
Pension Glossary

401(k) Plan A defined-contribution pension plan offered by many corporations.

403(b) Plan A retirement plan that is provided by nonprofit entities, such as public school systems, hospitals and 501(c)(3) entities. These plans are also called Tax-Sheltered Annuities (TSA).

Actuarial Assumptions A group of assumptions set about future inflation, rates of return, salary growth, probable death rates, and probable disability. As a whole, these form a basis for the actuary to determine the liability of the pension fund and the amount of money that needs to be paid into the plan.

Actuarial Valuation The actual cost of the municipality's pension plan based on the plan's demographics. The cost study is based on the plan's determined retirement age, benefit level, years of credited service, and the individual demographics of the employees. The actuary calculates how much money is needed to fund the pension.

Actuary A qualified independent professional who determines the amount of money that needs to be deposited in a defined benefit plan to ensure adequate assets accumulate to pay the promised benefit.

Aggregate Volatility The volatility of a total portfolio, as opposed to the volatility of individual securities, individual managers, or individual asset classes.

Agreement The document or contract between the employing municipality and employee that details the retirement benefits and eligibility requirements for plan members.

Alternate Payee A spouse, former spouse, child, or other dependent having a right to receive a portion of the participant's benefits under a Qualified Domestic Relations Order (QDRO).

Alternative Asset Classes Asset classes other than traditional asset classes such as stocks and bonds.

Annuitant A retiree or a survivor or beneficiary of a retiree who receives a monthly periodic payment.

Annuity A series of periodic payments that typically continues for the lifetime of the participant. Optional forms include a joint and survivor annuity and a term-certain annuity that pay a beneficiary a predetermined amount if the participant dies first.

Asset Class A category of assets, such as large U.S. stocks or high-yield bonds, or venture capital.

Asset/Liability Studies Studies based on (a) assumptions about the future performance of specific asset classes, and (b) projected liabilities of a pension fund, to determine an optimal asset allocation.

Back-Loaded Mutual Funds Mutual funds that charge a fee when an investor sells the mutual fund.

Benchmark A basis of comparison for the investment return of an investment manager or for an overall portfolio.

Beneficiary The joint annuitant or any other person, estate, or trust fund you last designated in writing to receive any benefits which may be payable upon your death.

Benefit Payment Forms Payment options, such as Single-life, 50 Percent Joint and Survivor, 100 Percent Joint and Survivor, Period Certain, or Certain and Life.

Book Value The price that was paid for an investment.

Capitalization of a Stock The number of a company shares outstanding (or available for trading), times the price of its stock.

Cash Balance Plan A defined benefit plan that looks like a defined contribution plan. Participants have hypothetical account balances that earn a guaranteed rate of interest.

Certificate of Deposit A deposit with a bank of a specific amount of money for a specific time at a specific rate of interest.

Commingled Fund A fund in which two or more clients invest. Mutual funds, group trusts, and most limited partnerships are common examples.

Compensation The salary, wages, and other earnings paid to a member for employment which is used in calculating the pension benefit.

Consumer Price Index (CPI) The index of inflation for the previous year as released each January by the U.S. Bureau of Labor Statistics.

Correlation A statistical term measuring the amount of similarity between the volatilities of any two indices, individual securities, or investment portfolios.

Cost of Living Adjustment (COLA) An annual adjustment in wages to offset a change (usually a loss) in purchasing power most often derived by the CPI.

Custodian The organization that holds and reports on the assets of an investment fund.

Deferred Retirement Option Plan (DROP) A DROP plan is an arrangement under which an employee who would otherwise be entitled to retire and receive benefits under an employer's defined benefit¹ retirement plan instead continues working. However, instead of having the continued compensation and additional years of service taken into account for purposes of the defined benefit plan formula, the employee has a sum of money credited during each year of the continued employment to a separate account under the employer's retirement plan. The account earns interest (either at a rate stated in the plan, or based on the earnings of the trust underlying the retirement plan). The account is paid to the employee, in addition to whatever benefit the employee has acquired under the defined benefit plan based on earlier years of service, when the employee eventually retires.

Derivative A security such as a convertible bond or futures contract where the market value is derived all or partially from a different security.

Diversifiable Risk Volatility that can be eliminated through diversification.

Diversification Assembling a portfolio of securities that fluctuates in value differently from one another.

Diversification Benefit The reduction in volatility or increase on return that can be gained through the diversification of a portfolio.

Dividend Yield A stock's dividend as a percent of its market value.

Dollar-Weighted Return Internal rate of return, the average percent return on every dollar that was invested over an interval of time.

Duration A measure of the average amount of time before returns on an investment are realized, including both interest and principal payments.

Early IRA Withdrawal Penalty A 10 percent penalty on money withdrawn from an IRA retirement plan before age 59 1/2. There are some exceptions to the penalty, such as payments on account of death, disability, termination of employment after age 55, and payments to an ex-spouse due to a qualified domestic relations order.

Efficient Frontier Given assumptions for the return, volatility, and correlation of each asset class, the Efficient Frontier is a graph showing the highest return that can be achieved at every level of portfolio volatility.

Elective Deferral A contribution that an employee makes to a 401(k) plan.

Emerging Markets Stock and bond markets of the less developed countries of the world.

EPS (Earnings Per Share) The net earnings of a company divided by the number of its outstanding shares.

ERISA (Employee Retirement Income Security Act) A law passed in 1974 covering qualified retirement plans that include the Internal Revenue Service pension laws, Department of Labor provisions, and the Pension Benefit Guaranty Corporation (PBGC).

Fiduciary Any person or entity that exercises discretionary authority or control over a plan or its assets and any person who gives investment advice to the plan for a fee. Generally, the employer, the trustee, and the investment advisor are fiduciaries.

Fixed Income Bonds and cash equivalents where principal and interest payments are fixed.

Forfeitures The portion of an account that a participant loses if he/she terminates employment before becoming 100 percent vested.

Front-Loaded Mutual Fund A mutual fund that deducts a sales charge from a purchase of that fund.

Frozen Plan A plan that continues to exist even though employer contributions have been discontinued or future accruals have ceased.

Funding Deficiency For defined benefit or money purchase plans, the amount of the minimum required contributions that were not funded by the minimum funding deadline (eight-and-a-half months after plan year-end).

Funding Ratio The ratio of (a) the market value of a pension fund to (b) the present value of the liabilities of that pension fund.

GDP/GNP Gross Domestic Product and Gross National Product are two measures of the size of a nation's economy.

Growth Stocks Stocks with higher growth rates in earnings per share.

Hardship Withdrawal An in-service withdrawal from a 401(k) or 403(b) plan because of the immediate and heavy financial need of a participant.

Hedge An investment that reduces the risk of another investment.

Hedge Funds A term designated for a broad range of funds that make both long and short investments, sometimes using a variety of derivatives.

High-Grade Bonds Bonds with high quality ratings.

High-Yield Bonds Bonds with lower quality ratings, once known as "junk bonds."

Illiquid Assets Assets that cannot be rapidly sold or otherwise converted to cash, usually for at least a year and perhaps for many years.

Index (a Securities Index) A measure of the investment return on an asset class.

Index Funds An investment fund that is designed to replicate as closely as possible the return on a particular index; for example, an S&P 500 index fund.

Individual Retirement Account (IRA) A qualified retirement plan into which an individual may contribute pretax dollars and keep the money tax-free until retirement age. The individual may withdraw the money without penalty anytime between ages 59-1/2 and 70-1/2.

In-House Management Management of all or a portion of a fund's investments by its internal staff.

Integration A feature of the plan whereby benefits are integrated with Social Security. An integrated plan generally provides larger benefits for employees who earn more than the Social Security taxable wage base. After 1986 integration was renamed "permitted disparity."

Leverage Investing with the use of borrowed money or credit.

Liabilities of a Pension Fund The value of promises made to the participants in a pension plan, usually the present value of those promises.

Liquid Assets Assets that can be sold or otherwise converted to cash in less than a year.

Long/Short Investments Investments that are both long and short, such as buying security A (long) and borrowing and selling security B (short), so that results depend entirely on the difference in return between securities A and B.

Market-Neutral Investments Investments where volatility has a very low correlation with the volatility of the stock and bond markets.

Market Value The price at which an investment could be sold at any given time.

Median The midpoint of a distribution, with half above and half below.

Micro Stocks Midsize stocks, such as (in the United States) stocks smaller than those included in the Russell 2000 index.

Mid-Cap Stocks Midsize stocks, such as (in the United States) stocks larger than those included in the Russell 2000 index, but excluding the larger stocks.

Money Market Mutual Funds Mutual funds that invest in fixed income securities shorter than one year in maturity, funds whose price is not expected to fluctuate.

Multiemployer Plan A retirement plan sponsored by more than one employer that is established pursuant to a collective bargaining agreement (union).

Net Returns Investment returns that are net of all fees and expenses.

Normal Retirement Age An assumed retirement age that is specified in the plan document. Participants are not required to retire when they reach retirement age. Participants generally continue to earn benefits if they work past retirement age. Participants are 100 percent vested at normal retirement age.

Operating Policies An organization's written policies relative to the operation of its investment committee.

Options The right, but not the obligation, to buy a security from (or sell a security to) a particular party at a given price by a given date.

PBGC (Pension Benefit Guaranty Corporation) A U.S. government agency that insures the payment of pension benefits up to a certain benefit level in the event that a private pension plan is terminated and can't come up with the money to meet its promises.

Plan Administrator The entity that has responsibility to administer the plan (i.e., collect data, calculate contributions, and pay benefits). Generally, the company is the Plan Administrator. Oftentimes, a company will appoint a committee to act as its agent to administer the plan. In addition, the Plan Administrator or committee can hire a company (third-party administrator or record keeper) to help it administer the plan. The Plan Administrator has legal responsibility for the plan and can be sued.

Plan Sponsor The business entity that sponsors the plan and has responsibility for the plan.

Policy Asset Allocation The target asset allocation that an organization has established in its Investment Policies.

Portfolio All of the securities held by an investment fund.

Predictive Value The extent a manager's past performance may provide some indication of that manager's future performance.

Price/Earnings Ratio The ratio of a stock's price to its earnings per share.

Private Investments Investments that are not sold publicly.

Proxy The voting on issues to be decided at a stockholder's meeting.

Quantitative Managers Managers who develop and rely on mathematical algorithms to determine the transaction to be made in managing an investment portfolio.

Quartile One-quarter of a distribution, for example the top 25 percent or the bottom 25 percent.

Real Return Investment return in excess of inflation.

Rebalancing Transactions that bring a portfolio's asset allocation closer to the investment fund's Policy Asset Allocation.

Reinvested Dividends Dividends paid by a stock that are used to buy more shares of that stock. For example, a total return index assumes that all dividends are reinvested.

REITs (Real Estate Investment Trusts) Common stocks of companies that invest in real estate, but instead of paying corporate income tax pass their income tax liability on to their stakeholders.

Required Minimum Distributions The minimum amount that must be paid to a participant each year after attaining age 70 1/2.

Retirement Eligibility Meeting the age and service requirements to be eligible for retirement.

Risk The probability of losing money, or that the value of an investment will go down. For a portfolio of investments, risk is often defined as volatility, which over long intervals tends to encompass most individual risks.

Risk-Adjusted Return Return-on-investment adjusted for its volatility over time, with a volatile investment requiring a higher return and vice versa.

Rollover A tax-free transfer of cash or other assets from one retirement plan to another retirement plan or to an IRA.

Rollover IRA An individual retirement account that is established for the sole purpose of receiving a distribution from a qualified plan. Oftentimes distributions in rollover IRAs can be rolled back into a qualified plan.

Roth IRA An IRA in which the contributions are nondeductible and the distributions are non-taxable.

SAR (Summary Annual Report) A summary of the Form 5500 (annual report) that is required to be distributed to plan participants.

Securities Evidence of ownership or debt, such as stocks or bonds.

Separate Accounts A portfolio that is held for only one investor. (Insurance companies, however, use "separate accounts" to denote a portfolio held for one or more investors that is valued for those investors at market value.)

Short Selling Borrowing a security and then selling it.

Short-Term Investment Fund (STIF) A money market fund provided by a bank for investment clients for whom the bank serves as custodian.

Small Stocks Stocks with relatively low capitalization, sometimes measured by the Russell 2000 index.

Social Investing Overlaying a fund's investment objectives with a set of social goals that constrain the fund from investing in certain kinds of companies or that encourage it to invest in certain other kinds of companies.

Social Security Retirement Age The age, used as the normal retirement age under the Social Security Act to pay unreduced benefits, that depends on the calendar year of birth.

SPD (Summary Plan Description) A detailed, but easily understood, summary of the plan that must be provided to participants and beneficiaries.

Standard Deviation A measure of volatility of the return on a security or a portfolio.

Style The manner in which a manager invests, such as in small, medium, or large stocks, or in growth stocks or value stocks.

Systemic Risk The portion of a security's volatility that is highly correlated with all or a portion of the market; for example, the portion of a stock's volatility that is highly correlated with the overall stock market or with other stocks in its own industry.

Tactical Asset Allocation A strategy of moving investments between different asset classes (such as between stocks and bonds), depending on which seems more attractive at time. Such strategies are typically driven by quantitative models.

Target Asset Allocation See Policy Asset Allocation

Time Diversification Purchasing investments in an asset class in multiple different years.

Time Horizon The time between when one makes an investment and when one will need to use the money for other purposes.

Time-Weighted Return The compound annual growth rate of a dollar that was in a portfolio from the beginning of an interval to the end of that interval. The portfolio's performance in each unit of time is given equal weight.

TIPS (Treasury Inflation-Protected Securities) Inflation-linked bonds are issued by the U.S. government.

Total Return The investment return on a security or a portfolio that includes income (such as dividends and interest) and capital gains (whether realized or not), net of all fees and expenses.

Total Return Index A securities index that assumes that all dividends are reinvested in the issuing company's stock.

TPA (Third Party Administrator) An outside company hired by the Plan Administrator to assist in administering the plan.

Track Record The historical investment performance of a manager.

Transaction Costs The total costs involved in buying or selling a security, including both brokerage commissions and market impact costs.

Treasury Bill (T-Bill) A short-term loan to the U.S. government.

Trust A legal entity established under state law to hold and administer plan assets. Federal law allows the trust to be tax-exempt.

Trustees The parties responsible for managing the trust. The trustees can manage the plan's assets or can appoint an investment manager.

TSA (Tax Sheltered Annuity) A type of retirement plan provided by non-profit entities such as public school systems, hospitals and 501(c)(3) entities. These plans are also called 403(b) plans.

Unfunded Liability The amount of funds or time (commonly measured in years) needed to pay for improvements over the years for present members and retirees who formerly contributed at a lower contribution rate for a lesser program.

USERRA The Uniformed Services Employment and Reemployment Rights Act of 1994, which prohibits discrimination against employees because of membership in the uniformed services.

Value Stocks Stocks with lower price-to-book-value ratios.

Venture Capital Private corporate investments, especially in start-up companies.

Vested The rights members of a retirement plan acquire by length of service needed to receive benefits.

Vesting The percentage of a participant's account or benefit that he or she owns and is entitled to when he or she terminates employment.

Volatility Fluctuation in the market value of a security or a portfolio.

Voluntary Contributions After-tax amounts that a participant voluntarily contributes to a retirement plan.

Wealth The total market value of a portfolio at any given time.

Wilshire 5000 Index A capitalization-weighted index of virtually all stocks traded in the United States, including foreign stocks listed on U.S. exchanges.

Withdrawal from a Fund The cash payment by an investment fund to its sponsor or to its plan participants.

Workers Compensation A state government system designed to address work-related injuries.