **California WaterFix**
2. Provide for a watershed-wide **regulatory planning and permitting** effort
3. Foster a coordinated approach to **environmental stewardship** efforts
4. Advance the **Anderson Dam Seismic Retrofit** Project
5. Advance **recycled and purified water** efforts with the City of San José and other agencies
6. Finalize the **Fisheries and Aquatic Habitat Collaborative Effort (FAHCE)**
7. Actively pursue efforts to increase **water storage** opportunities
8. Advance **diversity and inclusion** efforts
9. Ensure immediate emergency action plans and flood protection are provided for **Coyote Creek**

The District is responding to these challenges in several ways, including expanded efforts possible with the help of 4 new positions discussed in greater detail in the sections that follow.

The organization will incorporate specific activities that address the Board's urgent priorities into its workplan and 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 2018-19 budget includes projected revenues of approximately \$448.0 million. These revenues are a net increase of \$3.9 million from the \$444.1 million included in 2017-18 adopted budget. The net \$3.9 million increase is primarily derived from increases in water revenue (\$31.0 million), 1% ad valorem property taxes (\$6.6 million), and special parcel tax (\$1.5 million) offset by a decrease in State Water Project property tax (-\$8.0 million), capital reimbursement revenue (-\$26.9 million) and a net decrease to other revenues (-\$0.3 million).

Appropriations/Outlays

Net total operating and capital outlays for the 2018-19 budget is \$509.9 million. 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 2018-19 budget is \$304.8 million, an increase of \$21.9 million from the 2017-18 adopted budget. The increase in net outlays reflects continued efforts to maintain service levels that support key strategic objectives and the Board priorities

Capital Outlays

2018-19 capital project appropriations total \$205.1 million, a decrease of \$13.2 million from the 2017-18 adopted budget. It is anticipated that \$90.3 million of the 2017-18 adjusted budget for capital projects also will carry forward into 2018-19 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. For 2018-19, the total is \$85.5 million. 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. In general, 50% of intra-district charges are paid by the Water Utility Enterprise, 36% Watersheds, 6% General Fund, and 8% Internal Service Funds.

Other Financing Sources/Uses

Other financing sources include debt financing proceeds to fund capital improvements. For 2018-19, planned Bond Proceeds of \$64.2 million and Commercial Paper proceeds of \$110.0 million are to finance Water Utility (\$109.2 million) and Safe, Clean Water & Natural Flood Protection (\$37.2 million) capital improvement programs.

Reserves

There are nine major restricted reserves in the District, further detail is found in the summary budget document pages 3–40. The Water Utility Enterprise Fund had six restricted reserves prior to 2018-19: Rate Stabilization Reserve for Bond Covenant, San Felipe Emergency Reserve, Silicon Valley Advanced Water Purification Center Reserve, Supplemental Water Supply Reserve, Drought Reserve, and the State Water Project Tax Reserve. Staff proposes adding the seventh restricted reserve starting in 2018-19: Public-Private Partnership (P3). This special purpose reserve would provide a funding source for costs associated with the District's Public-Private Partnership (P3) to design, build, finance, operate and maintain the Expedited Purified Water Program. The Safe, Clean Water Fund has two restricted reserves for the Currently Authorized Projects Reserve and Operating and Capital Reserve.

The District has four major committed reserves. The committed reserves are Liability/Workers' Compensation Self-Insurance Reserve - Risk Fund, Property Self- Insurance/Catastrophic Reserve - Risk Fund, Operating & Capital Reserve (not including Safe, Clean Water & Natural Flood Protection Fund), and Currently Authorized Projects Reserve (not including Safe, Clean Water & Natural Flood Protection Fund).

Overall, budgeted reserves for 2018-19 are expected to decrease \$25.4 million to \$334.0 million. The decrease primarily occurs in the committed reserve portion in the Water Enterprise Funds (\$19.4 million) and restricted reserve portion in the Safe, Clean Water & Natural Flood Protection fund (\$22.7 million) and other funds (\$1.6 million). Please see the summary table below for the FY 2019 reserve budget.

(\$ in Thousands)	Actual 2016-17	Adopted Budget 2017-18	Projected Year End 2017-18	Adopted Budget 2018-19	Change from	
					Adopted \$ Diff	2017-18 % Diff
Restricted Reserves						
Safe, Clean Water & Natural Flood Protection Fund	129,650	162,071	85,473	139,404	(22,667)	(14%)↓
Water Enterprise Funds	50,018	45,625	51,352	56,919	11,294	25%↑
Subtotal	179,668	207,696	136,825	196,323	(11,373)	(5%)↓
Committed Reserves						
General Fund	5,962	5,152	4,281	4,565	(587)	(11%)↓
Watershed Stream Stewardship Fund	64,898	69,558	90,731	76,588	7,030	10%↑
Water Enterprise Funds	61,417	63,272	57,191	43,878	(19,394)	(31%)↓
Internal Service Funds	24,879	13,703	23,007	12,640	(1,063)	(8%)↓
Subtotal	157,156	151,685	175,210	137,671	(14,014)	(9%)↓
Grand Total	336,824	359,381	312,035	333,994	(25,387)	(7%)↓

Debt Overview

The 2018-19 debt portfolio total outstanding principal of \$877.3 million includes \$82.3 million for Watersheds, \$655 million for the Water Utility Enterprise, and \$140 million of Commercial Paper for Safe, Clean Water & Natural Flood Protection and Water Utility Enterprise projects. Annual debt service budget of \$59.2 million includes repayment of principal, interest and various banking and legal fees for the debt portfolio.

The District's debt management strategy includes the use of a short term Commercial Paper (CP) Program with a maximum program capacity of \$225 million, supported by a \$150 million Letter of Credit (LOC) from Bank of Tokyo Mitsubishi UFJ, LTD. (BTMU) and a \$75 million Revolving Line of Credit from Wells Fargo Bank, National Association (WFB).

The long-term strategy is to issue CP to provide short-term just-in-time funding for capital expenditures. As the outstanding CP reaches the program capacity, the outstanding CP is refunded with long-term debt to be repaid over the remaining of life of the assets. For the Water Utility Program, the issuance of long-term debt helps keep water charges stable over the long-term while resulting in inter-generational equity and allows for the completion of capital projects in a timely manner. The water charge study 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 was approved by voters on November 6, 2012 and has a sunset date of June 30, 2028.

The Santa Clara Valley Water District proactively manages its outstanding liabilities to ensure access to the credit markets at the lowest available borrowing cost, to preserve strong credit standing with the municipal rating agencies, to fulfill its fiduciary responsibility to its customers, and to provide high quality water service, stream stewardship and flood protection at the lowest possible cost.

Bond Ratings

The bond ratings for the District's outstanding debt reflect high grade investment quality debt. They are based on the District's 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 2018-19.

Bond Rating

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

Staffing

The 2018-19 budget includes 813 regular positions and 4 fellowships, an increase of four new positions from the 2017-18 Adjusted Budget. The new positions' cost totals \$0.7 million. The new positions support the District's Fisheries Aquatic Habitat Collaborative Effort (FAHCE), and support the review of external development proposals, such as the BART extension, High Speed Rail and San Jose downtown Google development that affect the District facilities.

Position Count by Organization Area

	Regular Positions				
	Adjusted Budget 2016-17	Adjusted Budget 2017-18	Adopted Budget 2018-19	Change* from 2017-18	% Change from 2017-18
Board Appointed Officers & Financial Planning & Mgmt Div	82	80	77	(3)	(3.8%)↓
External Affairs	25	28	32	4	14.3%↑
Water Utility	333	332	334	2	0.6%↑
Watersheds	209	219	221	2	0.9%↑
Administration	142	150	149	(1)	(0.7%)↓
Districtwide	791	809	813	4	0.5%↑

Future Outlook

It is important to maintain a long-term outlook given the major infrastructure investments planned for the next 10 years. The District has an ambitious capital program to help ensure a reliable and safe water supply. Planning for the future means acting now. Some of the major infrastructure investments included in this budget are to ensure dam safety, secure imported water supply, manage infrastructure reliability through maintenance asset management, complete flood protection projects and step up sediment removal and erosion protection to maintain the conveyance capacity of completed flood protection projects.

This budget positions the organization well to deliver much needed services and facility improvements to the community over the next several years

Sincerely,



Norma Camacho
Chief Executive Officer

NB:ls