Santa Clara Valley Water District

Valley Water

File No.: 20-0502 **Agenda Date:** 8/11/2020
Item No.: 4.1.

BOARD AGENDA MEMORANDUM

SUBJECT:
Receive Overview of Valley Water's Current Budget Processes and Consider the Benefits and Drawbacks Associated with Biennial Budgeting.

RECOMMENDATION:

A. Review Valley Water's current annual budget process in relation to a biennial budget process in order to identify the benefits and drawbacks associated with each; and
B. Direct staff to implement a rolling biennial budget process to be updated annually after implementation of, and demonstrated stability of, the Infor Enterprise Resource Planning system.

SUMMARY:
Valley Water is on an annual Capital Budget, Operating Budget, and Rate setting cycle. Based on staff's assessment, Valley Water could successfully transition to a biennial budget process, at the appropriate time, with investment of time and resources while also revising policies and procedures to accommodate the necessary budget process changes.

Background
Valley Water prepares the Operating Budget, Capital Budget and Rates on an annual basis. The Board has asked staff to examine the merits of adopting a biennial budget cycle conducive to long-term planning. Traditional biennial budgeting is defined as the practice of preparing and adopting budgets for two-year periods. As set forth below, staff is recommending a variation of the traditional biennial budgeting process. Staff evaluated the following budget process options for the purposes of this exercise:

- Traditional biennial budget with mid-cycle update - In a traditional biennial budget, staff submits, and the Board approves a 24-month appropriation. The budget is prepared in odd years and oversight is conducted in even years. A mid-cycle update process is employed to modify the second year of the budget.

- Rolling biennial budget updated annually - Under a rolling biennial budget process, the Board would adopt a one-year budget and approve an additional forecast that serves as the tentative spending plan for the non-budget development year. This results in the first year's appropriations being formally adopted by the Board, whereas the subsequent year's appropriations are not.

- The rolling biennial budget is updated annually as the just completed year rolls off and the new second year is added.
- One-year budget with time saving options - Under this option, the annual budget process would continue, but time savings alternatives would be incorporated.
- One-year budget, maintain status quo - This option would continue Valley Water's current budget process.

Considerations

Guiding State, District Act and Valley Water Policies - after reviewing the regulating guidelines and polices guiding Valley Water operations, staff concludes that an annual meeting with the board and related public hearings will still be necessary.

California Government Code (§ 65403) requires special districts to convene annually, soliciting stakeholder and public input for adoption of a five-year Capital Improvement Program (CIP). In considering a biennial budget, we would still have to convene annually on the CIP to meet this requirement.

The District Act, Section 20 and 26, requires the Board to convene annually and solicit public input in order to adopt a yearly budget and associated rates. In considering a biennial budget, we would still have to convene annually on the Operating Budget and Rates Setting to meet this requirement.

Additionally, in order to implement a traditional biennial budget process, the Board Governance Policies, Board Appointed Officers (BAO) Interpretations, and internal policies and procedures would require review and adjustments

Time Commitment and Costs vs. Benefits

Past experience brings insight: Valley Water previously utilized a traditional biennial budget from fiscal years 2001 to 2005 but ultimately reverted back to an annual budget. The number of budget adjustments that occurred, coupled with the updates necessary to implement second year projects, necessitated staff to undertake a process akin to what an annual budget process would entail with the second year. As such, the preparation of supplemental budget documents and budget adjustments replicated the amount of work required to deliver the annual budget in prosperous economic conditions, Valley Water's operating budget is relatively straight-forward; nonetheless, the organization is strongly capital project based, which requires forecasting assumptions be continuously monitored.

Budgetary Uncertainty: The current budgeting calendar assumes Valley Water begins the

Long-Term Forecast process, which guides the organization's high-level projections for ten years of project spending, in September of every fiscal year. The Operating and Capital budget process begins in December and concludes in June for the following fiscal year, which begins in July. Biennial Budgeting would involve working on the second year's budget in advance. In Valley Water's case, Budget staff would begin to put together budgets for the second fiscal year, of a two-year cycle, at least 20 months before the second fiscal year would start.

Long lead-times due to budgeting far in advance would most likely lead to dated assumptions unless a robust mid-cycle update were employed as under a traditional biennial budget, or unless a rolling biennial budget process, updated annually, is utilized. Biennial budgeting would imply a long-term, strategic, planning approach, requiring more effort in the development phase. When deteriorating economic or social conditions unfold, such as the most recent COVID pandemic, the approach to biennial budgeting should allow the budgeting process to remain dynamic and responsive to the needs of the organization as most recently demonstrated in during the FY 2020-21 Budget process.

Budget/Accounting Systems: Valley Water is currently using the Vena budgeting system on an annual basis. Vena was implemented in FY18 and continues to be refined. Financial information in Vena is currently synched with the accounting software by fiscal year. There will be costs associated with changes to the budgeting and accounting processes to accommodate a rolling biennial budget.

- Should the district adopt a rolling biennial budget, there would be significant implementation costs associated with Vena revisions, user training, and ERP integration, as well as ongoing expenditures related to system modifications
- Moving to a rolling biennial budget process would involve a rebuild of our project-based budgeting templates in both operating and capital
- The organization is currently in the process of transitioning to a new financial management solution / enterprise resource planning software and it's advisable to implement a full fiscal year budget before transitioning to biennial budgeting to ensure a successful transition

Staff Recommendation

Staff has examined the merits of adopting a biennial budget cycle to allow more flexibility and achieve the goal of long-term planning. There are benefits and drawbacks to both annual and biennial budget cycles. A biennial budget facilitates long-term planning, whereas an annual budget cycle is more responsive to short term changes in economic conditions.

Staff recommends implementing a rolling biennial budget process to be updated annually, which is aligned with the guiding State, District Act and Valley Water Policies, and is conducive to long-term planning while remaining responsive to the dynamic and ever-changing needs of the organization. Staff recommends implementing a rolling biennial budget process after completion of the Infor Enterprise Resource Planning system implementation and demonstrated ERP system stability.

Title 7 of the California Government Code § 65403
<https://leginfo.legislature.ca.gov/faces/codes_displaySection.xhtml?lawCode=GOV&sectionNum=65403>
[2] "District Act". Santa Clara Valley Water District. Accessed February 2018.
<https://www.valleywater.org/sites/default/files/Santa%20Clara%20Valley%20Water%20District%20-%20District%20Act.pdf>

FINANCIAL IMPACT:
The Valley Water budget and accounting processes may be adjusted as appropriate to accommodate direction of the Board as a result of this discussion. Should the Board direct staff to implement a rolling biennial budget model, there will be costs associated with budget system modifications, staff time, as well as time to train end users. Upon Board's direction, Staff will return at a later time to discuss these with a more detailed analysis.

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

ATTACHMENTS:
Attachment 1: PowerPoint

UNCLASSIFIED MANAGER:
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