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the
MANDMARBLESTONE*Group llc*
retirement plans redefined

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Cash Balance Pension Plans for Law Firms

Frequently Asked Questions

Introduction

This white paper provides law firm partners with answers to frequently asked questions about how cash balance pension plans provide partners with:

- immediate income tax reduction and
- a substantial liquid asset accumulation at retirement, while
- minimizing the firm's contribution expense to non-partners.

Summary of Questions Asked

1. What is a cash balance plan?
2. Who makes contributions to a cash balance plan?
3. Does the number of partners limit the applicability of a cash balance plan?
4. How much must a partner earn before a cash balance plan is appropriate?
5. Does fluctuating fee revenue limit the ability to use a cash balance plan?
6. How is the contribution amount by the practice determined?
7. If the practice has an existing 401(k) plan, may the practice also establish a cash balance plan?
8. What is the maximum amount a partner may receive in the plan?
9. How much must the practice contribute to highly compensated associates and to other non-partners in a cash balance plan?
10. Are the annual contributions predictable?
11. Do the partners have investment control over their accounts in the plan?
12. What determines if a law firm is a good candidate to establish a cash balance plan?
13. Does a cash balance plan have a vesting schedule?
14. What are the steps to establish a cash balance plan, and how long does it take?

Questions and Answers

Question 1: What is a cash balance plan?

Answer 1: A cash balance plan is a type of qualified retirement plan designed to accumulate predetermined annual contributions for its participants. Each participant in a cash balance plan receives an annual contribution (usually based on a percentage of pay) that is credited to a hypothetical account established in the participant's name (the contribution credit). The participant's hypothetical account balance is credited with an annual rate of return (the interest crediting rate). Both the contribution credit and the interest crediting rate are set forth in the plan documents.

Question 2: Who makes the contributions to a cash balance plan?

Answer 2: The law firm makes the contributions to the cash balance plan, not the plan participants.

Question 3: Does the number of law firm partners limit the applicability of a cash balance plan?

Answer 3: No – the number of partners does not limit the applicability of a cash balance plan.

Question 4: How much must a partner earn before a cash balance plan makes sense?

Answer 4: It is not the amount of a partner's earnings; rather, it is the amount that a partner is able to have contributed toward his or her retirement on an annual basis that is a factor in deciding if a cash balance plan makes sense. A reasonable starting point is a law firm that is able to contribute at least $100,000 per year for each partner for retirement purposes.

Question 5: Does fluctuating annual fee revenue prevent having a cash balance plan?

Answer 5: Since annual contributions to a cash balance plan are mandatory once the plan is established, as long as the fee revenue fluctuations do not prevent the firm from making the specified annual contribution, then fluctuation in gross fee revenue is not an impediment to having a successful cash balance plan.

<u>Question 6</u>: How is the contribution amount determined?

<u>Answer 6</u>: The partners define their objectives (who is to be covered, how much money are they able and willing to contribute on an annual basis, etc.). The appropriate formula to achieve those goals is determined by an actuary when the plan is established. Different levels of contributions may be provided to different groups of employees; however, the law firm contributions to the plan must not considered to be discriminatory in favor of partners.

<u>Question 7</u>: If a company has a 401(k) plan, may the company also establish a cash balance plan?

<u>Answer 7</u>: Yes, a company may have both a 401(k) plan and a cash balance plan. Ideally, these plans should be aggregated for discrimination testing purposes (rather than being tested as two isolated and separate plans). While this combination of plans is complex, and will require sophisticated professional advice, it also will provide the largest aggregate contributions for owners while preserving the greatest amount of flexibility related to the company cost for all other participants.

<u>Question 8</u>: How much may be contributed on behalf of a partner to an effectively designed combination 401(k) profit sharing plan and cash balance pension plan?

<u>Answer 8</u>: A partner's annual contribution depends on a combination of his or her age and compensation. The law does not set a contribution limit for each participant, as is the case in a 401(k) plan. Instead, it provides for a maximum annual benefit that may be paid at retirement. For example, in 2009 and 2010, the maximum annual retirement benefit for a plan participant is $195,000 per year. This equates to a lump sum of approximately $2,000,000. Accordingly, company contributions to a cash balance plan are based upon the projected lump sum needed at a participant's retirement to provide the maximum annual retirement benefit. This often results in substantially larger tax-deductible contributions being available for partners in a cash balance plan, especially as those individuals get closer to retirement age. Assuming that a partner has annual compensation of at least $245,000, the tables below compare maximum annual contributions to a 401(k) profit sharing plan alone, to the contributions that may be made to a combination 401(k) profit sharing plan and cash balance pension plan.

<u>401(k) Profit Sharing Plan</u>

Age	401(k) Deferral	Profit Sharing	Total
40	$16,500.00	$32,500.00	$49,000.00
45	$16,500.00	$32,500.00	$49,000.00
50	$22,000.00	$32,500.00	$54,500.00
55	$22,000.00	$32,500.00	$54,500.00
60	$22,000.00	$32,500.00	$54,500.00
65	$22,000.00	$32,500.00	$54,500.00

Combination 401(k) Profit Sharing Plan and Cash Balance Plan

Age	401(k) Deferral	Profit Sharing	Cash Balance	Total
40	$16,500.00	$32,500.00	$69,000.00	$118,000.00
45	$16,500.00	$32,500.00	$88,000.00	$137,000.00
50	$22,000.00	$32,500.00	$113,000.00	$167,500.00
55	$22,000.00	$32,500.00	$145,000.00	$199,500.00
60	$22,000.00	$32,500.00	$186,000.00	$240,500.00
65	$22,000.00	$32,500.00	$192,000.00	$246,500.00

Question 9: : If a law firm establishes a cash balance plan with the objective of maximizing contributions to the partners, how much will the law firm have to contribute for highly compensated associates and to other non-partners?

Answer 9: While the contribution amount for non-owners is determined by IRS regulations, in general, a law firm should count on contributing 3% of the compensation of associates who earn in excess of $110,000 per year, and between 5% and 8% of the compensation of other non-partner participants.

Question 10: Are the annual contribution amounts predictable, so that a company may budget for the contribution?

<u>Answer 10</u>: Yes, although it is best to budget for a range of amounts. Here's why: Since the interest crediting rate used in the plan's formula is guaranteed, the company's contribution will vary from year to year to account for differences between the interest crediting rate and the actual rate of return earned by the plan's investments. When the actual earnings rate is close to the guaranteed rate provided in the plan, then the company's contribution will be very predictable. If the actual rate of return on the investments is dramatically lower than the plan rate, the company contribution will increase; if the actual rate of return is higher, the company contribution will decrease. Accordingly, the plan's investment portfolio should be designed to produce a return approximating the plan's interest crediting rate.

<u>Question 11</u>: Do partners (and other plan participants) have control over the investment of their accounts?

<u>Answer 11</u>: No. The plan assets are invested as a single account which is managed by a Trustee.

<u>Question 12</u>: What determines if a law firm is a good candidate to establish a cash balance plan?

<u>Answer 12</u>: A law firm is a good candidate for a cash balance plan if a 401(k) profit sharing plan, by itself, does not provide a large enough tax deferred benefit to owners, and the firm can afford to make substantial contributions. As shown above, adding a cash balance plan can significantly increase the total amount of income saved, and sheltered from taxation. Since a company's cash balance contribution is mandatory, a good cash balance law firm candidate should have predictable revenue.

<u>Question 13</u>: Does a cash balance plan use a vesting schedule, so that if a plan participant terminates employment prior to being fully vested he or she may not be entitled to the entire hypothetical account balance?

<u>Answer 13</u>: Yes, the benefits of plan participants may be subject to a vesting schedule. If a participant leaves the company before three years of service, all or a portion of his or her account may be forfeited. The amount of the forfeiture will reduce the company's contribution.

Question 14: What is the process to establish an effective combination 401(k) profit sharing plan and cash balance plan, and how long does it take to complete the process?

Answer 14: The following steps should be taken to establish an effective combination 401(k) plan and cash balance pension plan:

1. Initial meeting scheduled with law firm partners (or designated partner group, or managing partner) to explore applicability of establishing a combination 401(k) plan and cash balance pension plan. If it appears that the law firm is a good candidate, a second meeting is scheduled at the conclusion of the first meeting.
2. Electronic employee census data must be provided to the consulting advisor within one week of the first meeting if the time line is to be met.
3. Three weeks after the first meeting, the second meeting with the partners is held, and the advisor presents an illustration of the plan design that comes closest to meeting the contribution objectives of the partners.
4. Following the second meeting, the partners decide whether to move ahead with establishing the retirement plan design, and if the partners decide to implement the program, an engagement agreement is provided to the partners within 3 days of notifying the advisor of their decision to proceed.
5. The completed documents to implement the program are provided to the partners for review and signature within two to three weeks following the advisor's receipt of the signed engagement agreement.
6. As soon as the retirement plans' investment vehicles have been determined (typically, a participant-directed 401(k) investment platform and a trustee-directed cash balance fund), the law firm may begin to make contributions to the program.

Conclusion

The attorneys at the MandMarblestone Group, llc are experts in helping law firms to quantitatively define their retirement plan contribution objectives. We then use sophisticated, IRS-approved techniques to guide the firm through an efficient process to establish a retirement plan design that enable the partners to achieve a financially secure retirement.

How to Reach Us

If you believe that the MandMarblestone IRS-approved Cash Balance Pension plan, in conjunction with our ***OCPP***® plan design (which allows maximum contribution flexibility), may be right for your law firm, contact:

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