

New funding rules and market turmoil could increase cash costs in defined benefit pension plans sponsored by law firms

Law firms with certain types of qualified defined benefit pension plans may face additional cash requirements in 2009 and 2010. New stricter funding rules apply as falling funding levels will lead to significant additional cash costs. Law firms should assess the impact of this anticipated cash hit on their business and review investment strategies and alternative methods of providing benefits to partners and staff.

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What You Need to Know

- The average funding level for US pension plans has fallen to around 70% during 2008, compared to 90% - 100% at the start of the year.
- New funding rules applied for the first time in 2008 following the new Pension Protection Act (PPA). For many plans the PPA and falling funding levels will trigger additional cash requirements in 2009 and 2010.
- Plan losses will typically be spread over a seven year recovery period. For a \$50m plan, typical losses in 2008 would trigger an additional \$1.5m - \$2m cash cost each year.
- Law firm plans subject to additional funding requirements include traditional defined benefit plans and certain cash balance plans. Variable annuity plans are largely unaffected.
- When funding falls below certain thresholds, plans will be unable to pay full lump sums and may need to discontinue further accrual of benefits.
- Congress has recently passed the Worker, Retiree, and Employer Recovery Act of 2008, a bill that relaxes phase-in of some of the PPA rules and allows smoothing of asset returns. Industry groups consider this relief insufficient and are lobbying for additional measures.

How PwC Can Help

- Review projected cash requirements for the defined benefit plan in 2009 and 2010 and discuss possible alternatives for mitigating costs.
- Review valuation assumptions and funding philosophy to evaluate ability to smooth contribution requirements.
- Perform asset liability modeling as part of a review of investment strategy to target less volatility and greater certainty over future cash requirements.
- Evaluate delivery vehicle for staff pension benefits and discuss alternatives. Note that switching to a defined contribution plan will provide more funding certainty, but may be more expensive in the long term.
- Discuss pros/cons of changing prospective partner benefit accruals to a defined benefit plan where funding is less dependent on plan asset performance. This could include a variable annuity plan or market-rate cash balance plan.
- Keep you advised about the prospects of additional pension relief and how it would affect cash requirements.

We understand that law firms are facing many challenges brought on by the current economic crisis. When it comes to pension plan funding, we want to make sure you understand all the options available to you to help ease the cash flow. We are ready to talk with you, share our insights on the industry, and help you deal with this latest set of challenges.

Solicitation

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