Invesco

Invesco Plan*Forward* Foundations℠

The Language of Retirement Plans Glossary

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Understanding employer-sponsored, tax-qualified retirement plans is easier when you know the terminology.

12(b)-1 fee

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

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 deferral contributions a participant may make to any employer-sponsored, tax-qualified retirement plan(s). The 402(g) limit is an annual individual limit covering all deferral contributions regardless of plan(s). All elective deferral contributions to any tax-qualified retirement plan are subject to 402(g) limits, which are adjusted annually to reflect increases in the cost of living (COLA). (Also see *catch-up contributions* on page 8.)

403(b) arrangement

An annuity contract or custodial account that meets the requirements of Section 403(b) of the IRC. Only employees of certain public schools, universities and tax-exempt organizations described in section 501(c)(3) of the IRC are eligible to establish 403(b) arrangements. The Treasury Department issued final 403(b) regulations that will cause administrative changes in the way current 501(c)(3) organizations, churches, schools and hospitals do business.

404 limit — employer deductible contribution limit

The maximum annual deduction permitted by an employer for federal income tax purposes with respect to tax-qualified, retirement plan contributions (employer contributions). 404 refers to the section of the IRC that sets the limit. Separate limits apply to defined contribution plans and defined benefit plans. The defined contribution limit is an aggregate limit covering all contributions by an employer to any defined contribution plan(s). The annual defined contribution plan deduction limit is 25% of eligible compensation earned by all plan participants for that year.

404(c) regulations

Regulations that relieve a plan fiduciary 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.

415 limit — annual additions limit

The annual contribution limit to a participant account. This limit includes all contributions except rollover and loan repayment. 415 refers to the section of the IRC that sets the limit. Separate limits apply to defined contribution plans and defined benefit plans. The defined contribution limit is an aggregate limit. All annual additions to the account of a participant — under all tax-qualified 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 addition limit:

- Designated Roth contributions. Also known as Roth 401(k) contributions, these are elective deferrals currently included in gross income. Qualifying distributions made from designated Roth accounts, including the earnings on designated Roth contributions, are tax free.
- Discretionary (or profit sharing) (nonelective). A nonmandatory 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
- Forfeiture reallocation. A reallocation of assets resulting from attrition in the work place

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.

ACP test

Actual contribution percentage test. See *ADP/ACP nondiscrimination tests* on page 5.

Administration

The party responsible for managing the day-to-day activities of the plan. This is often the plan sponsor. The plan sponsor may delegate these duties to a third party.

Administration and recordkeeping expenses

Fees for administrative and recordkeeping services pertaining to plan participants. 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 test

Actual deferral percentage test. See *ADP/ACP nondiscrimination tests* on page 5.

ADP/ACP nondiscrimination tests

Nondiscrimination tests that apply to 401(k) plans. The ADP test prohibits highly compensated employees (HCE) from making disproportionately greater elective deferral contributions to a 401(k) plan than nonhighly compensated employees (NHCE). The 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* on page 23.)

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.

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.

Annuitized payments

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

Annuity and stable value/GIC surrender charges

Vendors may require that surrender charges be paid if the plan terminates its contract with a provider of annuities or stable value/ GIC (guaranteed investment contract) funds prior to completion of the contract. (Also see *GIC* on page 15.) Vendors may also require surrender charges for an individual participant transfer or termination.

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 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

Automatic deferral default percentage

The percentage of pay that is automatically deferred when an employee is enrolled in a plan through automatic enrollment. A typical automatic deferral default percentage is 3% of pay. Generally, participants can choose to defer an amount other than the default percentage.

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."

Balance inquiry expense

Fee charged for each participant inquiry about account balance.

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).

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.

Beneficiary

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

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.

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 cannot be 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.

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.

Cliff vesting

A vesting schedule in which the participant's accumulation is not vested during the initial years of service but becomes fully vested upon completing the number of years required by the plan. While traditional vesting schedules are graduated (20%, 40%, 60%, etc.), cliff vesting is not (0%, 0% and 100%).

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 fund

A tax-exempt, pooled fund, operated by a bank or trust company that commingles assets of trust accounts for which the bank provides fiduciary services.

Commission

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

Compliance testing

Testing required by the IRS to ensure that nonhighly compensated employees (NHCEs) benefit enough from the plan relative to the benefit received by the highly compensated employees (HCEs). (Also see *HCE* on page 16 and *NHCE* on page 21.)

Contract administration charge

A charge for administering the insurance/annuity contract, 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" its insurance/annuity contract prior to the end of a stated time period. The charge typically decreases over time.

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.

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.

DB(k) plan

A defined benefit plan with a salary deferral feature. Beginning in 2010, employers with two to 500 employees when the plan is established may adopt a DB(k) plan.

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 (upon request) 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.

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 employers who offer pension or welfare benefit plans for their employees. DOL also enforces fiduciary, disclosure and reporting requirements for fiduciaries of pension and welfare benefit plans.

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 qualified and retirement 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 reduction 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 advisor 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, a federal law that imposes various requirements on voluntarily established pension, health and other welfare benefit plans in private industry, and establishes standards applicable to certain service providers of such plans in order to provide protection for plan participants.

ETFs

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

Exclusive benefit rule

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

Expense ratio

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

Fidelity bond

A bond designed to protect a retirement plan's participants in the event a fiduciary or other responsible person steals or mishandles plan assets.

Fiduciary (under ERISA)

Any person or party who:

- Exercises any discretionary authority or discretionary control with respect to management of the plan or exercises any authority or control with respect to management or disposition of its assets.
- Renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of the plan, or has any authority or responsibility to do so.
- Has any discretionary authority or discretionary responsibility in the administration of the plan.

ERISA section 3(21)(A)(ii) sets out a simple two-part test for determining fiduciary status: A person or party who (1) renders investment advice with respect to any moneys or other property of the plan, or has any authority or responsibility to do so; and (2) receives a fee or other compensation, direct or indirect, for doing so.

Fiduciary insurance

Insurance that protects plan fiduciaries in the event that they are found liable for a breach of fiduciary responsibility.

Forfeiture

The portion of a participant's account balance that is relinquished (the nonvested portion) upon termination of employment.

Form 1099R
A form sent to the recipient of a plan distribution and filed with the IRS to document the distribution amount.

Form 5500
A form that all qualified retirement plans — excluding Simplified Employee Pension (SEP) plans and Savings Incentive Match Plan for Employees (SIMPLE) IRAs — 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.

GIC
Acronym for guaranteed investment contract, in which the returns are set by contract. The principal does not fluctuate due to the application of book value accounting.

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 and the IRS Restructuring and Reform Act of 1998.

Hardship or in-service distribution

A participant's withdrawal of plan contributions prior to retirement. Financial hardship may be a condition for eligibility for this type of withdrawal, which may or may not be permitted under the terms of the plan. Reasons for hardship withdrawals can include coverage of 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; or certain damage repair expenses for the employee's principal residence. These distributions are taxable as early distributions and are generally subject to a 10% penalty tax if the participant is under 59½.

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.

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.

Individually designed plan

A plan established pursuant to a document that is not a prototype document. (See also *prototype documents* on page 24.) An individually designed plan document is not preapproved by the IRS. In general, individually designed plan documents are more costly to establish and maintain than prototype documents.

Individually managed account

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

Installation fee

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

Investment advice

Recommendations or guidance about an investment product that is intended to educate an investor.

Investment management fee

See *management fee* on page 19.

Investment manager

Any 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 advisor under the Investment Advisors Act of 1940; is registered as an investment advisor 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.

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.

IRS Form 5500

See *Form 5500* on page 15.

Keogh plan

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. Also known as an H.R. 10 plan.

Key employee

An individual who:

- Is 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.
- Owns more than 5% of the company that sponsors the plan.
- Is a 1% owner of the company that sponsors the plan, with income of more than $150,000.

Life cycle fund

A diversified mutual fund 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.

Mapping

See *investment mapping* on page 18.

Master plan

A retirement plan, sponsored by a financial institution, that has already been examined and approved by the IRS.

Matching contribution

An employer contribution to a participant's employer-sponsored retirement plan. The amount of the contribution is based on the amount of the participant's elective deferral contributions. For example, the plan might specify that it will contribute 50 cents for each dollar of elective deferral contributions under its 401(k) plan. Matching contributions are subject to ACP testing.

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.

Mortality risk and administrative expense

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

MPT

Acronym for modern portfolio theory, pioneered by Harry Markowitz in 1952. MPT 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.

Negative election

See *automatic enrollment* on page 6.

New comparability allocation

A type of allocation formula for profit sharing plans that allocates disproportionately greater amounts to a specific group of employees. (Also see *profit sharing plan* on page 23.) 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 nonhighly 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.

Opinion letter

A written statement from the IRS as to the acceptability of a prototype plan document.

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. 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.

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

Permitted disparity allocation formula refers to a tax-qualified retirement plan that takes into account either benefits or contributions under Social Security in determining the amount of a participant's benefits under the plan. Social Security benefits are used to integrate defined benefit plans and defined contribution plans. In general, profit sharing integrates with Social Security by allocating to plan participants a greater percentage of their compensation in excess of the Social Security taxable wage base and a lower percentage of their compensation at or below the Social Security taxable wage base. (Also see *profit sharing plan* on page 23.)

Plan administrator

The person or firm responsible for the administration of a retirement plan, determination of eligibility for benefits and payment of benefit claims.

Plan document/IRS filing fee

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

PPA

Acronym for the Pension Protection Act of 2006, legislation that affects qualified retirement plans, plan sponsors and plan participants. It contains 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 includes 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.

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* on page 5, *new comparability allocation* on page 20, *permitted disparity (integrated) allocation formula* on page 22 and *salary ratio allocation* on page 28.) A single plan can contain both a profit sharing and an elective deferral feature.

Prototype documents

Documents that provide standard language for different types of retirement plans that offer flexible options within each plan type. Prototype plan documents are sponsored by financial institutions and adopted by employers to create the plan. There are both standard and nonstandard prototypes. Standardized prototype documents are less flexible than nonstandardized prototype documents. Employers who adopt prototype plans are not required to obtain IRS approval (letter of determination) for their plan documents; however, this is a good practice for nonstandard documents.

Prudent man 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 man — 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.

QACA

Acronym for qualified automatic contribution arrangement, a type of automatic enrollment resulting from PPA that qualifies for safe harbor and automatically complies with nondiscrimination testing. 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 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 nonhighly compensated employees, whether they make deferrals or not).
- Provides for an automatic contribution percentage of at least a minimum specified percentage that ranges from 3% to 6% (depending on how long contributions have been made for the employee), but not more than 10%. This provision offers guidelines for the step-up feature, which increases the automatic deferral by 1% per year. (Also see *automatic enrollment* on page 6.)

QDIA

Acronym for qualified default investment alternative that provides relief from fiduciary liability with respect to automatic enrollment programs when a QDIA (as defined by the DOL) is selected by the plan. 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 are associated with a distribution resulting from a QDRO.

QMAC

Acronym for qualified matching contribution, which employers can make to 401(k) plans to correct failed ACP nondiscrimination tests. Qualified matching contributions satisfy the vesting and distribution requirements.

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.

Recordkeeping fee

See *administration and recordkeeping expenses* on page 4.

Registered representative

A person who is employed by a brokerage company licensed by the Security and Exchange Commission (SEC) and who acts as an account executive for clients trading stocks, bonds, mutual funds and other investment products.

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 advisor'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. Advisors receive no additional compensation as a result of these payments.

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.

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 provides an equal contribution to the overall portfolio risk.

Rollover

A qualifying distribution from a tax-favored retirement arrangement — a 401(k) plan, 403(b) arrangement, SEP plan, SIMPLE IRA, 457 plan or IRA — that is contributed to another qualified plan. 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) and contributes it (rolls it over) within 60 days of receiving the arrangement.
- A direct transfer of assets between IRAs may also be referred to as a direct transfer of assets.

Roth 401(k) contributions

See *designated Roth contributions under 415 limit, common types of contributions* on page 3.

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, 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* on page 23.)

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.

SARSEP plan

Salary Reduction Simplified Employee Pension plan, created as a simple alternative to a 401(k) plan for companies with 25 or fewer employees. Employees eligible to participate in a SARSEP have the opportunity to make elective deferral contributions to their SEP plans. Employers may no longer establish new SARSEPs. Contributions may continue to existing SARSEPs.

Self-directed brokerage fees

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

SEP plan

Simplified Employee Pension 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 generally has substantially lower administrative costs.

Separate account

An asset account established by a life insurance company, separate from other life insurance company funds, that offers investment funding options for pension plans.

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 I shares** are often called institutional shares because they are generally intended for financial institutions purchasing shares for their own or their clients' accounts. Class I shares have no front-end sales charge and cannot be purchased by the general public.
- **Class R shares** are typically provided exclusively to retirement plans and charges can vary based on the plan's requirements and recordkeeping preferences.

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 IRA, a retirement program that permits eligible employees to make elective deferral contributions to their IRAs and the sponsoring employer to make mandatory 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.

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 other than the owners and their spouses. Contributions are established by the plan document and are generally 100% vested immediately.

Sponsor

An employer who establishes and maintains a plan.

Stable value fund

An investment vehicle comprising mostly wrapped bonds, which can be short or intermediate term with longer maturities than other choices such as money market funds. They are paired (or wrapped) with insurance contracts to guarantee a specific minimum return.

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.

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.

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 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 EGTRRA that were originally to "sunset," or be automatically repealed, in 2010. The PPA made the EGTRRA provisions related to retirement plans and IRAs permanent. Among the provisions affected were salary deferral limits, contribution limits and catch-up contributions.

Surrender fee

See *termination fee* on page 32.

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 an 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.

Top-heavy test

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

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.

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.

Before investing, investors should carefully read the prospectus and/or summary prospectus and carefully consider the investment objectives, risks, charges and expenses. For this and more complete information about the fund(s), investors should ask their advisors for a prospectus/summary prospectus or visit invesco.com/fundprospectus.

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.

Note: Not all products, materials or services available at all firms. Advisors, please contact your home office.