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Glossary of Retirement Plan Terms

401(k) Plans: Employer –sponsored defined contribution plans in the private sector.

404(a)(1)(a) and (b): The section of Title I of ERISA that establishes the duties of a plan fiduciary, which are to act solely in the interest of participants and beneficiaries. This section includes the stipulation that the fiduciary must ensure plan expenses are reasonable for services provided.

- The investment of plan assets is a fiduciary act governed by the fiduciary standards in ERISA section 404(a)(1)(a) and (b), which require plan fiduciaries to act prudently and solely in the interest of the plan's participants and beneficiaries.
- When a plan allocates investment responsibilities to participants or beneficiaries, the plan administrator must take steps to ensure that such participants and beneficiaries, on a regular and periodic basis, are made aware of their rights and responsibilities with respect to the investment of assets in their accounts and are provided sufficient information regarding the plan and the plan's investment options, including fee and expense information, to make informed decisions with regard to their individual accounts.

404(c): A section of Title I of ERISA that protects plan fiduciaries from liability for the results of decisions made by plan participants who direct the investments in their accounts. Plan Fiduciaries are still responsible for making suitable investment options available to plan participants.

408(b)(2): A section of Title I of ERISA that provides plan sponsors certain protections as long as an arrangement or contract with a service provider is reasonable, the services provided are necessary and no more than reasonable compensation is paid for services. The regulation:

- Applies to defined contribution plans and defined benefit pension plans and addresses the disclosure of the direct and indirect compensation certain service providers receive.
- Focuses on service providers and compensation arrangements that are most likely to raise questions for plan fiduciaries with respect to potential conflicts of interest that might compromise the quality of services.

Actively Managed Funds and Accounts: Investment strategies in which the manager actively constructs a portfolio of securities to generate a return that exceeds a benchmark.

Annuity Investments: Products offered by insurance companies that are widely used in retirement plans, with plan assets frequently packaged on a group annuity platform. The participant has a pooled investment account with a contract for insurance-related elements and charges, such as an annuity feature, interest and expense guarantees, and any death benefit provided during the contract term.

Basis Point (BPS): A unit that is equal to 1/100th of 1%, and is used to denote the change in a financial instrument. The basis point is commonly used for calculating changes in interest rates, equity indexes and the yield of a fixed-income security. The relationship between percentage changes and basis points can be summarized as follows: 1% change = 100 basis points, and 0.01% = 1 basis point.

Benchmarking: Analysis providing defined contribution plan peer group comparisons of cost and service levels; used by plan sponsors to help assess whether fees are reasonable for services received.

Bundled and Unbundled Service Plans: In bundled service arrangements, the sponsor hires one company to provide a full range of retirement plan services directly or through subcontractors. In unbundled arrangements, the sponsor uses a combination of service providers directly.

Collective Trust Fund (CTF): A tax-exempt, pooled investment vehicle administered by a bank or trust company that available to defined benefit and defined contribution plans.

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Compliance Testing: Plan sponsors must test traditional 401(k) plans each year to ensure that the amount of contributions made by and for rank-and-file employees (nonhighly compensated employees) are proportional to contributions made for owners and managers (highly compensated employees). As the NHCEs save more for retirement, the rules allow HCEs to defer more. The following tests may apply to your retirement plan.

ADP/ACP Nondiscrimination Test

The nondiscrimination test is broken up into two parts; the Actual Deferral Percentage Test (ADP) (deferrals) and the Actual Contribution Percentage Test (ACP) (employer match).

The ADP test – The employees under the plan are separated into 2 groups; Highly Compensated (HCE) and Non-Highly Compensated (NHCE). The average deferral percentage for the NHCE group is the calculated and the average deferral percentage for the HCE group is also calculated. The average deferral percentage for the HCE group may not exceed the greater of: 1.25 times the average deferral percentage of the NHCE group, or the lesser of 2 times the average deferral percentage of the NHCE group; or the average deferral percentage of the NHCE group plus 2%.

Any amount that exceeds the limits of the above tests must be distributed to the highly compensated employees and becomes taxable income for the testing year. Also included in the distribution will be any earnings on the excess amount. The highly compensated employee that receives a refund will also receive a 1099R for the testing year.

The ACP test – This test is performed exactly like the ADP test, with one difference. This test is performed on the matching contribution. In the event of a test failure, all nonvested employer match money will be put into the plan's forfeiture account for later use. All vested employer match money will be distributed to the participant as taxable income for the testing year.

There is an alternative to receiving a refund in the event of an ADP test failure. If the plan is using the current year testing method, the employer may contribute a Qualified Non-Elective Contribution (QNEC) to all of the NHCEs employed on the last day of the plan year. The purpose of this contribution is to boost the average deferral percentage of the NHCE group to allow the plan to pass the test.

As there is an alternative to a refund for the ADP test, there is also another correction method for an ACP test failure. If the plan is using the current year testing method, the employer may contribute a Qualified Matching Contribution (QMAC) to all of the NHCEs employed on the last day of the plan year.

Please note: If your plan has a safe harbor feature, the ADP and ACP nondiscrimination tests do not apply to your plan.

Refunds due to a failure of the ADP/ACP nondiscrimination test must be distributed within 2 ½ months after the plan year end. If your plan year end is December 31st, then refunds must be distributed prior to March 15th. Refunds due to failure of the 402(g) limit or 415 limit tests must be distributed by April 15th of the year following the test failure. If refunds are not distributed by the given deadlines, the IRS will impose a 10% excise tax on the amount of the refund. A Form 5330 will have to be filed with the IRS in order to report the refund and a check for the 10% excise tax must accompany the filing. If this situation arises, Dyatech will prepare the form for your plan. If the refund is distributed by the appropriate deadline, the income is reported as taxable income for the year it was contributed to the plan. The participant will receive a 1099-R the following January, and will usually need to amend their personal tax return. We advise that any participant that receives a refund consult a tax specialist, such as a CPA, to help handle this additional taxable income.

The actual excess will have to be adjusted for any gains or losses prior to distribution. The amount of the check will reflect the actual excess plus or minus any gains or losses on the amount.

Top Heavy Test - A plan becomes top heavy when 60% or more of the plan's account balance belongs to the key employees. The top heavy test is generally performed on the last day of the plan year. If the plan's year end is 12/31, the test will be run as of that date to determine if the plan is top heavy for the next plan year. If the test shows that the plan is top heavy, the employer must make a maximum 3% contribution on behalf of each non-key employee that is employed on the last day of the plan year. This contribution is called the "top heavy minimum." If the plan currently allows for employer matching or employer profit sharing contributions, those contributions can and will count toward the top heavy minimum.

Minimum Coverage Test - The minimum coverage rules require employers to make their retirement plan available to a certain percentage of employees. There are some plans that automatically meet the coverage requirements. Other plans must pass either the ratio percentage test, or the average benefits test.
There are 4 types of plans that automatically pass the minimum coverage test; A plan that has no non-highly compensated employees (ex., an owner only 401(k)), A plan that benefits non-highly compensated employees at any time during the plan year, A plan that only benefits collective bargaining employees (union plan), and A plan involved in an asset or stock acquisition, merger or other transaction involving a change in the employer. The coverage requirements will be waived from the period of acquisition to the last day of the plan year following the plan year in which the acquisition occurs.

The ratio percentage test is one test used to satisfy minimum coverage requirements. In order to pass this test, the percentage of non-highly compensated employees benefiting under the plan must be at least 70 percent of the percentage of highly compensated employees under the plan. If the plan passes this test, there is no need to perform or pass the average benefits test.

The average benefits test consists of two parts, the nondiscriminatory classification test and the average benefit percentage test. The nondiscriminatory classification test requires that the 401(k) plan benefit a class of employees that is both reasonable and nondiscriminatory. The average benefit percentage test requires that the average benefit percentage of the 401(k) plan for the year must be at least 70 percent. The plan must pass both parts of the average benefits test to meet the minimum coverage requirements. That is, if the plan fails to first pass the ratio percentage test (above).

415 Annual Additions Test - Each year, your plan will be tested to see if anyone went over the "415 Limit" set by law. To determine the annual additions for each participant you must add; Pre-tax and Roth salary deferrals, Employer matching contributions, Employer profit sharing contributions, Employee voluntary after-tax contributions, Forfeiture allocations for the plan year in question, Employer safe harbor contributions.

Catch-up contributions for individuals over 50 will not be included as annual additions. Amounts such as rollovers or loan repayments are also not included as annual additions. The total amount of annual additions must not exceed the 415 limit for the testing year. If a participant exceeds his/her annual additions limit, a refund will need to be issued to the participant for the amount of the overage plus any earnings.

402(g) Limit Test - The 402(g) limit is an annual cap on the amount of elective deferrals that can be made by any individual for a given year. If a participant exceeds this limit, a refund will be issued to the participant in the amount of the excess plus any applicable earnings.

414(s) Compensation Ratio Test - A plan is allowed to exclude certain compensation from its definition of plan compensation and still be deemed reasonable compensation, i.e., bonuses, overtime, commissions. However, with these exclusions the plan's definition of compensation must pass non-discrimination testing. In order to ensure that the plan's definition of compensation is non-discriminatory, a 414(s) Compensation Ratio Test must be performed. To do this, we will need the plan compensation, and also the total of the compensation exclusions. Once the test is performed, the average of the Highly Compensated Employee compensation cannot be over a "de minimus" amount of the Non-Highly Compensated Employee's compensation average. "De Minimus" has been further defined to be no more than 3%.

Conflict of Interest: Relationships with other parties or interests that impact a provider's ability to act in the best interest of the plan and its participants.

Custody/Trustee Expenses: Charges for safekeeping of defined contribution plan assets.

Defined Contribution Plan: A retirement plan in which a certain amount of percentage of money is set aside each year by a company for the benefit of the employee. There are restrictions as to when and how you can withdraw these funds without penalties.

Department of Labor (DOL): Federal department responsible for overseeing private pension plans. A unit of the DOL, the Employee Benefit Security Agency (EBSA) is responsible for ERISA enforcement.

Direct and Indirect Compensation:

Direct: Compensation paid directly by a plan sponsor to plan service providers. More easily identified and reported than indirect compensation, direct compensation includes: a. Fees paid by sponsors to providers using plan assets, including amounts deducted from participant accounts. b. Payments made by sponsors to providers that are reimbursed from plan assets.

Indirect: Compensation received by service providers from any source other than the plan sponsor, an affiliate or a subcontractor. Since providers use a wide variety of service models, fee structures and products, there are many different types of indirect compensation. More complex than direct compensation, indirect compensation can be difficult to identify and report.

Distribution (12b-1) Fees: Sales and marketing charges. In defined contribution plans, these fees are paid by funds to financial advisors for retirement plan services, including assistance in selecting and monitoring funds, communications, investor education, and related services.

Due Diligence: An investigation or audit of a potential investment. Due diligence serves to confirm all material facts in regards to a investment selection. Generally, due diligence refers to the care a reasonable person should take before entering into an agreement or a transaction with another party.

Employee Retirement Income Security Act of 1974 (ERISA): A federal law that sets minimum standards for most voluntarily established pension and health plans in the private sector to provide protection for plan participants. Title I of ERISA covers fiduciary standards applicable to employee benefit plans. ERISA is enforced by the U.S. Department of Labor.

Fee Policy Statement: A written policy that provides guidelines and objectives for plan expense management and a framework for decision-making and documenting cost control processes.

Fee Types:

Fee Type	Charges Based On	Examples
Asset-based	Amount of plan assets, typically expressed as percentages or basis points	Investment expense, annuity fee
Per-person	Number of participants in plan or number of eligible employees	Education and enrollment fees
Transaction-based	Execution of particular plan service or transaction	Loan origination fee, distribution expense
Flat rate	Fixed charge that does not vary	Annual audit fee

Fiduciary: According to the DOL, “using discretion in administering and managing a plan or controlling the plan’s assets makes that person a fiduciary to the extent of that discretion or control. Thus, fiduciary status can be based on the functions performed for the plan, not just a person’s title.” Plan fiduciaries typically include the trustee, investment advisors, individuals exercising discretion in the administration of the plan, plan administrative committee members, and those who select committee officials. The key to determining whether an individual or an entity is a fiduciary is whether they are exercising discretion or control over the plan.

Finders’ Fees: Payment to a financial advisor for directing a fund to a plan sponsor; paid out of a mutual fund company resources rather than fund assets.

Form 5500 Schedule C: Annual report filed for employee benefit plans; revised in 2007 to include new reporting requirements for service provider fees and other compensation (on Schedule C of the 2009 Form 5500).

Group Annuity Contracts: See Annuity Investments.

Insurance-Related Charges: Fees for sales expenses, mortality risk charges, and the cost of issuing and administering the annuity contract.

Investment Consulting Fees: Expenses for consulting and plan advice on Investment Policy Statement drafting and investment manager due diligence, selection, monitoring, and fee negotiation.

Investment Management Expenses: Fees charged by the fund's investment advisor for managing securities in the portfolio. Expenses vary depending upon investment strategy. These charges represent the vast majority of plan expenses, often exceeding 90% of total costs.

Investment Policy Statement (IPS): A written policy used as a guideline for investment decisions by plan fiduciaries. An IPS may include definitions of acceptable asset classes, due diligence research, and fee guidelines for investment products.

Lipper Money Market Funds Index: An unmanaged index considered representative of money market funds tracked by Lipper.

Lipper Large-Cap Growth Funds Index: An unmanaged index considered representative of large-cap growth funds tracked by Lipper.

Lipper Mid-Cap Growth Funds Index: An unmanaged index considered representative of mid-cap growth funds tracked by Lipper.

Lipper Small-Cap Growth Funds Index: An unmanaged index considered representative of small-cap growth funds tracked by Lipper.

Lipper International Funds Index: An unmanaged index considered representative of international funds tracked by Lipper.

Mutual Fund Share Classes: Mutual fund companies may provide a multi-class share structure to pay for the advisory and shareholder services offered to different types of investors in the same portfolio. For defined contribution plans, the most common are R, A, and I shares, each tailored to the requirements of different plan sizes. Because R, and A share classes typically carry distribution (12b-1) and sub-transfer agency fees to fund the servicing needs of small and mid-size plans, operating expenses tend to be higher than for the I-share class funds used in large and mega plans.

Non-Settlor Functions: Plan expenses that may be paid from plan assets. Examples include costs for drafts of plan amendments for changes required by law, benefit calculations, nondiscrimination, and testing.

Open Architecture: This structure refers to trading and recordkeeping operations that make a wide range of investment vehicles available to a retirement plan.

Passively Managed Funds and Accounts: Investment strategies with the objective of matching the return of an index. Also known as index funds.

Plan Participant Account Statement: ERISA-required disclosure of account balances due to a plan participant.

Plan Sponsor: Designated party, usually a company or employer that sets up a healthcare or retirement plan such as a 401(k) for the benefit of the organization's employees. The responsibilities of the plan sponsor include determining membership parameters, investment choices and, in some cases, providing contribution payments in the form of cash and/or stock.

Proprietary Systems: Platform structures making only one investment provider available to a plan sponsor.

Recordkeeping Fees: Fees associated with plan operations and administration, including transaction processing, reporting, transfers, valuations, inquiries, statement preparation, and distributions.

Revenue Sharing: Revenue sharing occurs when investment providers pay other plan service providers for product distribution or recordkeeping/administrative services, or "share" or rebate a portion of fees to these other providers.

Safe Harbor: A legal provision to reduce or eliminate liability as long as good faith is demonstrated. Under SEC rules, safe-harbor provisions protect management from liability for making financial projections and forecasts made in good faith.

Separately Managed Accounts (SMAs): Institutionally managed portfolios of securities for investments that are owned directly by the account holder.

Service Providers: Vendors providing custody/trustee, investment advisory, investment management, recordkeeping, brokerage, consulting, banking, third-party administration, fiduciary, accounting, actuarial, audit, legal, and valuation services to a plan.

Settlor Functions: Costs associated with the establishment of ERISA plans. Generally, settler expenses must be paid by the plan sponsor and not from plan assets or revenue. Examples include costs for conducting a plan design study, amending the plan for non-legally required reasons, establishing a plan, and correction of compliance and fiduciary errors.

Shareholder Servicing: Fees typically paid to fund's transfer agent for recordkeeping, administration, and other account services.

Stable Value Funds: A portfolio of low-risk investments guaranteed against loss by insurance companies. Also known as Guaranteed Investment Contract (GIC) Funds.

Sub-Transfer Agency Fees: These fees represent a portion of transfer agency compensation paid out for defined contribution plan recordkeeping services provided by trust companies, third-party administrators, or banks.

Summary Annual Report (SAR): ERISA required disclosure to plan participants on the financial condition of the retirement plan. The SAR is a summary of information included in the annual report (Form 5500) and must be provided to participants within nine months of the close of the plan year.

Summary Plan Description (SPD): ERISA required document explaining how the retirement plan operates. The SPD must be provided to plan participants and beneficiaries and includes information on participant eligibility, employee rights, vesting, and claims and appeal provisions.

Surrender and Transfer Charges: Fees that may be assessed if the employer terminates an annuity contract early and assets are transferred to another investment option.

Total Fund Operating Expense (Expense Ratio): Expenses for investment management, distribution (12b-1) and other functions, including services and administration. Expenses vary depending upon share class and investment strategy.

Total Revenue Credit: Revenue sharing available to offset recordkeeping, administration, and investment consulting charges.

Total Revenue Sharing Debit: A shortfall that occurs when revenue sharing does not generate enough to pay for recordkeeping, administration, and investment consulting charges; must be paid by the plan, plan sponsor or a combination of the two.

Trading Costs: Transaction costs and brokerage fees for trades, trading costs are charged against fund value and are not included in the total operating expense ratio. Costs vary depending on portfolio turnover and market liquidity.

Wrap Fees and Annuity Charges: Insurance company costs for annuity feature, interest, and expense guarantees and any death benefit provided; these fees are for features not available in non-insurance vehicles and are in addition to investment product fees and sales commissions.

Online Resources

Department of Labor (www.dol.gov)

Internal Revenue Service (www.irs.gov)

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