REGIONAL WATER AUTHORITY
POLICIES AND PROCEDURES MANUAL

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Policy Title	:	Allocating Liabilities to Withdrawing Members
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ALLOCATING LIABILITIES TO WITHDRAWING MEMBERS

Background

Members of RWA operate under a joint exercise of powers agreement that outlines powers and responsibilities of RWA and of members. The Amended and Restated Joint Exercise of Powers Agreement of the Regional Water Authority, dated October 8, 2013, provides for the voluntary withdrawal from membership subsequent to 90 days' notice. Such withdrawal is subject to the provision that the withdrawing member "shall remain responsible for any indebtedness incurred by the Member under any Project or Program Agreement to which the Member is a party, and further provided that the withdrawing Member pays or agrees to pay its share of debts, liabilities and obligations of the Regional Water Authority incurred by the Member under this Agreement prior to the effective date of such withdrawal."

Most of RWA's obligations are budgeted for on an annual basis and incorporated into the annual budget. Some obligations are incurred during the membership, but the payment is made over several future periods. Examples of these types of delayed payments for past services include unfunded pension and other post-employment benefit ("OPEB") liabilities. Required payments of these future obligations based upon prior and current service are dependent upon estimates since investment performance and experience may be different than forecasted.

This policy outlines the framework to allocate debts, liabilities and obligations of the Regional Water Authority.

Unfunded Pension Liabilities

RWA provides defined pension benefits for plan participants that meet the vesting criteria as established by CalPERS, the California Public Employees' Pension Reform Act (PEPRA)[1]. The fundamental financial objective of an employee defined

[1] Any current or future changes to the pension laws will dictate available benefits to employees or retirees.

benefit pension plan is to fund the long-term costs of benefits promised to the plan participants. In a defined benefit plan, an employer has promised a benefit and must make contributions to the plan in order to meet the promised benefit[2]. In order to assure the pension benefits will remain sustainable, RWA should accumulate adequate resources for future benefit payments in a systematic and disciplined manner during the active service life of the benefitting employees.

These pension plan obligations are accumulated over the life time of employee service. RWA's pension plan payments have been based upon CalPERS Annual Valuation reports which specify the amount of payments RWA is required to make to fund these pension plan obligations. RWA has paid 100% of the annual required contributions towards the pension plan. However, due to amortization policies[3] of the CalPERS pension plan that account for differences between actuarial assumptions and actual results, RWA's actuarially determined pension liabilities for prior employee service has not yet been fully funded. Because RWA's membership is voluntary, RWA has adopted Policy 500.15 Defined Benefit Pension Plan Funding Policy. The goal of Policy 500.15 is to accelerate additional payments towards the unfunded pension liability over a period of four years so as to achieve a 100% funded ratio. A 100% funded ratio is calculated by comparing the allocated market value of pension assets compared to the actuarial accrued liability for RWA's plan. However, since every year new liabilities can be created when actual pension plan results don't match the actuarial assumptions or assumptions change, new additional unfunded liabilities can be created.

Since RWA membership is voluntary, it is important that the pension costs for employee services incurred while serving active members is adequately and timely funded by these RWA members as they receive these services so as to achieve intergenerational equity. The unfunded liability represents pension costs associated with past service of employees that have been received by RWA members. These past services have contributed to the current influence and success of RWA as a regional water advocate.

RWA's unfunded pension liability is considered incurred by the member for services received during membership. This liability shall be calculated and allocated to members who withdraw based upon the following framework:

1. Determine the withdrawing member's proportion of annual dues for all years of membership.
2. Determine total RWA membership dues since organization inception in July 2001 for all remaining members, including the withdrawing member.
3. Calculate an allocation percentage for the withdrawing member by taking the dues in step one divided by the dues in step two.

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[2] The required contributions are typically variable in nature due to variable market performance and changing assumptions.

[3] CalPERS has amortization policies that typically amortize these differences over 30 years with a five-year ramp up of amortization costs.

4. Obtain the unfunded hypothetical termination liability ("UHTL") as prepared by the latest available CalPERS annual valuation report using the highest discount rate available as calculated for the UHTL. The hypothetical termination liability assumes that once the termination lability is "paid" by the employer, the pension plan will no longer continue to receive employer funds and therefore must be self-sustaining to pay for legal pension obligations. A lower discount rate is assumed for this calculation to mitigate the risk of funds being insufficient to pay for pension obligations due to changes in assumptions. Even if RWA has fully paid its unfunded liability as determined by CalPERS using funding discount rates,[4] RWA can still have an unfunded hypothetical termination liability since lower discount rates are used.
5. The members' allocation percentage as calculated in step 3 multiplied by the UHTL in step 4 will result in a pension liability payment due from the withdrawing member.

Any funds received by RWA specifically for the pension plan obligations as calculated above will be remitted to CalPERS pension plan as part of the annual additional lump sum payment(s) made by RWA in excess of the required annual contributions. Based upon staff recommendations, the Board may exercise discretion in regards to the timing of the payment to CalPERS for these type of payments.

Unfunded Other Post-Employment Liabilities ("OPEB")

Bi-annually, RWA has an actuary calculate the unfunded OPEB. Beginning in fiscal year 2017, the unfunded liability includes two components – an explicit and implicit liability. RWA has been funding both portions of this liability since fiscal year 2017. The annual required contribution for OPEB pays for the current year employees OPEB benefits and for the prior year unfunded benefits. In determining the portion to allocate to a withdrawing member, the unfunded actuarial accrued liability as determined by the latest actuary report, including both the explicit and implicit liability, will be the liability basis used to allocate to the member. This unfunded actuarial accrued liability allocation will be determined in the same manner as the unfunded pension liability allocation.

Dues Surcharges

From time to time, RWA may incur obligations that benefit members but may be paid for over a period of several years, such as the Powerhouse Science center project. RWA may make one-time or multi-year special assessments to fund these opportunities. Withdrawing members will be responsible for the allocated obligation of these special assessments, including any future unpaid multi-year assessments. These obligations due from the withdrawing member will be calculated using the same allocation basis to derive the special assessments.

[4] The discount rates for funding have varied over the years. Historically, the discount rate was 7.75% and is expected to decrease to at least 7.0 and perhaps further in future years.

Project or Program Management Liabilities

These specific liabilities are based upon project management agreements between various members, depending upon the project. As stated in the joint powers agreement, the withdrawing member shall be obligated to pay its portion of liabilities as agreed to according to the project or program management agreement and approved by the Project Committee as of the date of withdrawal.

Leases

If leases represent use of space or equipment on a prospective or ongoing use basis, these obligations are accounted for in current dues and would typically not be allocated to withdrawing members.

Payment to RWA

Payment for these obligations and liabilities are payable to RWA within 90 days of invoice.