Santa Clara Valley Water District

Valley Water

File No.: 20-0414

Agenda Date: 4/28/2020
Item No.: *2.1.

BOARD AGENDA MEMORANDUM

SUBJECT:
Budget, Water Charge, & Capital Improvement Program Alternatives to Consider in Response to COVID-19 Pandemic.

RECOMMENDATION:
Discuss alternative actions and plans related to the Fiscal Year (FY) 2020-21 Budget, Water Charges, and Capital Improvement Program (CIP) and provide direction to staff as necessary.

SUMMARY:
Given the tremendous economic pressures unfolding due to the COVID-19 Pandemic, the Board held a special meeting on April 6, 2020 to discuss alternatives for staff to consider in preparation for the Groundwater Production Charge and CIP public hearings scheduled for April 28, 2020, and the Budget Work Study Session scheduled for April 29, 2020. The following is a high level recap of Board Comments:

1. Examine no increase in water rates for FY 21 for a period of three months, one half of the year, and the entire year;
2. Bring back ideas on how Valley Water could engage in targeted assistance to end customers, including potential partnerships with non-profit organizations within the county that provide direct assistance to families;
3. Bring back ideas on how Valley Water could provide targeted loans to end customers or retailers; and
4. Discuss the merits of a hiring freeze

<u>Financial Status Update</u>
Before discussing these Board comments in detail, it is important to provide context regarding the financial health of Valley Water. The following is a brief summary of Valley Water's cash position, revenue streams, outstanding debt, CalPERS employer contributions, and cash flow projection.

Cash and investments total over $600M as of the beginning of April, 2020 of which $120M is in cash equivalent deposits. All major retailers are current on payments to Valley Water as of April 2, 2020. All retailers have suspended water shutoffs, which could cause some end customers that can afford to pay, to choose not to. This does not necessarily translate to retailers choosing not to pay Valley Water, but it does increase that risk. Valley Water receives $15M to $30M per month from major retailers depending on seasonality, of which 33% comes from cities and other customers, and 67%

from Investor Owned Utilities. This is significant to note because cities are experiencing drastic reductions in sales tax revenue and are therefore likely to be under greater financial duress than investor owned retailers.

The pandemic will likely cause downward pressure on water usage, but weather will likely be the major driving factor. A $20 million revenue shortfall versus the FY 20 budget is already baked into the current groundwater charge projection included in the Annual Report on the Protection and Augmentation of Water Supplies (PAWS Report). However, if the spring is wet, a potential incremental $20 million revenue shortfall for FY 20 could happen. Likewise, if a pattern of reduced water usage continues throughout FY 21, it could result in a $22 million revenue shortfall relative to the proposed FY 21 Budget.

According to the County Assessor's Office, property tax collections are on track as of the writing of this memo, but a potential for heavy delinquencies could cause the Assessor's Office to suspend the Teeter Plan. The Teeter Plan provides California counties with an optional alternative method for allocating delinquent property tax revenues. Under the Teeter Plan, counties allocate property tax revenues based on the total amount of property taxes billed, but not yet collected. The Teeter Plan allows counties to finance property tax receipts for local agencies by borrowing money to advance cash to each taxing jurisdiction in an amount equal to the current year's delinquent property taxes. In exchange, the counties receive the penalties and interest on the delinquent taxes when collected. If property tax delinquencies are heavy for the installment due on April 10, 2020, and the Teeter Plan is suspended, Valley Water would receive less than 100% of its share of property tax receipts for FY 20 ($179 million Budget) by June 2020, and instead would receive any remaining balance sometime in the future.

Outstanding short term (Commercial Paper) debt is $50M currently with the next reissuance scheduled for 5/7/2020. Fortunately, as of the writing of this memo, the short term debt market has calmed since the March panic. The Federal Reserve program to purchase $500 Billion of short term debt from States/Counties/Cities has stabilized the market. Valley Water capital market contacts indicate that Valley Water will be able to reissue its Commercial Paper at a competitive borrowing rate on 5/7/2020.

Because of the stock market downturn, staff analysis indicates that CalPERS Employer Contributions will increase beginning in FY 22 unless the stock market rebounds. The estimated impact is an incremental $2.5 million beginning in FY 22, ramping up to an incremental $13 million per year in FY 26.

Staff prepared a best case and a worst case cash flow estimate for the next nine months. According to that estimate, under a worst case scenario where retailers stop paying for the entire nine months, there is no access to the capital markets, and management takes no action to reduce costs, Valley Water would still have over $250 million in cash and investments at the end of that time. It is important to note that this worst case scenario would primarily impact the Water Utility Fund. Critical management decisions regarding service levels, and continuation of capital projects should be made to prevent this scenario from playing out. Interfund loans would likely be required depending on the extent of cost reduction actions. It is also important to note that certain revenues, like the Safe Clean

Water special tax, can only be used for Safe Clean Water voter approved activities, and cannot be used to bolster the Water Utility Fund.

To hedge against future financial uncertainty, staff has planned to undertake the following actions:

1. Closely monitor retailer payments (next set of payments due at end of April);
2. Pursue one or more bank lines of credit up to $200M with Board approval;
3. As existing investments mature, convert to cash instead of reinvesting;
4. Reissue $50 million of Commercial Paper debt in May and perhaps an incremental $70 million;
5. Plan for long term bond issuance in the first quarter of FY 21 to free up Commercial Paper and potentially issue new debt to fund the Water Utility CIP for up to 3 years, depending on market conditions; and
6. Pursue federal stimulus funding for eligible projects

Potential Actions to Reduce Water Rates for FY 21

At the April 6 meeting, the Board requested analysis on potential actions that could help reduce water rates for FY 21. Potential actions include:

A. Pushing the start of construction of the Purified Water Program from FY 24 to sometime further in the future, which would have the effect of pushing cost out beyond the 10-year time frame, and lowering the 10-year water rate projection;

B. Delaying or forgoing our participation in the Delta Conveyance project to enhance reliability of Central Valley Project (CVP) supplies;

C. Pursuing Federal Stimulus funding for capital projects;

D. Deferring the rate increase for FY 21, and offsetting the impact with higher rate increases from FY 22 thru FY 30.

For the South County zones, the potential rate reduction actions are mainly geared toward new groundwater benefit zone W-7 as staff is recommending that the Board proceed with groundwater charge decreases proposed for modified Zone W-5 and New Zone W-8. Attachment 1 contains additional details on potential rate reduction alternatives.

Potential Actions to Provide Targeted Assistance to End Customers

The Board requested that staff look at ideas to provide targeted assistance to end customers. Staff has analyzed the following ideas:

A. Pursue partnerships with water purveyors to assist with water related activities.

(Purveyors in turn help targeted customers)

Pros:

- Could provide financial or in-lieu assistance to water purveyors (retailers have suggested programs where Valley Water could partially offset costs)

Cons:

- Would put upward pressure on water rates, or reduce funding for flood protection depending on revenue source
- May take some time to negotiate agreements or logistics to provide in-lieu services
- May be difficult to ensure that partnership would translate to assistance for targeted end customers

B. Contribute funding to non-profit organization that in turn assists targeted customers

Pros:

- Could provide financial assistance to targeted end customers

Cons:

- Legal constraint - prohibition of gift of public funds
- Would put upward pressure on water rates, or reduce funding for flood protection depending on revenue source

C. Partner with the Silicon Valley Strong Fund to solicit donations from the community to assist targeted customers

Pros:

- Could provide financial assistance or service to targeted end customers
- Would not impact Valley Water finances as revenue source would come from private sources

Cons:

- Degree of success is an unknown

<u>Potential Actions to Provide Targeted Loans to Retailers or End Customers</u>

The Board requested that staff look at ideas to provide targeted loans to retailers or end customers.

It should be noted that delinquent groundwater charge payments incur an interest charge of 1% per month per District Act section 26.9, which is in effect, a loan. Similarly, delinquent treated water payments incur an interest charge of .5% per month per the treated water contract, which is in effect, a loan. In addition, staff has analyzed a potential loan program for retailers, which would provide upfront funding for water supply related projects. Key components of the potential program structure could be as follows:

- $20 million maximum program size, with up to a $1 million loan per borrower
- Investor owned utilities excluded as they could raise equity or access capital markets themselves
- 5 year maximum loan term
- Interest rate at Valley Water cost of money
- Collateral pledge of 80% loan to value

A retailer loan program would provide cashflow assistance to retailers that may not have the same access to the capital markets as Valley Water, or that may not be able to secure the same borrowing rate. In terms of cons, there is risk of non-repayment of the loan, and it should be noted that additional staff resources may be required to manage the loan program.

<u>Potential Actions to Freeze Hiring</u>

Finally, the Board requested that staff look at a potential hiring freeze. Staff has analyzed two potential forms of a hiring freeze. The first is a freeze on all recruiting activities as of a certain date, or prior to a certain point in the recruiting process. A hiring freeze of this nature would put Valley Water into an “attrition” mode, in which headcount would decrease with each departure of an existing employee. Staff estimates an FY 21 savings ranging from $11 million to $15 million. However, there are several cons that should be considered including:

- Some essential capital and O&M work would not move forward in FY 21
- Attrition of critical positions could put delivery of essential services at risk
- Need for more consultant and temporary worker help would not be satisfied in timely manner, resulting in delays of critical work
- Key positions would not be available up front to ensure timely delivery of critical “mega” projects
- Staffing would not be available to take advantage of Federal stimulus funds

The second hiring freeze option is to delay FY 21 position requests and manage current vacancies to advance essential work. Staff estimates this would save up to $4M relative to the proposed FY 21

Budget. This option would allow for replacement of critical positions and would allow for continuation of current essential capital work. Several cons should be considered including:

- Will delay some essential O&M work (creating larger O&M backlog)
- Will delay long term feasibility studies and planning efforts
- Will result in need for more consultant and temporary worker help
- Staffing may not be available to take advantage of Federal stimulus funds without delaying other essential work

Management Tactics In Place to Reduce Costs

Management has taken certain actions in accordance with the transition to telework to reduce expenditures while protecting employee welfare including:

- Reducing temporary and intern staffing levels
- Adjusting facility service contracts to enhance certain service levels to better protect against the spread of COVID-19, while scaling back other services in accordance with the minimal number of employees on Valley Water campuses.

Staff has identified the following adjustments to capital projects based on project plan refinements, that would also have the effect of reducing the FY 21 budget and improving cash flow. These adjustments include:

- San Francisquito Creek Upstream schedule adjustment to move construction from FY 21 to FY 22 to align with Newell Road Bridge Replacement, which would reduce the FY 21 budget by $4 million
- Guadalupe River, Tasman Dr. to I-880 schedule change for FY 21 (shift from design to planning phase), which would reduce the FY 21 budget by $1.55 million
- Residuals Remediation Project refinement to estimated FY 21 budget needs, which would reduce the FY 21 budget by $3 million;
- 10-Year Pipeline Project work plan refinement based on regional partnerships, which would reduce the FY 21 budget by $3 million.

In addition, staff has reviewed the Capital Improvement Program for work that can be deferred in response to COVID-19 orders regarding essential work. Watersheds staff has identified the following projects that would be deferred to FY 22:

- Defer the Bolsa Road Fish Passage Improvement construction from FY 21 to FY 22, which would reduce the FY 21 budget by $3 million

- Defer the Upper Guadalupe Gravel Augmentation construction from FY 21 to FY 22, which would reduce the FY 21 budget by $0.7 million

Finally, staff proposes the following CIP adjustments that would also have the effect of reducing the FY 21 budget and improving cash flow:

- Pushing the start of construction of the Purified Water Program from FY 24 to sometime further in the future, which would reduce the FY 21 budget by $5.5M, and would have the effect lowering the 10-year water rate projection;

- Slow down the construction of South County Recycled Water Pipeline, which would reduce the FY 21 budget by $9.3 million;

- Defer the largest portions of the Rinconada Water Treatment Plant (RWTP) Reliability phases 3-6 by two to four years, which would reduce the FY 21 budget by $10 million;

Summary

Staff is seeking Board direction on the alternative analyses provided.

FINANCIAL IMPACT:
There is no financial impact associated with this item. However, the direction provided by the Board may have a significant impact on the budget, water charges, and CIP adopted by the Board for FY 2020-21.

CEQA:
The recommended action does not constitute a project under CEQA because it does not have a potential for resulting in direct or reasonably foreseeable indirect physical change in the environment.

ATTACHMENTS:
Attachment 1: PowerPoint
*Handout 2.1-A, Legal
*Handout 2.1-B, Poseidon
*Handout 2.1-C, SJW
*Handout 2.1-D, Sunnyvale
*Handout 2.1-E, City Support
*Handout 2.1-F, Colleagues Memo

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