

# RETIREMENT CHECK-UP



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## Know Your Retirement Plan: Glossary of Terms

Through the AACPS Supplemental Retirement Program (SRP), you have access to two types of retirement plans: a 403(b) and a 457(b) tax-deferred compensation plan. To make the most of the benefits offered in the SRP, it is important to understand how the SRP fits within your investment portfolio. Understanding basic investment terminology will help you manage your account and make adjustments over time to maximize your retirement benefits. To help you make the most of your retirement benefits, review the following glossary of commonly used investment and retirement program terms.

### Often used terms

- **12(b)1 fee** – An investment fee assessed on certain mutual funds to help cover the costs associated with selling or marketing those funds. This fee may also be used to cover certain shareholder service-related expenses.
- **Annual rate of return** – The annual rate of return refers to the yearly gain or loss on an investment and is shown as a percentage.
- **Asset allocation** – Asset allocation refers to dividing your assets among different broad categories of investments such as stock funds, bond funds and capital preservation funds. Asset allocation is a strategy for reducing the risk associated with investing. Finding the right mix of assets depends on your age, your accumulated assets, your financial objectives and your risk tolerance.
- **Balanced fund** – A balanced fund is one that maintains a balanced portfolio, generally 50% bonds and 50% common stocks, although this percentage can, and does, vary. The goal is to seek a strong return while minimizing risk.
- **Basis point** – A basis point is one-hundredth of one percent, or 0.01%. For example, 10 basis points equals 0.10%. Investment expenses are often expressed in basis points.
- **Beneficiary** - The designated person who is entitled to receive benefits from a retirement plan following the death of the employee. Under the terms of the SRP, the beneficiary is your spouse unless the you designate someone else. If you do not designate a beneficiary and you do not have a spouse, payment will be made to your estate. You must make an election for the 403(b) and the 457(b) if you participate in both Plans.
- **Bond** – A bond is a certificate of debt issued by companies or governmental entities. Bonds generally pay a specific rate of interest and pay back the original investment after a specified period of time.
- **Brokerage window** – A brokerage window, or a self-directed account, allows investment in mutual funds that are not part of the SRP's core investment line-up.
- **Compounding** – Compounding is the ability of an asset to generate earnings that are then reinvested and generate their own earnings (earnings on earnings).
- **Defined Benefit Plan** – An employer sponsored plan where the retirement benefit is a specified payment amount based on a pre-determined formula which may consider factors such as the employee's earnings, length of service, and age. The employer bears the investment risk. The Employees' and Teachers' Retirement System sponsored by the State of Maryland is a defined benefit plan.
- **Defined Contribution Plan** – A defined contribution plan, like a 403(b) and the 457(b), allows an employee to contribute money to the plan on a tax deferred basis. Upon retirement the amount contributed and any investment gains will become available for withdrawal at the discretion of the employee. The employee bears the investment risk. The 403(b) and 457(b) sponsored by AACPS are defined contribution plans.
- **Diversification** – Diversification is an investment strategy that encourages investing in different options with different return patterns over time. In other words, "Don't put all your eggs in one basket." Diversification may include investing in different types of funds – stock funds, bond funds, money market funds.

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- **Dollar-cost averaging** – Dollar-cost averaging is a process of investing a fixed dollar amount to buy securities at regular intervals. When the prices are lower, the investor buys more shares or units; when prices are higher, the investor purchases fewer shares or units.
- **Fiduciary** – A fiduciary is a person or organization that acts on behalf of another person to manage assets. Fiduciary duties are both ethical and legal. They are required to act in the best interest of plan participants.
- **Glide path** – Glide path refers to the gradual reduction of risk within a portfolio based on the number of years to a target date (generally, this would be retirement date).
- **Growth fund** – A growth fund is a fund that invests primarily in the stocks of companies with above-average risk in return for potentially above-average gains.
- **Hardship and unforeseen emergency withdrawals** – Retirement funds may be available from a 403(b) and 457(b) to alleviate certain immediate and heavy financial or an unforeseen emergency such as purchase of a primary residence, tuition expenses, prevention of eviction or foreclosure, or burial or funeral expenses. Contributions may not be made to the 403(b) for six months after a hardship withdrawal. Hardship and unforeseen emergency withdrawals may not be re-paid to the plan(s).
- **Index fund** – An index fund is a mutual fund that is designed to mirror an index, such as the S&P 500. An index fund is passively invested in that there are no fund managers actively trying to beat the market. They are typically lower cost funds.
- **In-service distributions** – Distributions may be available from a 403(b) or 457(b) account even if you are still working. Up to \$5,000 may be available from the 457(b), provided no contributions have been made to the plan within the past two years and there has not been a prior in-service distribution. With the 403(b), an in-service distribution may be available without penalty upon attaining age 59 ½. Generally, there is a 10% federal tax penalty on withdrawals taken before age 59 1/2, though there are some exceptions. There are no early withdrawal penalties in a 457(b) plan. Distributions are taxed when paid out.
- **Money market fund** – A money market fund is a fund that invests in short-term, high-grade fixed income securities, and seeks the highest level of income consistent with preservation of capital.
- **Mutual fund** – A mutual fund is a type of pooled fund operated by an investment company that raises money from shareholders and invests it in stocks, bonds, options, futures, currencies, or money market securities. Mutual funds offer investors the advantages of diversification and professional management. Shares are redeemable on demand at net asset value by shareholders, who share equally in the gains and losses generated by the fund.
- **Net asset value** – Net asset value is like a stock price. It is the value of one share of a fund. It is the price at which investors can buy or sell their shares at the end of the trading day.
- **Normal retirement age** – The age at which full retirement benefits are payable, unreduced for early retirement. Normal retirement age for Social Security is age 56-67 depending on your date of birth.
- **Prospectus** – A prospectus is the written statement that discloses the terms of a securities offering or mutual fund including investment objectives, risks, services and fees. Strict rules govern the information that must be disclosed to investors in the prospectus.
- **Rebalancing** – Rebalancing is the process of moving money from one type of investment to another to maintain a desired asset allocation.
- **Required minimum distribution** – Minimum amounts that must be withdrawn annually from a retirement account starting with the year in which the employee reaches 70 ½ years of age, or if later, the year in which the employee retires. Generally, the amount that must be paid is calculated by dividing the prior December 31 account balance by a life expectancy factor published by the IRS.
- **Risk tolerance** – Risk tolerance refers to your comfort level when it comes to accepting risk of loss as you pursue financial reward. The more risk you are comfortable accepting, the greater your “risk tolerance” is said to be.
- **Social Security** – A federally run insurance program that provides benefits to American retirees, their survivors, and workers who become disabled.
- **Stock** – An investment representing ownership interest in a corporation.
- **Target date (or Lifecycle) Fund** – Target date funds, also known as lifecycle funds, maintain your asset allocation based on your target retirement date. Generally, target date funds shift to lower risk assets as you get closer to retirement.
- **Valuation** – The process of determining the current worth of an asset.
- **Value fund** – A value fund seeks to invest in stocks that are deemed to be undervalued by the fund's managers because of high dividend yields and/or fundamentals that indicate a higher value than the current price.
- **Volatility** – Volatility refers to the amount and frequency of fluctuations in the price of a security, commodity or a market within a specified time period.