The Language of Retirement Plans Guide

Understanding retirement plans is easier when you know the terminology

Glossary

12b-1 fee

A cost charged to shareholders to pay for a mutual fund's distribution and marketing costs or certain shareholder services.

3(16) Plan Administrator

A fiduciary under ERISA responsible for managing the day-to-day operation of the plan. The duties of the plan administrator are set by ERISA and the terms of the plan document. The plan must designate an ERISA 3(16) plan administrator; most plan documents name the plan sponsor.

3(21) Investment Adviser

A co-fiduciary role under ERISA whereby an adviser provides investment advice with respect to funds in a retirement plan investment menu. Plan sponsors retain the discretion to accept or reject the advice. Also referred to as a 3(21) fiduciary.

3(38) Investment Manager

A plan fiduciary under ERISA with full discretionary authority and control over selecting, monitoring, and replacing retirement plan investments. The plan sponsor offloads fiduciary risk for investments to the adviser; however, they still carry a fiduciary duty to monitor the adviser. Also referred to as a 3(38) fiduciary.

401(k) plan

An employer-sponsored defined contribution plan that allows participants to defer part of their compensation on a pretax basis to save for retirement. 401(k) refers to the section of the Internal Revenue Code (IRC) that describes this arrangement. 401(k) plans are often referred to as "cash or deferred arrangements" (CODA).

402(g) limits (employee elective deferral limits)

The maximum amount of elective salary deferral contributions a participant may make to any 401(k) plan, 403(b) plan or SIMPLE IRA plan in one year. The 402(g) limit is an annual individual limit covering both pretax and Roth salary deferral contributions. The 402(g) limit, which refers to the section of the IRC that describes the limit, is adjusted annually to reflect increases in the cost of living (COLA). (Also see **catch-up contributions** definition.)

403(b) arrangement

An annuity contract or custodial account that meets the requirements of Section 403(b) of the IRC. Only certain public schools, universities and tax-exempt organizations described in section 501(c)(3) of the IRC, and certain ministers, are eligible to establish 403(b) plans. A written plan document is required. Once adopted, the plan must be "universally available" to employees of the sponsoring organization to make elective salary deferrals into a 403(b) arrangement. Most 403(b) plans are not subject to ERISA, but a tax-exempt organization's plan will be subject to certain requirements under ERISA if the employer makes contributions to the plan or exercises certain discretionary functions in relation to the plan.

404 limit — employer deductible contribution limit

The maximum annual deduction permitted by an employer for federal income tax purposes with respect to employer contributions made to a defined contribution retirement plan. 404 refers to the section of the IRC that sets the limit. The deductible contribution limit is an aggregate limit covering all contributions by an employer to any defined contribution plan(s). The annual deduction limit is 25% of eligible compensation earned by all plan participants for that year.

404a-5 fee disclosures

The purpose of the ERISA Regulation 404a-5 disclosures is to provide sufficient information regarding the plan, including investments, fees, and expenses, to participants in participant-directed individual account plans so that they can make informed decisions with regard to the management of their individual plan accounts.

404(c) regulations

Under the 404(c) regulations, a plan fiduciary may be relieved of liability for investment decisions made by retirement plan participants who have the ability to exercise control over their plan account investments, provided certain other conditions are met. Compliance with 404(c) is optional.

408(b)(2) fee disclosure

The purpose of the ERISA 408(b)(2) disclosures is to ensure that plan fiduciaries receive the information they need to assess the fees and expenses and reasonableness of a service provider contract or arrangement, and identify conflicts of interest, before accepting services to the plan.

415 limit — annual additions limit

The maximum annual contribution limit to a participant account in a defined contribution plan. This limit includes all contributions except rollover and loan repayment. 415 refers to the section of the IRC that sets the limit. The defined contribution limit is an aggregate limit. All annual additions to the account of a participant under all defined contribution retirement plan(s) maintained by the employer are counted against the limit. The annual defined contribution plan 415 limit for a year is generally the lesser of 100% of the participant's eligible compensation for a year or a specified dollar limit, which is adjusted annually to reflect changes in the cost of living.

Common types of contributions

All contributions count toward a participant's annual additions limit:

- **Designated Roth.** Also known as Roth 401(k), 403(b) or 457(b) contributions, these are elective salary deferrals currently included in the participant's gross income. Because these contributions were taxable when contributed to the plan, they will be distributed tax-free from the plan. If the participant meets the requirements for a qualified distribution from the designated Roth account, the investment earnings on designated Roth contributions will also be tax-free.
- **Discretionary (or profit-sharing) (nonelective).** A non-mandatory amount paid by the employer in accordance with the terms of the plan.
- **Elective deferrals.** A participant's voluntary pretax contribution in accordance with the terms of his or her retirement plan and the participant's salary deferral election.
- **Forfeiture reallocation.** A reallocation of employer contributions that were forfeited by participants who terminated employment before becoming fully vested in the employer contributions made to their account.

457 plan

A deferred compensation arrangement sponsored by a federal, state or local government/ municipality or a tax-exempt organization. Most 457 plans are funded by elective deferrals and are similar to 401(k) plans (but significantly different tax rules apply). 457 refers to the section of the IRC that describes the tax treatment of 457 plans. 457 plans may be an eligible plan, referred to as a 457(b) plan, or an ineligible plan, referred to as a 457(f) plan.

457(b) plan — Typically offered by state and local governments to allow employees to supplement their state-funded pension plan with elective salary deferrals but may be offered by a tax-exempt organization if the assets are held in the name of the employer rather than in a plan trust. Governmental 457(b) plan assets are eligible to be rolled over to profit sharing/401(k) plans, 403(b) plans and IRAs.

457(f) plan — Typically non-qualified plans offered by non-governmental entities to provide additional benefits to highly paid employees and key management personnel (also known as Top-Hat plans).

5-Part Test

Under the current ERISA 3(21) fiduciary regulations, an investment adviser would be considered an ERISA fiduciary as a result of the advice given to a retirement investor if all five elements are satisfied. The adviser:

1. Renders investment advice or makes recommendations for a fee;
2. On a regular basis;
3. Pursuant to a mutual understanding.
4. The advice will serve as a primary basis for the investment decision, and
5. The advice will be individualized based on the investor's needs.

The DOL has interpreted the "regular basis" condition to include a pre-existing advice relationship with the investor or a potential ongoing relationship after a rollover of tax-qualified retirement assets. A fiduciary adviser must satisfy the ERISA investment fiduciary standards and avoid conflicts of interest and/or operate under a prohibited transaction exemption. Also see **PTE 2020-02**.

Whether an adviser who makes a rollover recommendation is considered to give advice "on a regular basis" has been the source of much litigation. Various administrations have revised the DOL's fiduciary rule, and it remains unsettled. However the rule finally emerges, advisers should carefully weigh the manner in which they provide such rollover advice.

529 plan

A qualified tuition program (QTP), also referred to as a section 529 plan, is a program established and maintained by a state that allows a contributor either to prepay a beneficiary's qualified higher education expenses at an eligible educational institution or to contribute to an account for paying for education expenses. Contributions to a 529 account are taxable but investment earnings accrue tax-free, and distributions will not be taxable if used to pay for qualified higher education expenses. Employers may offer payroll deduction or other benefits associated with 529 plan contributions to their employees. Starting in 2024, 529 assets may be rolled over to a beneficiary's Roth IRA. Eligibility rules apply, including that the 529 account has existed for at least 15 years.

Active management

Where a person or team, often called the portfolio manager, actively makes investment decisions and initiates buying and selling of securities using analytical research, forecasts, and their own judgment and experience. The opposite of active management is called passive management, better known as "indexing."

Active share

A measure of how different a fund's portfolio is from its benchmark, determined by comparing the stocks held and their weightings with those of the benchmark.

Administrator

The party responsible for managing the day-to-day activities of the plan. This is often the plan sponsor (i.e., the employer). The plan sponsor may delegate these duties to a third party but retains overall responsibility to monitor the performance and suitability of any such service providers.

Administration and recordkeeping expenses

Fees for administrative and recordkeeping services pertaining to plan participants in a retirement plan. Plan administration fees may be paid by the employer or by plan assets.

For start-up or takeover plans, these fees typically include charges associated with processing information from the previous service provider and mapping participant information.

Adoption agreement

The portion of the plan document that contains all of the alternatives and options that may be selected by the employer.

ADP/ACP nondiscrimination tests

Nondiscrimination tests that apply to 401(k) plans. The Actual Deferral Percentage (ADP) test prohibits highly compensated employees (HCE) from making disproportionately greater elective deferral contributions to a 401(k) plan than non-highly compensated employees (NHCE). The Actual Contribution Percentage (ACP) test prohibits HCEs from making employee after-tax contributions and receiving employer matching contributions in disproportionately greater amounts than NHCEs.

Age-weighted allocation

A profit-sharing allocation formula designed to provide a greater benefit to older participants. (Also see **profit-sharing plan** definition.)

Allocation

The amount credited to a participant's account as a result of employer and employee contributions, forfeitures, and investment earnings.

Alpha

An expression of performance that measures the difference between a fund's actual returns and its expected performance given its level of risk as measured by beta.

Alternative investments

An investment that is not one of the three traditional asset types: stocks, bonds, and cash. Some examples of alternative investments include hedge funds, managed futures, real estate, commodities, and derivatives contracts.

Amendment

If a plan sponsor changes the plan's features after establishing the plan, the plan document must be amended to incorporate the new feature. This is a "discretionary" plan amendment and generally must be adopted by the end of the plan year in which the amendment is effective (As of the 2024 tax year, plan sponsors can make discretionary amendments to a plan until the tax return due date, including extensions, but only if the amendment increases participants' benefits.) If a new law or regulation requires plan documents to be amended, it is referred to as an "interim" plan amendment. The IRS will set the deadline by which plan sponsors must execute the required plan amendment. Both types of amendments are incorporated into the plan document with the next restatement. Also see **Restatement**.

Annual annuity fee

Fee charged for the distribution of plan proceeds as annuitized payments.

Annual audit

All plans with more than 100 participants are required by federal law to undergo an annual audit conducted by an independent auditor. A Department of Labor (DOL) or IRS examination of a plan is commonly referred to as a plan audit.

Annuity

A financial product that pays out a fixed stream of payments to an individual and is primarily used as an income stream for retirees. Annuities were primarily designed to be a reliable means of securing steady cash flow for an individual during their retirement years and to alleviate fears of longevity risk of outliving one's assets. Annuities are created and sold by financial institutions, which accept and invest funds from individuals. Annuities can be structured according to a wide array of details and factors, such as the duration of time that payments from the annuity can be guaranteed to continue. Annuities can be created so that, upon annuitization, payments will continue so long as either the annuitant or their spouse (if a survivorship benefit is elected) is alive. Alternatively, annuities can be structured to pay out funds for a fixed amount of time, such as 20 years, regardless of how long the annuitant lives. Buyers can purchase an annuity that offers an immediate payment or a deferred payment, depending on their individual retirement needs.

Annuitized payments

A distribution arrangement involving a series of payments made regularly over a specified time period.

Annuity and stable value/Guaranteed investment (interest) contract (GIC) surrender charges

Stable value (with GICs being the original product offering) is not available in a retail environment. It is, however, a staple of the defined contribution market — 401(k), 457 and 403(b) plans. GICs (see the **GIC** definition) are utilized to provide the stable value (book value) accounting and were typically group annuity products that offered annuity options to participants; some have provisions for early surrender charges. GICs, while still available, are not as prominent today. Current stable value funds utilize newer benefit responsive investment contract types, such as synthetic contracts offered by insurance companies or banks and separate account insurance products. Current insurance-based group annuity products are typically evergreen in nature with no stated maturity date.

While the group annuity products still offer annuities, the annuity features are rarely, if ever, used by participants. In some cases, stable value funds may experience surrender charges should the plan sponsor terminate a GIC or other benefit responsive contract. Participants who transfer away from stable value or terminate their stable value holdings never pay surrender charges.

Asset allocation

An investment strategy that seeks to balance risk and reward based on apportioning portfolio assets among three main asset classes (equities, fixed income and cash and equivalents, which frequently behave differently over time) according to an individual's goals, risk tolerance and investment horizon. Asset allocation cannot guarantee a profit or protect against loss.

Audit-DOL, IRS, CPA

While both the Department of Labor (DOL) and the Internal Revenue Service (IRS) perform plan audits, their enforcement powers are governed by different laws and regulations, and they focus on different issues. The DOL is responsible for the enforcement of labor laws, including ERISA. The DOL has the power to exact penalties for breaches of fiduciary conduct, and if it chooses, it can sue fiduciaries for these breaches on behalf of a plan. The DOL's investigation and enforcement emphasis is on fiduciary breaches and prohibited transactions. The IRS is responsible for the management of our tax system through the Internal Revenue Code (the Code) and has the power to enforce infractions under the Code. When infractions are found, it can impose taxes, penalties, and interest. The IRS's audit and enforcement emphasis is on compliance with the requirements of the Code, which rolls up under the umbrella of the plan's tax qualification. Both the DOL and the IRS select plans for audit primarily by random selection; however, (a) answers to certain questions on the Form 5500 may trigger an audit, (b) the DOL may refer a case to the IRS if it discovers compliance infractions that are subject to penalties and interest under the Code, (c) certain audit initiatives by the agencies may lead to audits for plans that fall within the initiative's criteria and (d) failure to respond to an IRS questionnaire could result in an audit. Essentially, if the DOL or IRS perceives some elevated risk of noncompliance, the chances for an audit will go up substantially.

In enacting ERISA in 1974, Congress included a requirement for employee benefit plans to file an annual report of their financial condition and operations with the DOL. Among other information, the plan's annual report must include an audit report stating whether the plan's financial statements (and other schedules required to be included in the annual report) are presented fairly in conformity with generally accepted accounting principles. As a practical matter, almost all plan audits are performed by Certified Public Accountants (CPAs). Almost all plans with over 100 participants must be audited annually in accordance with generally accepted auditing standards. Audited financial statements and the CPA's report on the fairness and consistency of their presentation must generally be filed with the Form 5500 Annual Report within 210 days after the close of the plan year. The audit requirement is intended to ensure the integrity of financial information that is incorporated in the annual reports.

Automatic deferral default percentage

The percentage of pay that is automatically deferred when an employee is enrolled in a plan through automatic enrollment. Automatic deferral default percentages typically range from 3-6% of pay but may increase to 15%. Generally, participants can choose to defer an amount other than the default percentage or to opt out of deferring entirely.

Automatic enrollment

A plan feature that allows an employer to enroll employees in a salary deferral plan without the employees' initial consent, as long as employees have the right to "opt out" of contributing to the plan. Also known as "negative election."

Under the SECURE 2.0 Act, most retirement plans established on or after December 29, 2022, will have to include an automatic enrollment feature beginning with the 2025 plan year. Plans that were established before that date are not required to add this provision. New businesses, small businesses (with 10 or fewer employees), and certain other entities are exempt from this requirement.

Auto escalation

A plan which automatically increases the percentage of participants' salary deferrals, typically on an annual basis. This type of plan generally features a default or standard contribution escalation rate; participants have the right to opt out.

Balanced fund

A fund portfolio that combines a stock component, a bond component and, sometimes, a money market component. These hybrid funds generally maintain a relatively fixed mix of stocks and bonds that is either moderate (higher equity component) or conservative (higher fixed-income component).

Basic Plan Document (BPD)

In a pre-approved plan, the portion of the plan document that contains all of the nonelective provisions. The BPD cannot include any options or blank spaces for the employer to complete.

Basis point (BP)

A unit of measure used to describe the percentage change in the value or rate of a financial instrument. One basis point is one-one-hundredth of a percentage point, or 0.01%. If the US Federal Reserve increases its short-term interest rate target by 50 basis points, or a bond's yield rises by 50 basis points, the change would be 0.50% or one-half of one percent.

Behavioral finance

Behavioral finance is a field of finance that proposes psychology-based theories to explain stock market anomalies such as severe rises or falls in stock price. Within behavioral finance, it is assumed the information structure and the characteristics of market participants systematically influence individuals' investment decisions as well as market outcomes.

Benchmarking

A quality assurance tool allowing organizations to compare themselves to others regarding some aspect of plan design or performance, with a view to finding ways to improve. The SECURE 2.0 Act requires the Department of Labor to update its benchmarking regulations by December 2024 to promote better comparisons of mixed asset classes, which should help participant decision-making.

Beneficiary

The party designated by a participant — or the terms of a plan — to receive the retirement plan benefits of a deceased participant.

Best interest contract exemption (BICE)

The DOL fiduciary rule allowed Advising Fiduciaries to receive commissions and other variable compensation so long as the Advising Fiduciaries and their firms met the conditions of the prohibited transaction exemption referred to as the best interest contract exemption (BICE). This included providing disclosure to plan sponsors about potential conflicts of interest associated with that compensation, and how the firm planned to address those conflicts to ensure that the plan and its participants received advice recommendations that were in their best interests. The BICE outlined the requirements for firms and Advice Fiduciaries. The BICE also applied to Advising Fiduciaries providing advice recommendations regarding rollovers into IRAs, and to IRA owners. The DOL fiduciary rule and BICE were invalidated by the US Fifth Circuit Court of Appeals in a decision rendered on March 15, 2018, reinstating the 5-part test. Also see the **5-Part Test** and the **DOL fiduciary rule** definition. In the fall of 2023, the DOL submitted a new proposed rule to the Office of Management and Budget, stating that it would more appropriately define when recommendations constitute investment advice.

Beta

A measure of volatility, or risk, relative to the index. By definition, the index beta is one. A beta greater than one implies the fund has been more volatile than the index; a beta of less than one implies the fund has been less volatile than the index.

Blackout period

A period during which plan participants cannot access their accounts. A blackout period may occur due to a change in plan providers, recordkeepers, trustees or company status, or during the valuation process. The blackout period can also be referred to as lockdown, transitional period or quiet period. Plans subject to ERISA that allow participants to direct their own investments must provide a notice to participants if a blackout period will last more than three consecutive business days.

Break in service

Typically, a one-year break in service is defined as a period of 12 consecutive months during which an employee is not credited with more than 500 hours of service.

Bundled services

An arrangement in which plan service providers charge an all-inclusive fee for 401(k) plan establishment, investment services and administration. Bundled services are priced as a package and generally are not priced on a per-service basis.

Cafeteria plan (Section 125)

A plan permitting pretax payment of employee benefits. Section 125 of the IRC defines all benefits that may be paid pretax. Examples of such benefits include health, dental, disability and dependent care.

CARES Act

Acronym for the Coronavirus Aid, Relief, and Economic Security Act. Signed into law on March 27, 2020, the Act was the largest economic relief bill in US history and allocated $2.2 trillion in support to individuals and businesses affected by the pandemic and economic downturn. Among other things, the Act gave direct payments to individuals, boosted unemployment insurance, provided tax relief to businesses, bolstered health care infrastructure, provided student loan relief, and made several changes to retirement savings policy that allowed plan participants to access cash for emergencies. Among the Act's retirement-related provisions, it waived the 10% additional tax for early distributions from retirement plans and individual retirement accounts (IRAs) associated with any "coronavirus-related distribution" taken by qualifying employees in 2020 for amounts not to exceed $100,000, allowed expanded plan loans for qualifying employees, waived required minimum distributions (RMDs) payable in or for 2020, generally gave plan sponsors until the end of the 2022 plan year to adopt related amendments, delayed single-employer funding obligations for defined benefit plans due during 2020 to Jan. 1, 2021 (with interest for late payments) and extended IRC Section 127 (which currently allows for tuition reimbursement up to $5,250/year) to apply to student loan repayments for employees, with no tax implications.

Cash balance plan

A defined benefit plan that defines the benefit in terms that are more characteristic of a defined contribution plan. In other words, a cash balance plan defines the promised benefit in terms of a stated account balance. In a typical cash balance plan, a participant's account is credited each year with a "pay credit" (such as 5% of compensation from his or her employer) and an "interest credit" (either a fixed rate or a variable rate that is linked to an index such as the one-year treasury bill rate). Increases and decreases in the value of the plan's investments do not directly affect the benefit amounts promised to participants. Thus, the investment risks are borne solely by the employer. When a participant becomes entitled to receive benefits under a cash balance plan, the benefits that are received are defined in terms of an account balance. When the participant decides to retire, he or she would have the right to an annuity based on that account balance. In many cash balance plans, however, the participant could instead choose (with consent from his or her spouse) to take a lump-sum benefit equal to the account balance. If a participant receives a lump-sum distribution, that distribution generally can be rolled over into an IRA or to another employer's plan if that plan accepts rollovers. Also see **Defined benefit plan** and **Defined contribution plan**.

Cash or deferred arrangement (CODA)

Any direct or indirect election made by an employee to the employer to either receive an amount in the form of cash or other taxable benefit or contribute the amount to a trust, thus deferring the receipt of compensation. The election generally remains in force until the participant either changes the election through written or approved electronic means or ceases to be an employee of the employer that sponsors or adopted the plan. Most commonly, CODAs allow employees to contribute a portion of their salaries to a 401(k) plan so that their savings can grow on a tax-deferred basis. According to the IRS, a CODA is effective as of the first day of the plan year. However, a deferral may not be retroactive.

Catch-up contributions

Contributions that permit individuals 50 or older to make additional elective deferral contributions in excess of the 402(g) limit, the 415 limit or any other limit imposed by the terms of a tax-qualified retirement plan. Catch-up contributions were established by the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA). The maximum amount of annual catch-up contributions is adjusted annually to reflect increases in the cost of living. 403(b) plans and 457(b) plans may also allow for other catch-up contributions. In 2025, the SECURE 2.0 Act increases the catch-up contributions allowed for those attaining age 60-63. In addition, starting in 2024 those earning over $145,000 (indexed) will be required to make catch-up contributions as Roth contributions.

Cliff vesting

A vesting schedule in which the participant is not vested in his or her right to employer contributions made to his or her plan account until completing the number of years required by the plan. While graded vesting schedules are graduated (20%, 40%, 60%, etc.), cliff vesting is not (0%, 0% and 100%). Three years is the maximum length permitted for a cliff vesting schedule for a defined contribution plan.

COLA

Acronym for cost-of-living adjustment, which refers to periodic (generally annual) changes in wages, benefits or contribution levels. The IRS issues COLAs, which are designed to compensate for the effects of inflation.

Collective investment trusts

A tax-exempt, pooled fund, operated by a bank or trust company that commingles assets of retirement plans for which the bank provides fiduciary services. Also known as collective trust funds.

Commission

A fee paid to a broker or other intermediary for executing a trade.

Compliance testing

Testing required by the IRS to ensure that non-highly compensated employees (NHCEs) benefit enough from the plan relative to the benefit received by the highly compensated employees (HCEs). (Also see **HCE** and **NHCE** definitions.)

Conflict of interest

A conflict between the private interests and the official responsibilities of a person in a position of trust.

Contract administration charge

A charge for administering an insurance/annuity contract, often including costs associated with participant account maintenance and all investment-related transactions initiated by participants.

Contract termination charge

A charge to the plan for “surrendering” or “terminating” an insurance/annuity contract prior to the end of a stated time period. The charge typically decreases over time. This type of charge is rarely seen anymore except in indexed annuities.

Controlled group

When two or more businesses are under common control, meaning one entity owns at least 80% of the stock, profit or capital interest in the other organization, or when the same five or fewer people own a controlling interest in each entity.

Conversion

The process of changing from one service provider to another.

Corrective distribution

A distribution of excess contributions or excess aggregate contributions made as a result of failure of the plan's annual ADP or ACP testing. These limits are plan, not individual limits. The determination of whether these limits have been exceeded is performed after year-end based on total participant compensation and contributions during the year. These corrective distributions must include allocable earnings or losses through the end of the plan year in which the contribution was made. The corrective distributions plus allocable earnings are taxable to the participant in the year the distribution is made. The gross corrective distribution amounts and taxable amounts are both reported on Form 1099-R to assist in reporting on a participant's personal income tax return. Also see **ADP/ACP nondiscrimination tests**.

Cross-testing

Generally, refers to nondiscrimination testing performed on a defined contribution plan by projecting the contributions to retirement age, converting the projected account balances to monthly benefits, and comparing the benefits. Examples of cross-tested plans include age-weighted or new comparability plans.

Custodian

A person or entity that has lawful custody of plan assets for another individual or entity. The custodian's responsibility is to track and hold the plan's securities. Financial institutions — such as trust companies, banks, or mutual fund companies — and insurance companies often serve as custodians.

Custody fee

Fee for the safekeeping of plan investments.

DCIO

Acronym for the "defined contribution investment only" business, which refers to investment management mandates, awarded within qualified retirement plans such as 401(k), 403(b) and 457 plans.

Defined benefit plan

An employer-sponsored retirement plan that pays a specific amount to a retired employee. The amount to be paid to the retired employee is usually based on a formula that takes salary history and years of service into account. The employer bears the investment risk because the plan promises a specific benefit. If plan assets (including employer contributions and investment earnings) are insufficient to fund benefit payments to plan participants, the employer must generally contribute the difference.

Defined contribution plan

An employer-sponsored retirement plan, such as a 401(k) or profit-sharing plan, that is funded by employer contributions, employee elective deferrals or both. Unlike defined benefit plans, the participants bear the investment risk because the plan does not promise a specific benefit. Instead, it promises to pay the employee the amount in his or her account, which is the sum of contributions and investment earnings.

Determination letter

A letter issued by the IRS acknowledging that the IRS has reviewed the plan document and determined it to be in compliance. A letter of determination may be relied on as proof of having a qualified plan document in good order. Determination letters are now issued only for individually designed plans and in certain narrow circumstances.

Direct compensation

Compensation that the service provider receives directly from the plan. This includes payments made directly from the plan for services rendered to the plan or because of a service provider's position with the plan.

Discretionary contributions

Amounts an employer may — but is not obligated to — contribute to a plan. Discretionary contributions can be profit-sharing or matching contributions.

Distribution

A lump-sum or periodic payment paid to a participant or beneficiary as required under the terms of a retirement plan.

Distribution expense

The costs typically associated with processing distributions from plan assets to a participant, including required filings (1099 and 945).

Diversification

A risk management technique that mixes a variety of investments within a portfolio. The rationale for this technique is that different kinds of investments will, on average, result in higher returns with lower risk than any individual investment in the portfolio because positive performance of some investments will neutralize the negative performance of others. Diversification cannot guarantee a profit or protect against loss.

DOL

Acronym for Department of Labor, which enforces legislation that regulates private employers who offer pension or welfare benefit plans for their employees. The DOL and IRS work cooperatively to enhance plans' compliance with ERISA and with their tax-qualification status under the IRC.

DOL fiduciary rule

A DOL regulation went into effect in June 2017 and expanded the definition of who is an Advising Fiduciary under ERISA Sec. 3(21). It incorporated plans and accounts that were previously governed only by the IRC (such as IRAs). The DOL fiduciary rule applied a fiduciary standard to Advising Fiduciaries and their firms who provide any advice recommendations to plan sponsors, plan participants or their beneficiaries, and IRA owners. The rule resulted in retirement investors receiving new disclosures from firms and Advising Fiduciaries about the way in which they do business and avoid conflicts of interest, and new content in the agreements firms use to open retirement accounts.

The DOL fiduciary rule (as described above), including the associated best interest contract exemption (BICE), was invalidated (i.e., struck down in its entirety) by the US Fifth Circuit Court of Appeals in a decision rendered on March 15, 2018 and made effective by court mandate in June 2018.

The DOL has created a new proposed fiduciary rule (pending review by the Office of Management and Budget) that is intended to clarify when certain recommendations constitute investment advice. Because the SEC has its own standards of conduct for broker-dealers and investment advisers, many hope that the DOL will coordinate its fiduciary rule with the SEC's. See also **5-Part Test** and **PTE 2020-02**.

Downside capture ratio

A statistical measure of an investment manager's overall performance in down-markets that is used to evaluate how well the manager performed relative to an index during periods when that index has dropped. The ratio is calculated by dividing the manager's returns by the returns of the index during the down market and multiplying that factor by 100.

Education program expenses

Costs associated with providing print, video, software, and live instruction to educate employees about their retirement plan, the plan's investment funds and asset allocation strategies. There may be a one-time cost associated with implementing a new plan, as well as ongoing costs for an existing program. Fees may be charged as specific line items or may be part of the service schedule related to investment and/or recordkeeping fees.

EGTRRA

Acronym for the Economic Growth and Tax Relief Reconciliation Act of 2001, which made significant changes in several areas, including income tax rates, estate and gift tax exclusions and retirement and qualified plan rules. In general, the act simplified retirement and qualified plan rules for individual retirement accounts (IRAs), 401(k) plans, 403(b) and pension plans.

Elective deferral

Payroll deduction contributions made by an employer on behalf of an employee pursuant to an election by the employee to have such a contribution made in lieu of cash compensation, which is otherwise payable to the employee.

Eligible employee

An employee who meets a plan's age and service requirement provisions for participation.

Eligible investment advice arrangement

An arrangement that provides that fees (including any commission or other compensation) a fiduciary adviser receives for investment advice or investment of plan assets either do not vary according to the investment option selected or are based on a computer model under an investment advice program that meets regulatory requirements.

Employee Benefit Security Administration (EBSA)

An agency of the Department of Labor responsible for protecting the integrity of retirement plans, health plans and other employee benefits.

Enrollment expenses

Costs associated with enrolling employees in a retirement plan and providing materials to educate them about the plan. There may be a one-time cost associated with implementing a new plan, as well as ongoing enrollment costs. Fees may be charged as a specific line item or may be part of the service schedule related to investment, conversion and/or recordkeeping fees.

ERISA

Acronym for the Employee Retirement Income Security Act of 1974, which is the federal law that sets minimum standards for most voluntarily established retirement and health plans to provide protection to the plan participants and plan assets. The DOL has both the responsibility to issue regulatory guidance and the authority to enforce the law and regulations.

ESG (environmental, social and governance)

Environmental, social, and governance (ESG) are non-financial factors investors and fund managers use to screen potential investments. Environmental criteria consider how a company safeguards the environment, including corporate policies addressing climate change, for example. Social criteria examine how it manages relationships with employees, suppliers, customers, and the communities where it operates. Governance deals with a company's leadership, executive pay, audits, internal controls, and shareholder rights.

ETFs

An acronym for exchange-traded funds, which are investment portfolios that trade like stocks on an exchange and usually track an index.

Exclusive benefit rule

The ERISA standard that requires plan fiduciaries to act solely for the benefit of the plan participants and beneficiaries.

Expense ratio

The cost of administering and managing investments expressed as a percentage of total assets.

Factor-based investing

Factor investing (also known as smart beta) is an investment strategy in which securities are chosen based on certain characteristics and attributes.

Fidelity bond

A bond required by ERISA Section 412 for each fiduciary who handles plan assets. A fidelity bond is designed to protect a retirement plan's participants in the event a fiduciary or other responsible person steals or mishandles plan assets. Each plan official must be bonded for at least 10% of the amount of assets they handle. The minimum bond amount is $1,000 per plan official. The maximum bond amount with respect to any one plan official is $500,000 per plan ($1,000,000 for plans that hold employer securities). Also called a surety bond.

Fiduciary

Plan fiduciaries are those persons or entities who exercise discretionary control or authority over plan management or plan assets, anyone with discretionary authority or responsibility for the administration of a plan, or anyone who provides investment advice to a plan for compensation or has any authority or responsibility to do so are subject to fiduciary responsibilities. Plan fiduciaries include, for example, plan trustees, plan administrators, and members of a plan's investment committee.

The primary responsibility of fiduciaries is to run the plan solely in the interest of participants and beneficiaries and for the exclusive purpose of providing benefits and paying plan expenses. Fiduciaries must act prudently and must diversify the plan's investments in order to minimize the risk of large losses. In addition, they must follow the terms of plan documents to the extent that the plan terms are consistent with ERISA. They also must avoid conflicts of interest. In other words, they may not engage in transactions on behalf of the plan that benefit parties related to the plan, such as other fiduciaries, services providers or the plan sponsor.

The fiduciary duty is the highest standard of care in the law, and those who do not follow these principles of conduct may be personally liable to restore any losses to the plan, or to restore any profits made through improper use of plan assets. Courts may take whatever action is appropriate against fiduciaries who breach their duties under ERISA including their removal.

Fiduciary insurance

Insurance that protects plan fiduciaries in the event that they are found liable for a breach of fiduciary responsibility. Fiduciary insurance coverage is optional.

Financial wellness

Financial wellness is a state of being in which you can fully meet your current and future financial obligations while feeling secure in your financial future and making choices that allow you to enjoy life.

Finder's fee

A commission paid to an intermediary or the facilitator of a transaction. The finder's fee is rewarded because the intermediary discovered the deal and brought it forth to interested parties. Depending on the circumstance, the finder's fee can be paid by either the transaction's buyer or seller.

Forfeiture

The non-vested portion of a participant's account balance that is relinquished upon termination of employment.

Form 1099-R

A form sent to the recipient of a plan distribution and filed with the IRS to document the distribution amount, the withheld amount (if any), and the distribution reason.

Form 5500

A form that employee benefit plans subject to ERISA must file annually with the IRS. Fees to prepare Form 5500 are usually included in recordkeeping and administration charges.

Front-end load

Sales charges resulting from the purchase of an investment such as a stock or mutual fund.

General account

In a general account structure, assets are invested in and owned by the insurance company's general account. This means the entire general account of the insurance company, and effectively the ultimate claims-paying ability of the insurer, supports the contract guarantees. The assets in a general account are not attributable to any single policyholder or liability, and ERISA excludes the assets supporting these contracts from the definition of plan assets and treatment as plan assets.

Glide path

Refers to a formula that defines the asset allocation mix of a target-date fund, based on the number of years to the target date (which is typically a year in which the investor expects to reach their objective, such as retirement). The glide path creates an asset allocation that typically becomes more conservative (i.e., includes more fixed-income assets and fewer equities) as a fund gets closer to the target date. Also see **Target-date fund**.

Group annuity

A series of pooled investment accounts offered by an insurance company that are unitized into shares in order to be reflected on a daily valued 401(k) recordkeeping system. There are two types of group annuity platforms. The first one invests the pooled accounts exclusively in shares of retail mutual funds. Because these pooled accounts are invested only in shares of a particular mutual fund, the value fluctuation is almost identical to that of the actual fund. The only difference is an asset charge or contract fee imposed in addition to the mutual fund expenses. The second type is a sub-advised arrangement in which the pooled accounts are managed with objectives similar to those of a particular mutual fund or managed portfolio but are not invested in the actual fund itself. These sub-advised funds may either be exclusive to one particular financial institution or made available to a select number of banks and insurance company platforms. Group annuities are also used in stable value products.

Guaranteed Investment (interest) Contract (GIC)

A contract between an insurance company and a corporate profit-sharing or pension plan under which the insurance company guarantees a specific rate of return over the life of the contract. GICs are used less frequently in stable value than synthetic contracts.

GUST

Acronym for several pieces of legislation passed since 1994, including the Uruguay Round General Agreement on Tariffs and Trade (GATT), the Uniformed Services Employment and Reemployment Rights Act of 1994 (USERRA), the Small Business Job Protection Act of 1996 (SBJPA), the Taxpayer Relief Act of 1997, the IRS Restructuring and Reform Act of 1998 and the Community Renewal Tax Relief Act of 2000.

Hardship distribution

Plan permitting, a participant may withdraw from their plan account prior to retirement if they experience an "immediate and heavy financial need" and demonstrate that a hardship distribution is necessary to satisfy the financial need. Most plans use the regulatory safe harbor rules for hardship distributions, which deem the following to meet the immediate and heavy financial need requirement: uninsured medical expenses for the participant, a spouse or eligible dependents; purchase of a primary residence (excluding mortgage payments); payment of post-secondary tuition costs for the participant, a spouse or eligible dependents; payments necessary to avoid foreclosure or eviction from the participant's principal residence; funeral expenses for the employee, a spouse, dependents, or beneficiary of the employee; certain damage repair expenses for the employee's principal residence; or expenses or losses incurred if the employee's residence or place of employment was in a federally declared disaster area.

Plan sponsors must follow a general standard for determining whether the hardship distribution is necessary to satisfy the financial need.

- The hardship may not exceed the amount of need, plus taxes and penalties.
- The participant must have obtained all other plan distributions available (other than loans, unless required by the plan).
- The participant must represent in writing that they don't have the cash or liquid assets to satisfy their financial need, and the plan administrator does not have actual knowledge to the contrary.

These distributions are taxable and are generally subject to a 10% penalty tax if the participant is under 59½. Hardship distributions are not eligible for rollover.

For plan years beginning after December 29, 2022, the SECURE 2.0 Act allows plan administrators to accept self-certification from participants that a distribution qualifies as a hardship distribution and that they have no alternative means to satisfy their financial needs.

HCE

Acronym for highly compensated employee, who meets one of the following conditions:

- Owned more than 5% of the employer business at any time during the year or preceding year.
- For the preceding year, received compensation of more than a specified dollar amount that is adjusted annually to reflect increases in the cost of living, and if elected by the employer, was in the top 20% of employees when ranked by compensation.

Health Savings Account (HSA)

A Health Savings Account (HSA) is a tax-advantaged account created for individuals who are covered under high-deductible health plans (HDHPs) to save for medical expenses that HDHPs do not cover. Contributions are made into the account by the individual or the individual's employer and are limited to a maximum amount each year because they are tax-deductible. The contributions are invested over time and can be used tax-free at any time to pay for qualified medical expenses, which include most medical care plus dental, vision, and certain over-the-counter medicine expenses.

IAR

Acronym for investment advisory representative, an investment advisory company employee whose main responsibility is to provide investment-related advice. IARs must be registered with state authorities and can provide advice only about topics for which they have passed appropriate examinations.

Index

An index is an indicator or measure of something, and in finance, it typically refers to a statistical measure of change in a securities market. In the case of financial markets, stock and bond market indices consist of a hypothetical portfolio of securities representing a particular market or a segment of it.

Indirect compensation

Compensation received by service providers to a plan from sources other than the plan or plan sponsor. Indirect compensation information that must be provided by service providers to plan sponsors under DOL Rule 408(b)(2) includes soft dollars, float, charges to plan participant accounts, and income from investment option sponsors. It includes money or "anything else of value" received by a service provider in connection with services provided to the plan.

Individually designed plan

A plan established pursuant to a document that is not a pre-approved document. (Also see **pre-approved documents** definition.) In general, individually designed plan documents are more costly to establish and maintain than pre-approved plan documents because they are generally drafted for and used by one employer vs. many employers.

Individually managed account

An investment account managed for a single participant based on individual preferences.

In-service withdrawal

In-service withdrawal, also known as early distribution, occurs when an employee takes a withdrawal of funds from a qualified employer-sponsored retirement plan (if permitted by the plan) while still working or before experiencing a distribution-triggering event (e.g., retirement at normal retirement age, death, disability, or plan termination). A common in-service withdrawal would be a distribution to the participant who is stil working but who has reached age 59 1/2.

Installation fee

A one-time fee charged by some vendors for initiating a new plan.

Investment advice

Refers to any recommendations regarding an investor's portfolio. See definitions for **DOL fiduciary rule** and **fiduciary**.

Investment management fee

See **Management fee** definition.

Investment manager

A fiduciary other than a trustee or a named fiduciary who:

- Has the power to manage, acquire or dispose of any asset of the plan.
- Is registered as an investment adviser under the Investment Advisers Act of 1940; is registered as an investment adviser under the laws of the state where the principal office and place of business is located; is a bank; or is an insurance company qualified to perform services under the laws of more than one state.

- Has acknowledged in writing that he is a fiduciary with respect to the plan. Also see **3(38) investment manager**.

Investment mapping

The process of keeping plan assets invested while changing service providers. This is typically done by ensuring that investment of plan assets maintains the strategy and objective used by the previous provider. For example, assets invested in large-cap growth stocks would remain invested in that asset class under the new provider.

Investment policy statement

The document that provides guidelines for the plan's investment management. It typically sets forth the plan's investment objectives, investment strategies, policies, and investment limits.

Investment transfer expense

Charge associated with a participant changing investments and/or investment allocation.

Involuntary cash-outs

Plan sponsors may adopt a plan provision that allows them to cash out account balances up to $5,000 ($7,000 starting with distributions in 2024) without a participant's consent if the participant terminates employment and does not make a decision regarding the distribution of their plan account. Cash-outs, also referred to as mandatory distributions, between $1,000 and $5,000 ($7,000 starting in 2024) must be automatically rolled over to an IRA on behalf of the participant. Balances of $1,000 or less may either be rolled over to an IRA or cashed out and sent to the participant, depending on the option chosen by the plan sponsor in the plan document. If a plan sponsor meets the DOL's safe harbor requirements for automatic rollovers, the plan sponsor is released from fiduciary responsibility for those assets when they are deposited in the safe harbor IRA on behalf of the participant.

IRC

Acronym for the Internal Revenue Code (IRC), which contains the federal tax laws enacted by Congress in Title 26 of the United States Code.

IRS Form 5500

See **Form 5500** definition.

Keogh plan

A term that is sometimes used to refer to a tax-deferred retirement account for self-employed individuals or employees of unincorporated businesses. It can be established as either a defined contribution or a defined benefit plan. The term is derived from the Congressman who sponsored the bill, and is also known as an H.R. 10 plan.

Key employee

A key employee is any employee (including former or deceased employees), who at any time during the plan year was:

- An officer of the company that sponsors the plan and earns income in excess of a specified dollar amount that is adjusted annually to reflect increases in the cost of living,
- Who owns more than 5% of the business that sponsors the plan, or
- An employee owning more than 1% of the business that sponsors the plan, with income over $150,000 for the plan year.

Liability driven investment (LDI)

LDI is a form of investing in which the main goal is to gain sufficient assets to meet all liabilities.

Life cycle fund

A diversified mutual fund or collective trust designed to offer an appropriate level of risk during different phases of life. Target-risk and target-date funds are two examples of life cycle funds. A target-risk fund targets a specific risk profile (for example, conservative, moderate or growth), while a target-date fund targets a specific future date and generally becomes more conservative over time until it reaches its final risk profile.

Loan fees

Vendors may charge a fee when a plan loan is originally taken, as well as an ongoing fee for administration.

Longevity risk

The risk that the amount of money a person has saved for retirement might not be enough due to increased life expectancy.

Management fee

Fee charged by an investment manager.

Master plan

A form of retirement plan document, sponsored by a financial institution and made available to employers, that had already been examined and approved by the IRS. A master plan required adopting employers to use the same trust or custodial account, whereas employers using a prototype plan document had separate trusts or custodial accounts. The terms “master” and “prototype” and “volume submitter” were eliminated with the Cycle Three Restatements by Revenue Procedure 2017-41 and replaced with a single term: “pre-approved plan.” Pre-approved plan documents are either standardized or non-standardized.

Market value adjustment (MVA)

An adjustment to the market value of an annuity contract to account for increases/decreases in interest rates when an early withdrawal or surrender occurs.

Money market

Refers to trading in very short-term debt investments. At the wholesale level, it involves large-volume trades between institutions and traders. At the retail level, it includes money market mutual funds bought by individual investors and money market accounts opened by bank customers. In any case, the money market is characterized by a high degree of safety and a relatively low return in interest.

Money purchase plan

A defined contribution plan that requires the plan sponsor to make contributions on behalf of each participant based on the plan's formula, which is specified in the plan's document. Contributions must be made to a money purchase pension plan regardless of the profitability of the sponsor. Historically, money purchase pension plans were paired with profit sharing plans to increase the potential employer contribution. But law changes allowed standalone profit sharing plans to achieve the same result, so money purchase pension plans are becoming much less common.

Mortality risk and administrative expense

A variable annuity fee that covers the cost of returning principal in case the annuitant dies.

Modern portfolio theory (MPT)

MPT, pioneered by Harry Markowitz in 1952, asserts that risk-averse investors can construct portfolios to maximize expected return based on a given level of market risk. According to the theory, it's possible to construct an "efficient frontier" of optimal portfolios offering the maximum possible expected return for a given level of risk. MPT cannot guarantee a profit or protect against loss.

Multiple employer plan (MEP)

An MEP is a qualified retirement plan established and administered by an MEP sponsor or organizer, who makes the plan available to two or more separate employers who are not members of a controlled group or under common control. If the plan meets certain requirements in the Internal Revenue Code and ERISA, the plan will be treated as a single plan administered by the MEP sponsor, instead of a series of separate plans administered by each participating employer. Historically, to be treated as a single plan, only employers who shared a common interest, based on the entity sponsoring the MEP, could join (e.g., employers in a trade or industry association, or a professional employer organization (PEO)). Because of this requirement, these MEPs have been referred to as "closed MEPs." Under the SECURE Act of 2019 (SECURE 1.0), pooled employer plans (PEPs) were created to allow unaffiliated businesses to participate in the same retirement plan. This change opened the door for many businesses to establish a retirement plan in conjunction with other businesses (See also **Pooled employer plan (PEP)**).

Negative election

See **automatic enrollment** definition.

New comparability allocation

A type of allocation formula for profit-sharing plans that allocates disproportionately greater amounts of the employer contribution to a specific group of employees. (Also see **profit-sharing plan** definition.) The formula is generally designed to maximize the amounts allocated for HCEs within the contribution nondiscrimination limits established by the IRC.

New comparability profit-sharing plan with a safe harbor 401(k)

A plan that combines a new comparability allocation formula with safe harbor 401(k) provisions.

NHCE

Acronym for non-highly compensated employee, which includes employees who do not meet the criteria for an HCE.

Nondiscrimination testing

Various types of nondiscrimination tests applicable to employer-sponsored, tax-qualified retirement plans under the IRC. The tests are generally designed to prevent HCEs from receiving disproportionately greater benefits than NHCEs. The ADP/ACP nondiscrimination tests are two examples.

Nondiscrimination testing expense

Costs associated with the process of nondiscrimination testing to determine whether the plan is in compliance. These costs are often included in recordkeeping and administration fees.

Nonqualified deferred compensation plan

A written agreement between an employer and employee that gives the employee the employer's unsecured promise to pay some future benefit in exchange for services today. Because it is nonqualified, it does not fall under ERISA, meaning it does not receive favorable tax treatment and can freely discriminate. Most nonqualified deferred compensation plans cover only highly paid executive employees.

Nonqualified plan

A retirement plan that doesn't meet the requirements of the IRC to qualify for tax-favored treatment.

Open architecture

A platform that allows for a myriad of investment choices for a plan to utilize for its participants. Instead of offering a set group of funds to pick from, there are usually thousands to choose from.

Opinion letter

A written statement from the IRS as to the acceptability of a pre-approved plan document. An opinion letter addresses only the form (text) of the plan; it cannot address whether the plan is in operational compliance with qualification requirements.

Orphan plan

A defined contribution plan for which there is no plan sponsor or other plan fiduciary willing to act with respect to the plan.

Participant

An employee who is eligible to participate in an employer-sponsored retirement plan. Generally, an employee who is eligible to elect to have his or her employer make elective deferral contributions to a 401(k) plan — but chooses not to — is still considered a participant.

Passive management

Passive investment management strategies attempt to replicate the performance of a predetermined benchmark. This strategy is also known as indexing.

Payroll deduction IRA

If an employer offers a payroll deduction IRA program, an employee can elect to have the employer withhold an amount from the employee's paycheck and deposit it into an IRA established by the employee

PBGC

Acronym for Pension Benefit Guaranty Corp., which was established by ERISA to ensure that benefits will be payable to participants when due if the sponsor of a defined benefit pension plan is unable to make payments. Companies that sponsor defined benefit plans pay premiums to PBGC based on the number of employees in the plan and the current ratio of assets to liabilities in the plan.

Permitted disparity (integrated) allocation formula

A profit sharing allocation formula that tax-qualified retirement plans may use to integrate a participant's benefits under the plan with his or her benefits or contributions under Social Security. May be used with defined benefit plans and defined contribution plans. In general, plan participants who earn compensation in excess of the Social Security taxable wage base (or other level set by the plan) receive a greater profit sharing allocation on their compensation above the taxable wage base and a lower percentage on their compensation below the taxable wage base. This allocation formula is nondiscriminatory if the difference between the base contribution percentage and excess contribution percentage does not exceed the maximum permitted disparity. (Also see **profit-sharing plan** definition.)

Plan administrator

The person or firm responsible for the administration of a retirement plan, determination of eligibility for benefits and payment of benefit claims is a fiduciary under ERISA. (See **3(16) Plan Administrator**.)

Plan document/IRS filing fee

Costs associated with preparing and filing required IRS documentation, including the request for a determination letter.

Plan sponsor

A business, employer organization, public entity or nonprofit organization that sponsors a retirement plan and is ultimately responsible for its administration.

Pooled employer plan (PEP)

Effective January 1, 2021, a Pooled Employer Plan (PEP) is a type of defined contribution multiple employer plan (MEP) that does not have a commonality requirement for adopting employers; any employer can join a PEP. To be treated as a single plan under ERISA, a PEP must be sponsored by a Pooled Plan Provider (PPP). The PPP must

- Register with the DOL and IRS,
- Be designated as the named fiduciary and the ERISA 3(16) plan administrator responsible for ensuring the PEP meets the requirements of ERISA and the tax code, and

- Be bonded and ensure that other entities acting as fiduciary to the PEP are bonded.

A PEP may sometimes be referred to as an "open MEP." (Also see **Multiple employer plan (MEP)**.)

Portability

Refers to an employee's option to retain certain benefits when switching employers. Some pension plans and health insurance have portability. Most 401(k) plans also have portability of benefits, as do health savings accounts (HSAs). Retirement plans are made portable through qualified rollovers into a new 401(k) or individual retirement account (IRA).

Portfolio construction

Portfolio construction is a disciplined, personalized process. In constructing a portfolio, the individual risk and return characteristics of the underlying investments must be considered along with the investor's unique needs, goals, and risk considerations.

PPA

Acronym for the Pension Protection Act of 2006, legislation that affected qualified retirement plans, plan sponsors and plan participants. It contained extensive new rules governing the implementation of automatic enrollment plans, cash balance and other hybrid plans and combined defined benefit pension/401(k) plans for small employers. The act also included changes affecting retirement plan contributions and distributions, including liberalization of plan rollover rules and new disclosure and reporting rules for ERISA-covered plans, including fiduciary protection for providing certain investment advisory services to participants.

Pre-approved plan documents (also see Prototype documents)

Plan documents that provide standard language for different types of retirement plans that offer flexible options within each plan type. Pre-approved plan documents are drafted and sent to the IRS for approval before being made available through plan providers for adoption by employers to create a plan. Beginning with the Cycle 3 Restatement, the IRS eliminated the terminology "prototype," "master plan" and "volume submitter" (Revenue Procedure 2017-41). Plans are now referred to as standardized or non-standardized pre-approved plans. Standardized plan documents are less flexible than non-standardized plan documents. Employers who adopt standardized plans are not required to obtain additional IRS approval (letter of determination) for their plan documents. Employers are permitted to make minor modifications to non-standardized pre-approved plan documents and may want to obtain a determination letter from the IRS.

Profit-sharing plan

A defined-contribution plan that permits the employer to make discretionary contributions. A participant's retirement benefits are based on his or her account balance, which consists of profit-sharing contributions, investment earnings and forfeitures. (Also see **age-weighted allocation**, **new comparability allocation**, **permitted disparity (integrated) allocation formula** and **salary ratio allocation** definitions).

Prohibited transaction exemption

A prohibited transaction is a transaction between a plan and a disqualified person that is prohibited by law — either the IRC or ERISA. The Department of Labor may issue individual and class exemptions from the prohibited transaction rules under the tax Code or ERISA. A prohibited transaction exemption (PTE) allows disqualified persons to conduct an otherwise prohibited transaction if they meet the requirements or conditions prescribed in the exemption. (Also see **PTE 2020-02**.)

Prototype documents

A form of retirement plan document, sponsored by a financial institution and made available to employers, that had already been examined and approved by the IRS. A prototype plan document provided standard language for different types of retirement plans that offer flexible options within each plan type. Employers who adopted prototype plans were not required to obtain IRS approval (letter of determination) for their plan documents. The terms “master” and “prototype” and “volume submitter” were eliminated with the Cycle Three Restatement by Revenue Procedure 2017-41 and replaced by a single term: “pre-approved plan.” Pre-approved plan documents are now either standardized or non-standardized.

Prudent person rule

The fiduciary duty under section 404(a)(1)(B) of ERISA that requires a fiduciary to discharge his or her duties to a plan under the prevailing circumstances with the care, skill, prudence, and diligence that a prudent person — acting in a like capacity and familiar with such matters — would use in the conduct of an enterprise of like character and with like aims.

PTE 2020-02

In December 2020, the DOL issued Prohibited Transaction Exemption (PTE) 2020-02 under ERISA and the Internal Revenue Code for financial professionals who provide fiduciary investment advice under ERISA Sec. 3(21). Non-discretionary Advising Fiduciaries may rely on this PTE to receive compensation that would otherwise be prohibited, including commissions, so long as the PTE conditions are satisfied, and Advising Fiduciaries render advice that is in their plan’s or IRA customer’s best interests. The PTE and the fiduciary advice rules apply to IRAs and IRA rollovers, particularly to recommendations to roll assets out of ERISA-protected plans into an IRA. One of the conditions under the PTE, effective July 1, 2022, requires Advising Fiduciaries to document and disclose in writing the specific reasons that a rollover recommendation is in the retirement investor’s best interest.

QACA

Acronym for qualified automatic contribution arrangement, a type of automatic enrollment resulting from PPA with special safe harbor provisions that exempt a 401(k) plan from annual actual deferral percentage (ADP) and actual contribution percentage (ACP) nondiscrimination testing requirements. A QACA arrangement under PPA regulations:

- Does not automatically enroll current employees who:
  - Were eligible to participate in the plan before the automatic enrollment arrangement became qualified.
  - Had deferral elections (or elections not to defer) in place when the automatic enrollment arrangement became qualified.
- Requires that employees who are eligible to participate in the qualified arrangement receive written notice of their legal rights and obligations within a reasonable time (generally between 30 and 90 days) prior to the start of the plan year.
- Provides that employer contributions become 100% vested after an employee has completed no more than two years of service.

- Requires that the plan sponsor make either matching contributions (100% of the first 1% of compensation deferred, plus 50% of the next 5% deferred) or nonelective contributions (at least 3% of compensation to all eligible non-highly compensated employees, whether they make deferrals or not).
- Provides for an automatic contribution percentage of at least a minimum specified percentage that typically ranges from 3% to 6% (depending on how long contributions have been made for the employee), but not more than 10% in the first year (and not more than 15% in any subsequent year). This provision offers guidelines for the step-up (automatic escalation) feature, which increases the automatic deferral by 1% per year. (Also see **automatic enrollment** definition.)

QDIA

Acronym for qualified default investment alternative, which provides relief from fiduciary liability with respect to the performance of the default investment chosen by the plan fiduciary when participants fail to make an investment election. The DOL has approved these four types of investments as QDIAs:

- A product with a mix of investments that takes into account the individual's age or retirement date (e.g., a lifecycle or target-retirement-date fund)
- An investment service that allocates contributions among existing plan options to provide an asset mix that takes into account the individual's age or retirement date (e.g., a professionally managed account)
- A product with a mix of investments that takes into account the characteristics of the group of employees as a whole, rather than each individual (e.g., a balanced fund)
- A capital preservation product for only the first 120 days of participation (e.g., a stable value fund)

QDRO

Acronym for qualified domestic relations order, which is a judgment, decree or order that creates or recognizes an alternate payee's (such as a child or former spouse) right to receive all or a portion of a participant's retirement plan benefits. Fees may be associated with a distribution resulting from a QDRO.

QLAC

Acronym for qualified longevity annuity contract, a deferred annuity funded with an investment from a qualified retirement plan or IRA. QLACs may give savers some peace of mind by providing income later in life. They are not included in calculating RMDs until they begin to pay out (no later than age 85). The annuity contract is a guarantee of monthly payments until death, and it is shielded from stock market downturns. As long as the annuity complies with IRS requirements, it is exempt from the required minimum distribution (RMD) rules until payouts begin after the specified annuity starting date. SECURE 2.0 raised the cap on how much money a participant can use from their retirement account to purchase a QLAC. It used to be either 25% of the account's value or $125,000, whichever was greater. The new figure of $200,000 is also indexed to inflation, whereas the previous $125,000 maximum was not.

QMAC

Acronym for qualified matching contribution, which employers can make to 401(k) plans to correct failed ACP nondiscrimination tests.

QNEC

Acronym for qualified nonelective contribution, which employers can make to 401(k) plans to correct failed ADP/ACP nondiscrimination tests.

Qualified plan

A retirement plan that meets the requirements of the IRC to qualify for tax-favored treatment.

Qualified separate lines of business (QSLOB)

A QSLOB is a portion of a controlled group that is treated separately for purposes of minimum participation standards. The portion of the plan being tested that benefits the employees of each QSLOB is treated as a separate plan maintained by that QSLOB.

Re-enrollment

A process that allows retirement plans to modify participants' existing (and, in many cases, unsuitable) 401(k) investment choices into a qualified default investment alternative (QDIA). Typically, the QDIA is a professionally managed target-date fund (TDF). Participants receive a notification that their existing assets, as well as future contributions, will be directed to the QDIA on a specified date, unless they choose other funds in the plan's lineup, or reaffirm a previous choice. The intended purpose is to help ensure that participants' plan investment portfolios are age-appropriate and diversified; it may also help reduce fiduciary liability. Also see **QDIA** and **Target-date fund**.

Regulation Best Interest (Reg. BI)

In June of 2019, the Securities and Exchange Commission (SEC) finalized new standards of conduct for broker-dealers and investment advisers. The centerpiece of the reform package is Regulation Best Interest (or Reg BI).

The other three parts of the package are Form CRS, a relationship summary which is meant to help investors understand the differences between brokers and advisers; a reaffirmation of the fiduciary duty of conduct for investment advisers; and an SEC interpretation of language that allows brokers to avoid registering as advisers — and being fiduciaries — if the advice they provide is "solely incidental" to their work and includes no special compensation. In a nutshell, Reg BI imposes an enhanced standard of conduct on broker-dealers when they provide recommendations to retail customers regarding a securities transaction or an investment strategy involving securities. Under Reg BI, a broker-dealer must act in the retail customer's best interest and cannot place its own interests ahead of the customer's interests. The final rule makes clear that this new standard of conduct applies to account recommendations, including a recommendation to roll over assets from a workplace retirement plan account to an IRA. To meet the new standard, broker-dealers must meet four obligations (as detailed in the rules): disclosure, care, conflict of interest and compliance. Compliance with Reg BI was required as of June 30, 2020. (See also **DOL fiduciary rule**.)

Registered representative

A person who is employed by a brokerage company registered with the Securities and Exchange Commission (SEC). A registered representative must register with the Financial Industry Regulatory Authority (FINRA), pass a qualifying examination, and be licensed by a state securities regulator. They can act as an account executive for clients trading stocks, bonds, mutual funds, and other investment products as determined by the brokerage company.

Required minimum distribution (RMD)

A required minimum distribution (RMD) is the amount that traditional, SEP or SIMPLE IRA owners and qualified plan participants must begin distributing from their retirement accounts by April 1 following the year they reach age 73 (earlier ages apply for those born before 1951 — see the **SECURE Act** definition). An RMD must then be distributed each subsequent year based on the current RMD distribution calculation amounts.

Restatement

The IRS has established a six-year restatement cycle for keeping pre-approved plan documents up to date with new laws and regulations. Every six years, pre-approved plan documents must be rewritten to incorporate law and rule changes that occurred prior to the start of the cycle. This process incorporates previously made discretionary and interim amendments into the plan document. When the IRS announces a new cycle, document vendors typically have two years to draft new plan documents and submit them to the IRS for approval. The IRS has approximately two years to review and approve the submitted documents. After document providers receive an approval (opinion) letter from the IRS, plan sponsors generally have two years to restate their plans on to the new document. The latest six-year cycle, referred to as "Cycle 3" required plan sponsors to complete the restatement by July 31, 2022.

Revenue sharing

An agreement between a mutual fund company and a broker-dealer whereby payment is made to the brokerage firm from the mutual fund company's investment adviser's revenues or profits. These payments are in addition to any sales charges, 12b-1 fees, redemption fees and deferred sales charges and do not come from the assets of the fund.

RIA

Acronym for registered investment advisor, a person or group that makes investment recommendations or conducts securities analysis in return for a fee and who has sufficient assets to be registered with the SEC, as determined by the brokerage company. RIAs have a fiduciary duty to their clients under the Investment Advisers Act of 1940.

Risk-adjusted returns

A measure of how much an investment returned in relation to how much risk it took on.

Risk parity

A method of portfolio construction and asset allocation in which each holding is designed to provide an equal contribution to the overall portfolio risk.

Robo-advisor

Robo-advisors (robo-advisers) are digital platforms that provide automated, algorithm-driven financial planning services with little to no human supervision. A typical robo-advisor collects information from clients about their financial situation and future goals through an online survey, and then uses the data to offer advice and/or automatically invest client assets.

Rollover

A qualifying distribution from a tax-favored retirement arrangement — a 401(k) plan, 403(b) arrangement, SEP plan, SIMPLE IRA, governmental 457(b) plan or IRA — that is contributed to another qualified arrangement. There are two types of rollovers from a qualified plan: direct and indirect.

- With a direct rollover, the distribution is paid directly to the trustee or custodian of the receiving arrangement.
- With an indirect rollover, an individual takes a cash distribution from a qualified plan (less 20% withholding for non-IRAs) and contributes it (rolls it over) within 60 days of receiving the arrangement.
- A direct movement of assets between IRAs is referred to as a transfer, not a direct rollover, because there is no taxable or reportable distribution from the IRA.

Roth 401(k) contributions

Also see **Designated Roth** under **415 limit – Common types of contributions** definition. An employer-sponsored investment savings account that is funded with after-tax dollars up to the plan's contribution limit. The Roth after-tax contributions will be distributed tax free and the investment earnings in the account will be distributed tax free if the distribution is qualified (i.e., five years have elapsed since January 1 of the year that the participant first made a Roth contribution under the plan, and the participant is age 59½ or older, disabled or deceased). The traditional 401(k) plan, on the other hand, is funded with pretax money, which results in a tax on future withdrawals.

Roth contributions under the SECURE 2.0 Act

Several provisions in SECURE 2.0 allow for additional Roth contributions to plans. First, employers with defined contribution plans may allow participants to elect to receive matching and profit-sharing contributions as Roth contributions. Second, employers may allow SEP and SIMPLE plan participants to take employers contributions as Roth contributions. And third, SIMPLE plan deferrals may be made as Roth contributions. These provisions were effective upon SECURE 2.0's enactment, but because of implementation concerns, most employers are waiting for definitive IRS guidance before permitting any of these new elections in their plans.

Safe harbor 401(k) plan

A plan that provides many of the features and flexibility of a traditional 401(k) without the administrative concerns of ADP/ACP nondiscrimination testing. However, employers must match 100% of employee elective deferrals up to 3% of the employee's compensation, plus 50% of employee elective deferrals on the next 2% of the employee's compensation. Alternatively, the employer could make an "enhanced match" (which is at least as generous as the basic match) or make a nonelective contribution on behalf of each eligible employee equal to 3% of such eligible employee's compensation. All safe harbor 401(k) contributions are 100% vested immediately.

Salary ratio allocation

A type of allocation possible within a profit-sharing plan, which allocates contributions as a flat percentage of compensation among all eligible employees. (Also see **profit-sharing plan** definition.)

Salary reduction agreement

A formal agreement between an employer and employee under which the employee agrees to take a reduction in salary or to forgo a salary increase. In return, the employer agrees to deposit the portion deferred from the employee's salary into a benefit plan, such as a 403(b), 401(k), thrift, or cafeteria plan. The agreement may state a specific dollar amount of salary reduction or a percentage of compensation reduction.

Same desk rule

A participant in a seller's retirement plan may not receive a distribution of his or her account balance if the participant becomes an employee of the buyer "at the same desk" because a "separation from service" had not occurred.

Saver's Match

SECURE 2.0 is replacing the current nonrefundable Saver's Credit with a refundable Saver's Match in 2027. For low- to mid-income individuals, this credit is up to 50% of the contribution that a saver makes to an IRA or other eligible retirement plan, but is capped at $1,000. The federal government will deposit this match into the individual's IRA or other retirement plan.

SECURE Act of 2019

Acronym for the Setting Every Community Up for Retirement Enhancement Act.

Signed into law on Dec. 20, 2019, the act included numerous retirement savings provisions, which were intended to encourage employers to offer retirement plans and enhance the savings opportunities for plan participants and IRA owners. Among other things, the Act created Pooled Employer Plans (PEPs), expanded tax credits for small businesses, repealed the maximum age for traditional IRA contributions, mandated 401(k) plan eligibility for certain long-term, part-time workers, allowed plan or IRA withdrawals (subject to limits) for birth or adoption of a child without the 10% early withdrawal penalty, required defined contribution (DC) plans to include an annual lifetime income stream estimate on participant benefit statements, increased the age at which required minimum distributions (RMDs) must begin, expanded Section 529 college savings plans, modified RMD rules for post-death distributions from DC plans and IRAs to beneficiaries and included fiduciary protection for selection of an insurer for offering guaranteed income contracts under a retirement plan. Many (but not all) provisions of the legislation required implementation as early as the 2020 plan year or taxable year.

SECURE 2.0 Act of 2022

Refers to one of the most significant pieces of retirement plan legislation since ERISA. This bill was enacted on December 29, 2022. These are some of the nearly 100 items in the bill including:

- Further expanding eligibility for part-time employees from three years to two years with 500 hours of service
- Allowing small financial incentives to employees for contributing to a 401(k) plan
- Treating student loan payments as deferrals for purposes of matching contributions
- Increasing catch-up contribution limits for certain age participants
- Requiring certain catch-up contributions to be designated as Roth contributions
- Raising the required minimum distribution (RMD) age to age 73 (for those born after 1950)
- Increasing the dollar amount for involuntary cash-outs to $7,000

Securities lending

Securities lending is the act of loaning a stock, derivative or other security to an investor or firm. Securities lending requires the borrower to put up collateral, whether cash, security, or a letter of credit. When a security is loaned, the title and the ownership are also transferred to the borrower.

Self-directed brokerage fees

Transaction and annual fees related to balances in self-directed brokerage accounts.

SEP plan

Simplified Employee Pension (SEP) plan, a retirement program that permits an employer to make tax-deductible contributions to IRAs established by eligible employees. SEPs can be sponsored by employers of all sizes. This plan is more popular among small employers because it has substantially lower administrative costs as compared to a profit sharing plan.

Separate account

Accounts established by life insurance companies where the assets held are segregated from the insurance company's general account assets and held for the benefit of investors in the separate account. These accounts are used for retirement plan investment options, including group annuities and stable value products.

Share classes

Different types of shares issued by a single fund, often referred to as Class A shares, Class C shares and so on. While each class invests in the same "pool" (or investment portfolio) of securities and has the same investment objectives and policies, share classes offer different shareholder services and/or distribution arrangements, resulting in differing fees, expenses, and performance results.

- **Class A shares** typically impose a front-end sales load and tend to have a lower 12b-1 fee and lower annual expenses than other mutual fund share classes. Some mutual funds reduce the front-end load as the size of an investment increases.
- **Class C shares** generally have a level load and might include a 12(b)-1 fee, other annual expenses and either a front- or back-end sales load.
- **Class R shares** are typically provided exclusively to retirement plans and charges can vary based on the plan's requirements and recordkeeping preferences.
- **Class R5 shares** are often called institutional shares because they are generally intended for financial institutions purchasing shares for their own or their clients' accounts. Class R5 shares have no front-end sales charge and cannot be purchased by the general public.
- **Class R6 shares** are generally available only to Qualified Plan investors where plan level or omnibus accounts are held on the books of the fund.
- **Class Y shares** are a class of mutual fund shares that often have a high minimum investment, such as $500,000 per lot, and the added benefit of waived or limited load charges and fees. Due to the high minimum investment required, Y shares are often accessible only to large institutional investors.

Sharpe ratio

A risk-adjusted measure of performance calculated using standard deviation and excess return to determine reward per unit of risk.

SIMPLE IRA

Savings Incentive Match Plan for Employees of Small Employers (SIMPLE) IRA plan, a retirement program that permits eligible employees to make elective deferral contributions to their IRAs and requires the sponsoring employer to make matching or nonelective contributions. Generally, only employers with 100 or fewer employees, each with at least $5,000 of compensation in the prior calendar year, are eligible to establish SIMPLE IRA plans. Plan contributions must be deposited into SIMPLE IRAs established by each eligible employee.

Smart beta

Smart beta defines a set of investment strategies that emphasize the use of rules-based index methodologies that systematically rebalance over traditional market capitalization- based indexes. Smart beta emphasizes capturing investment factors or market inefficiencies in an objective, transparent way.

Soft dollars

A means of paying brokerage firms for their services through commission revenue instead of through normal direct payments (hard-dollar fees).

Solo 401(k)

A plan designed for businesses with no employees (that would be eligible to participate in the plan) other than the owners and their spouses. Contributions are established by the plan document (generally salary deferrals and profit sharing contributions) and are generally 100% vested immediately. Also known as Individual(k) plans and self-employed 401(k) plans, these plans follow the 401(k) plan contribution limits and distribution rules, including plan loans.

Stable value fund

An investment designed to provide capital preservation and to offer, in most markets, higher returns than a money market fund. While offered in many forms, a pooled stable value fund typically consists of bonds or bond collective trusts, wrapped by benefit responsive contracts issued by banks or insurance companies to provide capital preservation. Most stable value funds credit a specific rate to plan participants for a set period of time, such as a quarter or year.

Stable value put

Requires plans invested in a pooled stable value fund to tender an irrevocable notice in order to redeem their plan's entire balance in the fund. Most pooled stable value funds require a 12-month notice; some require a 24-month notice. Participant withdrawals continue normally during this so-called "put period". Some pooled stable value funds require this notice under all conditions; others require it only when the market value of the stable value fund is below its book or contract value.

Standard deviation

A statistical measure of the historical volatility of a mutual fund or portfolio. Measures a fund's range of total returns and identifies the spread of a fund's short-term fluctuations.

Start-up credits

SECURE 2.0 expanded the start-up credit for small employers. Now, employers with 50 or fewer eligible employees who start a workplace retirement plan may claim a 100% credit for their plan start-up costs. Plans include 401(k), SEP, and SIMPLE plans. (The existing credit of 50% of start-up costs remains the same for employers with 51-100 employees.) This credit is available for the first three years that the plan is in place.

An additional credit of up to $1,000 is available for employer contributions that are made to employees making $100,000 or less. The credit is 100% of eligible contributions for the first two years; 75% in year three; 50% in the fourth year; and 25% in the fifth year. This combination of credits may allow employers to start a new plan with virtually no out-of-pocket expenses for the first several years.

Starter 401(k) plan

For employers with no existing retirement plan, starting in 2024 SECURE 2.0 allows them to establish a deferral-only 401(k) (or 403(b)) plan. The deferral limits are similar to the IRA limits, and employees are automatically enrolled at 3 to 15% of compensation unless they opt out of participation or choose a different deferral rate.

Strategic allocation

Strategic allocation is a portfolio strategy that involves setting target allocations for various asset classes, and periodically rebalancing the portfolio back to the original allocations when they deviate significantly from the initial settings due to differing returns from various assets.

Student debt relief

An increasing number of companies are giving employees money and other assistance to help them pay off their student loan debt and a small segment of companies within that group have begun tying the benefit to already-existing retirement plans. Many workers prioritize paying off their student loans over saving for retirement, and these programs aim to help them to do both.

Among other provisions, the SECURE 2.0 Act allows plans to treat student loan debt payments as elective deferrals for purposes of matching contributions in 401(k) plans.

The CARES Act temporarily extended IRC Section 127 which allowed for employer-provided tuition reimbursement up to $5,250/year to apply to student loan repayments for employees, with no tax implications. This provision has since been extended through December 31, 2025. The CARES Act also provided automatic suspension of principal and interest payments on federally held student loans through September 30, 2020. This was ultimately extended through August 31, 2022.

Also see **CARES Act**.

Subaccount transfer fee

An expense charged against the fund that, in certain situations, is used to offset some of the administrative expenses of a third-party administrator.

Sub-advised

Arrangement in which pooled accounts are managed with objectives similar to a particular mutual fund or managed portfolio, but not invested in the actual fund itself.

Summary plan description (SPD)

A document containing a comprehensive description of a retirement plan, including the terms and conditions of participation. ERISA requires an SPD to be written so that the average plan participant can understand it and to be distributed to each plan participant within 90 days of becoming a participant and to each beneficiary receiving benefits within 90 days of first receiving benefits.

Sunset provisions

Provisions of tax law that are to "sunset," or be automatically repealed, typically within 10 years of becoming effective. For example, many of the provisions in EGTRRA related to retirement plans and IRAs were originally supposed to sunset, but the PPA made them permanent. Among the provisions affected were salary deferral limits, contribution limits and catch-up contributions.

Surrender fee

A penalty charged an investor for withdrawing funds from an insurance or annuity contract early or canceling the contract. Also referred to as a surrender charge.

Synthetic GIC contract

A contract between a bank or insurance company and a corporate or public defined contribution plan under which the bank or insurance company guarantees a crediting rate no less than zero for investment and redemption activity by plan participants investing in their plan's stable value option. Under a synthetic GIC contract, the contract's value is based on assets such as bond portfolios, collective investment trust units, or separate account investments, rather than the general account assets of an insurance company.

Tactical allocation

Tactical allocation is a dynamic investment strategy that actively adjusts a portfolio's asset allocation. The goal of a tactical allocation strategy is to improve the risk-adjusted returns of passive management investing.

Target benefit plan

A type of money purchase plan in which an employer establishes a "target benefit" for employees based on a formula in the plan document, but each employee's actual benefit is based on the amount in his individual account.

Target-date fund

A mutual fund that automatically resets the portfolio's asset mix of stocks, bonds, and cash equivalents according to a time horizon that is appropriate for a particular investor.

Termination fee

Costs associated with terminating a relationship with a service provider, permanent termination of a plan or termination of specific plan services. Also called "surrender" or "transfer" charges.

Third-party administrator (TPA)

An organization that administers retirement plans for an employer. This organization works with the employer as well as the insurer to communicate information between the two, as well as processing claims and determining eligibility.

Top-heavy test

A nondiscrimination test that generally requires a tax-qualified retirement plan sponsor to make minimum contributions when account balances of key employees are disproportionately greater (60% or more) than account balances of non-key employees (i.e., when the plan becomes top-heavy).

Triggering event

Tax-qualified retirement plans are designed to restrict plan participants from using their savings before retirement. Under the general rules, participants can't access the employer matching and profit sharing contributions in their account until they have experienced a distribution triggering event, such as "termination of employment after attaining normal retirement age" and "plan termination." Plan documents will specify other triggering events applicable to the plan.

Certain contributions, including salary deferrals made by plan participants, are subject to more restrictive distribution requirements. These may be distributed only upon

- Termination of employment
- Death
- Disability
- Attainment of age 59½
- Hardship
- Plan termination

Trustee: Individual/employer

One or more individuals who are appointed by the employer to act as trustee under its retirement plan.

Trustee: Institutional

The bank or trust company designated to serve as the plan trustee. Typically, this type of trustee serves as the custodian of the plan's assets.

Unbundled services

Plan sponsors provide services through a combination of in-house staff and independent service providers for each critical task. It allows for maximum control and the ability to select among different service providers, including investment options. This model is more prevalent among larger plans that have adequate resources to manage such a plan. Independent consultants are often hired to help construct and manage unbundled plans.

Upside capture ratio

A statistical measure of an investment manager's overall performance in up markets that is used to evaluate how well the manager performed relative to an index during periods when that index has risen. The ratio is calculated by dividing the manager's returns by the returns of the index during the up market and multiplying that factor by 100.

Vesting schedule

The schedule that determines the portion of a participant's accrued benefit or account balance to which the participant has a nonforfeitable right after completing a specified number of years of service.

Wrap expense

A fee based on all plan assets and in addition to individual fund-related fees. The wrap expense typically pays for bundling of services related to investing plan assets and may include administrative services such as recordkeeping or the preparation of signature- ready Form 5500s.

This glossary is not intended to be legal or tax advice. Rather, it is intended only as a general summary, in nontechnical terms, of certain basic concepts applicable to 401(k) and, in some cases, certain other types of tax-qualified retirement plans. Although this material concentrates on DC plans, it is not intended to provide a comprehensive discussion of DC plans or other types of tax-qualified retirement plans.

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