



CALIFORNIA EDUCATOR'S GUIDE TO 403(b) AND 457 PLANS

INVESTING FOR **YOUR** FUTURE.



CTA Business Initiatives & Development Department
ctainvest.org

nea

CALIFORNIA TEACHERS ASSOCIATION 403(b)/457 GUIDE FOR EDUCATORS

Investing for Your Future **A Message from David Sanchez**



Dear Colleague,

As a classroom teacher, I know about the challenges you face, juggling the important work you do with the demands of home and family. Your own needs, such as preparing for the future, may take a back seat to more pressing concerns. However, I also know how important it is to save for retirement by investing in a 403(b) or 457 plan.

I recall the difficulty I had in making investment choices for my own plan. But it doesn't have to be overwhelming. One of my goals as CTA president – and your advocate – is to provide you with financial planning and investment education and resources. We want to empower you to make informed choices. That is why we have produced our new 403(b)/457 Guide for Educators, *Investing for Your Future*.

Along with this guide, we've developed a new Web site, the California Educators Investment and Retirement Guide, at www.ctainvest.org. The site includes a wealth of information that can help you create a plan for a more secure financial future.

CTA continues work on your behalf, recognizing the vital role that educators play in building a better future for our children. With this guide, our Web site and other investment and retirement educational materials, we hope to help you build a better future for yourself as well.

A handwritten signature in black ink that reads "David A. Sanchez". The signature is written in a cursive, flowing style.

David A. Sanchez
President
California Teachers Association

CONTACT US

CTA Risk Management/Business
Initiatives & Development Department

1705 Murchison Drive

Burlingame, CA 94010

business_initiatives@cta.org

Phone: (650) 552-5200

Investing for *YOUR* Future

As a dedicated educator, you deserve a future that includes a financially comfortable retirement. Your defined benefit pension plan through CalSTRS or CalPERS is an excellent starting point, and CTA works hard on your behalf to protect and enhance your pension benefits.

Still, your CalSTRS or CalPERS pension may not provide enough retirement income to support the lifestyle you envision. Fortunately, you have another key advantage in your favor: the option to participate in a 403(b) or 457 defined contribution plan. By

choosing to contribute to a 403(b) or 457 plan through your district, you have a unique opportunity to supplement your defined benefit pension.

CTA has developed this guide to explain how 403(b) and 457 plans work, what they can do for you and how you can best take advantage of them. Don't delay. Read the guide, and if you haven't signed up for your 403(b) or 457 plan, consider doing so today. The sooner you start saving, the greater your potential to reap the rewards of a financially secure and dignified future.

Table of Contents

2.....	What Is a 403(b) Plan?	24.....	About Annuities
3.....	What Is a 457 Plan?	26.....	What You Need to Know About Fees
4.....	Contribution Limits	28.....	What Is 403bcompare.com?
5.....	Comparison Chart	29.....	Choosing the Investments in Your Plan
6.....	Roth 403(b)s and Roth IRAs	30.....	Selecting a 403(b) or 457 Plan Vendor
7.....	What Optional Benefits May Be Available in Your Employer's Plan?	33.....	Changing Your Investments
7.....	Next Steps	35.....	Working with a Financial Professional
8.....	Why Do You Need a 403(b) or 457 Plan?	38.....	Income Options When You Retire
10.....	The Tax Benefits of 403(b) and 457 Plans	40.....	How the New 403(b) Regulations Affect You
14.....	Before Investing, Know Your Investing Options	42.....	So Now What Do I Do?
15.....	Asset Classes	43.....	Glossary
17.....	403(b) and 457 Plan Investment Options	45.....	Questions to Ask Agents
18.....	Types of Mutual Funds	46.....	Questions to Ask Before Investing
21.....	Mutual Funds – The ABCs of Fees and Share Classes	47.....	Risk Tolerance Quiz
23.....	What Do Indexes Measure?	48.....	Resources



Introduction to 403(b) and 457 Plans

What Is a 403(b) Plan?

A 403(b) plan is a voluntary **defined contribution** retirement plan for employees of public schools, employees of eligible tax-exempt organizations and some ministers. It's sometimes referred to as a tax-sheltered annuity (TSA). A 403(b) plan is similar to a 401(k) plan in the private sector – a way to empower workers to save toward retirement.

403(b) plans are offered by your employer, who is the plan sponsor. The plan sponsor has specific reporting and compliance responsibilities for the administration of the plan. Plan documents spell out the overall offering of a 403(b) program, including approved vendors who offer an array of investments to plan participants. To find the approved vendors in your district's plan, visit 403bcompare.com.

How 403(b) Plans Work

A defined contribution plan such as a 403(b) plan gives you the opportunity to supplement your **defined benefit** plan (CalSTRS or CalPERS) with your own savings.

- When you decide to participate in a 403(b), you (the plan participant) complete a salary reduction form and submit it to your district. Don't be alarmed by the terminology. Salary reduction doesn't mean you're lowering your salary. It simply means you will contribute a certain amount of your pay each pay period that will be used to purchase shares in the investments you choose through the vendors available within your plan.
- You make contributions to your 403(b) account with the vendor(s) of your choice, up to annual allowable limits, on a pre-tax basis from your paycheck. We'll cover pre-tax contributions and tax-deferral more starting on page 10.
- You choose the investments from among those offered by the approved vendors available in your plan, and you assume the investment risk.
- The amount you accumulate for retirement will depend on the amount you contribute, how long you participate in the plan, the performance of the investment choices you make and the fees charged by your plan and the investments within the plan.
- If you leave your job, you can roll over your balance to another employer-sponsored retirement plan,



such as another district's 403(b) or 457 plan (as long as the new plan accepts rollovers), or roll it into an **individual retirement account (IRA)**.

Tax Benefits

When you contribute to a 403(b) plan, your contributions are deducted from your pay on a pre-tax basis. In addition, your earnings grow tax-deferred. We'll explain more about this on page 10.

Investment Options

Your district's 403(b) plan provides a convenient way for you to invest in any of the annuity or mutual fund investment options offered by the approved vendors in your plan. We will go into further detail about different types of investments offered by 403(b) vendors that may be available in your district's plan on page 17.

A Bit of HISTORY

403(b) plans were introduced in 1958 as a way for employees of public schools and other eligible institutions to put away money for retirement on a tax-deferred basis. Originally, annuities were the only allowable investment option. In 1974, Congress allowed participants to also invest directly in mutual funds through 403(b)(7) custodial accounts.

In 2008, new regulations were passed to make a 403(b) more like a 401(k) plan in the private sector, including the requirement that the plans be governed by a plan document maintained by your employer. The plan document includes a list of approved 403(b) vendors, and therefore you may now have more or different investment choices than you did before the regulations were put into place.

What Is a 457 Plan?

Your district may also offer a 457 plan. A 457 plan is similar to a 403(b) plan, but intended for state and government employees. Established by Congress in 1978, the basic features of a 457 plan are the same as a 403(b) plan:

- Pre-tax contributions
- Tax-deferred growth
- Portability if you leave your job
- The district is required to have a written document governing the program and its features, such as loans and hardship withdrawals.
- The district providing the plan must assume compliance responsibilities.
- Salary reduction agreements are the same.

There are some major differences:

- The assets in a 457 plan are held in a contract by the employer rather than the employee. It's important to note that the assets in your 457 plan account are protected from your employer's creditors by law.
- There is no penalty for early distributions from a 457 plan, as there is with a 403(b) plan (see page 5).
- Roth provisions are not approved for 457 plans.
- There is no requirement that the 457 plan be offered to all employees, as there is with a 403(b) plan.
- There may be some different investment options available in a 457 plan.

To learn more: Visit www.ctainvest.org.

Can I Contribute to *BOTH*?

Yes! If you are eligible for and have access to a 403(b) and a 457 plan and have enough includable compensation, you can contribute the maximum amount to each of the plans. In other words, up to \$16,500 to your 403(b) and \$16,500 to your 457, for a total of \$33,000 – more if you are eligible for the age 50 or other catch-up provisions.



Contribution Limits for 2009

	CONTRIBUTION LIMIT	AGE 50 CATCH-UP	OTHER CATCH-UP PROVISIONS
403(b)	\$16,500	\$5,500	15-year rule*
457	\$16,500	\$5,500	3-year provision**

* Eligible employees with 15 or more years of full-time service may be able to contribute up to \$3,000 more for five years, or a maximum of \$15,000.

** Employees may be eligible to defer up to two times the contribution limit in effect for the final three years of service. Employees cannot participate in the 3-year catch-up and the 457 plan age 50+ catch-up during the same tax year.



Retirement Plan Comparison Chart

	401(k) (for comparison only)	403(b)	457	Roth 403(b)
Who is eligible?	Employees whose employers offer the plan (private employers, some nonprofit employers)	Employees of nonprofits such as public schools and some hospitals, charitable organizations	State and local government employees	Employees of nonprofits such as public schools and some hospitals, charitable organizations
Pre-tax contributions?	Yes	Yes	Yes	No
Limits on employee contributions (2009)	Up to \$16,500	Up to \$16,500	Up to \$16,500	Up to \$16,500
Age 50+ catch-up contributions	\$5,500	\$5,500	\$5,500	\$5,500
Other catch-up	No	Yes – 15-year rule*	Yes – final 3-year provision**	Yes – 15-year rule*
Distributions while still employed (in-service distributions)	Only on hardship if under age 59½	Only on hardship if under age 59½	Only on account of unforeseeable emergency	Only on hardship if under age 59½
Distributions without tax penalties	<ul style="list-style-type: none"> Retirement after age 55 Death or disability Payments after age 59½ Lifetime annuity or installments Rollover to other qualified plan or IRA 	<ul style="list-style-type: none"> Retirement after age 55 Death or disability Payments after age 59½ Lifetime annuity or installments Rollover to other qualified plan or IRA 	<ul style="list-style-type: none"> Termination from employment at any age Death or disability Unforeseeable emergency 	<ul style="list-style-type: none"> Age 59½ and hold account at least five years Other provisions same as 403(b)
Distributions with penalties	10% prior to age 59½, except as above	10% prior to age 59½, except as above	None	Same as 403(b)
Required minimum distributions***	April 1 following the year participant reaches age 70½	April 1 following the year participant reaches age 70½	April 1 following the year participant reaches age 70½	Same as 403(b)
Tax treatment of distributions	Ordinary income tax	Ordinary income tax	Ordinary income tax	Tax-free if qualified distributions
Rollovers allowed to other plans	<ul style="list-style-type: none"> Yes – to 401(k), 403(b) or 457 plan (allowed but not required) Yes – to IRA 	<ul style="list-style-type: none"> Yes – to 401(k), 403(b) or 457 plan (allowed but not required) Yes – to IRA 	<ul style="list-style-type: none"> Yes – to 401(k), 403(b) or 457 plan (allowed but not required) Yes – to IRA 	To another designated Roth account, but only by direct rollover (allowed but not required)

* Eligible employees with 15 or more years of full-time service may be able to contribute up to \$3,000 more for five years, or a maximum of \$15,000.

** May be eligible to defer up to two times the contribution limit in effect for the final three years of service. Employees cannot participate in the 3-year catch-up and the 457 plan age 50+ catch-up during the same tax year.

*** Required minimum distributions are waived for 2009 only.

What Is a Roth 403(b)?

You may have heard about a Roth individual retirement account (IRA). In January 2006, the Roth 403(b) was introduced. Your district may offer a Roth 403(b) option, but it is not required to.

If your district does offer a Roth feature with its 403(b) plan, you have a decision to make. Should you choose the traditional 403(b), which gives you upfront tax savings, or a Roth 403(b), which offers tax-free distributions when you retire? Your choice will depend on your goals and financial circumstances.

Comparing the Accounts

With a **traditional 403(b)** retirement plan, your contributions are made before taxes, so you save on your current tax bill. Contributions and earnings grow tax-deferred, and withdrawals at retirement are taxed at ordinary income tax rates.*

With a **Roth 403(b)**, your contributions are made on an after-tax basis; there is no current tax break.

Contributions and earnings can be withdrawn tax-free at retirement if certain conditions are met.**

So Which Is Better?

There is no right answer for everyone. Whether a Roth 403(b) rather than a traditional 403(b) makes sense for you will depend on your current and anticipated financial situations. If you expect your tax bracket to be lower in retirement than it is now, it may make sense to contribute to a traditional plan and take advantage of the tax break now. However, if you expect your tax bracket to be the same or higher in retirement, it may make sense to contribute to a Roth 403(b) and benefit from tax-free withdrawals later.

A financial or tax advisor can help you look at the options to see which makes more sense for you.

* Withdrawals made prior to age 59½ (age 55 if leaving your job) may be subject to a 10% tax penalty.

** Withdrawals from a Roth 403(b) plan are tax-free if the account has been held at least five years and the account holder is at least age 59½. Nonqualified withdrawals are subject to ordinary income tax rates and a 10% tax penalty.

Note that there are no provisions for a Roth 457 plan.

What about a Roth IRA?

A Roth IRA is different from a Roth 403(b) in several important ways:

- It is a personal account. You do not participate through your employer. Instead, you set up a Roth IRA with a credit union, bank or broker and invest through them.
- You cannot establish a Roth IRA if your income is greater than \$176,000 for married couples

filing jointly or \$120,000 if you are a single filer. (These amounts are for 2009 and may be indexed to inflation in future years.) There is no income restriction to participate in a Roth 403(b).

- A Roth IRA has the same contribution limits as a traditional IRA, which are much lower than the contribution limits for a 403(b) plan. In 2009, you can contribute up to \$5,000 to an IRA, or \$6,000 if you are age 50 or older.

What Optional Benefits May Be Available in Your Employer's 403(b) Plan?

Loans

Your district's 403(b) plan may offer loans. But keep in mind that the reason you are saving in a 403(b) plan is for your long-term financial health. Explore all other options for loans before taking money out of your 403(b) plan through a loan. If you borrow from your 403(b) plan, you will likely pay:

- A loan processing fee, which can be \$100 or more.
- An interest rate determined by the 403(b) provider. This interest is generally paid back to your account.

Loan Pitfalls

- You lose out on any compounding earnings (see page 13) while the loan is outstanding.
- You pay back the loan with after-tax dollars. When you eventually withdraw the money from your plan in retirement, you will pay taxes again – essentially, double taxation.

Other optional features may include:

- Exchange and transfer of contracts.
- Hardship withdrawals.
- In-service withdrawals of rollover contributions.

You will need to review the features available in your district's 403(b) plan, as well as the options available through your chosen 403(b) vendor.

Next STEPS:

- Contact your district to sign up for a 403(b) and/or 457 plan or to identify the approval list for 403(b) vendors.
- Determine what types of investment products available through your plan's approved vendors meet your needs (see page 29).
- Determine your risk tolerance (see the quiz on page 47). This quiz is just to give you a general idea of your risk tolerance. You may want to consult with a financial advisor for more information.
- Go to ctainvest.org and use the 403(b) calculator and Webinar, "Asset Allocation: A Strategy for Life."
- Go to 403bcompare.com to compare vendors, their investment options and fees, to make your 403(b) plan investment selection(s). See page 17 for more about choosing your investment options.
- Choose the amount you want to contribute and the investments you want in your plan and complete a salary reduction form.

Learn more at www.ctainvest.org.

Why Do You Need a 403(b) or 457 Plan?

Everyone has dreams for retirement. Perhaps you'd like to travel the world or indulge in a hobby. Maybe you dream of having a second home on a beach. Or maybe you'd like the financial wherewithal to help an adult child or grandchild purchase their first home or launch a business. The reality is that retirement is expensive, for a number of reasons:

Inflation – Even a very low rate of inflation can erode your savings over a long period (see chart on next page).

Health care expenses – It's estimated that a married couple age 65 may need \$295,000 in retirement savings just to cover health insurance premiums and out-of-pocket expenses during retirement.

Longevity – Living longer is usually a good thing, but it can also mean that you run out of money if your savings are insufficient to cover decades in retirement. The average age of retirement for CalPERS members is 60; for CalSTRS, 61.3. That means you could easily spend 20 years or more without a paycheck.

Your Pension Is Not Enough

If you are counting on your CalSTRS or CalPERS pension to see you through, consider this:

60%-65% = Percentage of salary the California State Teachers Retirement System (CalSTRS) pension replaces, on average, for current and retired members, according to CalSTRS.*

\$1,876 = In 2006, the average monthly check for an employee who left after 20 years of service at age 60, according to CalPERS.

\$0 = Amount CalSTRS participants can expect in the form of federal Social Security benefits. (Please note that educators participating in the California Public Employees' Retirement System (CalPERS) do pay Social Security taxes and are eligible to receive benefits. In addition, CalSTRS participants may be eligible for Social Security



benefits from a spouse's earnings or earnings from other jobs, but those benefits may be reduced by the **Windfall Elimination Provision** or **Government Pension Offset**.)

90% = Percentage of salary financial experts recommend replacing in retirement to maintain same standard of living as your working years.

30%-40% = Percentage of CTA members who take advantage of a 403(b) retirement savings plan to supplement their pension plan.

The bottom line: The majority of educators are facing a retirement savings shortfall. That's why you need a 403(b) or 457 plan – to make up the difference.

Let's take a closer look at these sources of retirement income:

CalSTRS and **CalPERS** state pension funds. Your pension, or defined benefit plan, is an important part of your retirement savings. These retirement systems continue to provide a key benefit to educators. Your benefit is based on your age at retirement, years of service and final compensation level. You can run the numbers and estimate your benefit level by using the calculators on your pension's Web site (www.calstrs.com or www.calpers.ca.gov).

Social Security. Educators with a CalSTRS pension do not pay Social Security taxes. They contribute a greater percentage of pay into the pension fund instead, and therefore are generally not eligible for Social Security benefits. They may qualify for benefits earned through another job, although those benefits may be reduced due to the Windfall Elimination Provision. For more information, visit www.ssa.gov/pubs/10045.html. CalSTRS pensioners who are eligible to receive Social Security benefits based on a spouse's earnings may have their benefits reduced due to the Government Pension Offset (www.ssa.gov/pubs/10007.html).

Educators with a CalPERS pension pay 6.2% of salary for Social Security and generally qualify for Social Security benefits. Educators are often confused or mistaken about what they will collect from Social Security in retirement. You should receive an annual estimate of your projected benefit from the Social Security Administration, although the statement will not reflect adjustments due to the Windfall Elimination Provision or Government Pension Offset.

403(b) plan. The 403(b) is a voluntary tax-deferred retirement plan available for eligible employees of public schools and other tax-exempt organizations. It is called a defined contribution plan, because the participant makes contributions and investment decisions. It is different than your pension or defined benefit plan, where you and your employer make contributions to CalSTRS or CalPERS and they make all of the investment decisions. Ultimately, you are in control of your 403(b).

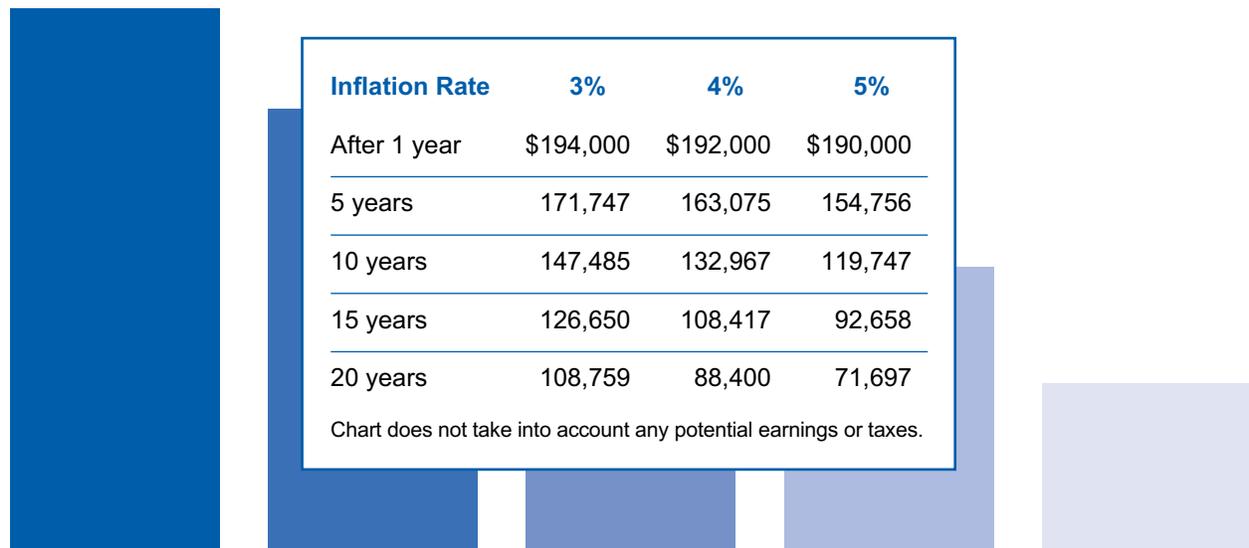
Prepare for a Financially Secure Retirement

The 403(b) or 457 plan is designed with features to help you make the most of your retirement savings. In 2009, you can contribute up to \$16,500, or an additional \$5,500 (total of \$22,000) if you are age 50 or older. If you're a long-term employee who has not consistently contributed to your plan, you may also be eligible to make lifetime catch-up contributions.

Visit www.ctainvest.org to find calculators that can help you estimate what you need to save for retirement based on your financial goals.

* Source: CalSTRS Policy Report, November 2007.

Here's how three different average rates of inflation could affect the value of a \$200,000 nest egg over time.



The Tax Benefits of 403(b) and 457 Plans

The federal government (and many state governments, including California's) want to encourage you to save for retirement. As a result, 403(b) and 457 plans offer two valuable tax advantages:

- Pre-tax contributions from your paycheck.
- Tax-deferred growth.

Pre-Tax Contributions – Current Tax Savings

With pre-tax contributions, you save on taxes now. That's because the money you contribute to a 403(b) or 457 plan is subtracted from your paycheck before federal and state income taxes are deducted.

Let's take this example: Suppose you are in the 25% federal tax bracket and 8% California income tax bracket. If you contribute \$100 in a pay period, it doesn't reduce your take-home pay by \$100. Instead, that \$100 contributed to your account could reduce your take-home pay by just \$67.

Put another way, let's say your gross paycheck is \$2,100. After federal and state taxes are deducted, your net pay is \$1,407. However, if you make a \$100 pre-tax contribution to your 403(b) plan, your net pay would be calculated like this: \$2,100 - \$100 = \$2,000 – 33% federal and state taxes = \$1,340 net pay. Your paycheck is reduced by \$67, but you've saved \$100.

457 and 403(b) Plan Contributions Let You Save on Taxes **Now**

Regular semi-monthly paycheck with no plan contribution:

$$\begin{array}{r}
 \$2,100 \text{ (gross pay)} \\
 - 33\% \text{ (federal and state income tax)} \\
 \hline
 \$1,407.00 \text{ (net pay)}
 \end{array}$$

With a pre-tax contribution to a 403(b) plan:

$$\begin{array}{r}
 \$2,100 \text{ (gross pay)} \\
 - \$100 \text{ (contribution = \$100)} \\
 \hline
 \$2,000 \text{ (federal and state income tax)} \\
 - 33\% \\
 \hline
 \$1,340 \text{ (net pay)}
 \end{array}$$

Contribution amount is \$100, but net pay is only \$67 less!

Note that no local or other taxes are considered in this simple calculation. Actual tax rates will vary depending on income, number of dependents claimed, amount of contribution, etc.



Note that this is a simplified example that doesn't take into account the effect of other deductions from your paycheck. But it does illustrate how pre-tax contributions work in your favor.

Tax-Deferred Growth – Continued Tax Savings

The benefit of a tax-deferred account is that taxes are deferred until withdrawal. In a taxable account – like an interest-earning savings account at a bank or credit union, or an investment account that you have on your own – taxes are due each year on the earnings.

In a 403(b) or 457 account, any earnings in the account – such as interest, dividends and capital appreciation (increase in price of the investment) – remain in the account until you begin withdrawing money.*

You will have to pay taxes on the money once you start withdrawing it (Uncle Sam wants his due, after

all). However, you may have already benefited from many years of compounding returns. In a taxable account, you would likely have to pay taxes on any earnings in the account each year. Instead, with a tax-deferred account, any positive investment returns remain in the account to potentially earn more returns. In addition, there is a possibility that you will be in a lower tax bracket after you retire, because you will no longer be drawing a steady paycheck.

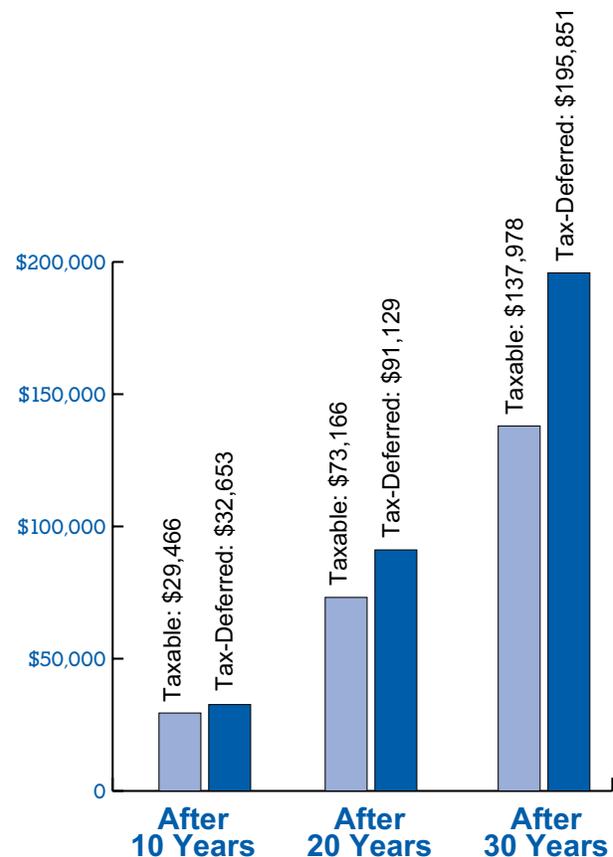
Finally, you can control the amount of money you withdraw from your 403(b) plan in retirement (subject to **required minimum distributions** – see page 38), which allows you to maintain some control over your tax bill in retirement.

* Taxes will be due upon withdrawal. Distributions before age 59½ (age 55 upon separation from service) may incur a 10% tax penalty. 10% penalty does not apply to 457 plans.

Tax-Deferred Savings

A tax-deferred retirement plan like a 403(b) or 457 plan can help grow your savings over time. For example, the chart compares a taxable account with a tax-deferred account. The amount invested is the same (\$200 a month), and the annual rate of return is the same (6%). The only difference is that the taxable account figures in an annual 33% combined federal and state income tax rate, while the 403(b) account grows tax-deferred.*

* Return shown is for illustration only and does not represent the return of any actual investment. Your results will vary. Taxes will be due upon withdrawal. Distributions before age 59½ (age 55 upon separation from service) may incur a 10% tax penalty (does not apply to 457 plans). Note that the taxable account's tax burden may be overstated by this example because it assumes that all earnings within the account are taxable every year. That could be the case with interest earnings and short-term capital gains reported by a mutual fund, but not necessarily the case in an account that had little or no trading during the year.



Long-Term Compounding

If you've been an educator for many years, it's still not too late to start saving for retirement. But if you are young and just starting out in your career, you have an important advantage over your older colleagues: time.

If you have decades before you retire, you can truly benefit from the magic of long-term compounding. Albert Einstein called compound interest "the most powerful force in the universe." Although that may be arguable, it's certainly the most powerful force you

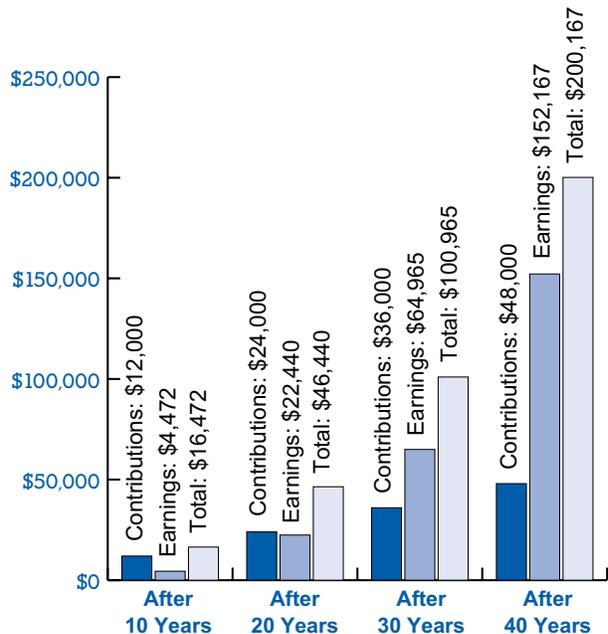
have working for you when you save and invest over many years. Compounding interest simply means that, when the money you invest (your principal) earns interest and/or dividends, those dividends and interest are added to your principal and begin earning more interest, and so on. Over time, the money you earn in your account can actually outpace the principal amount you invest.

Albert Einstein called compound interest "the most powerful force in the universe."

Over Time, Compounded Earnings Eclipse Contributions

As your money compounds for longer periods, the share of your balance from reinvested earnings grows. These charts show how your balance grows if you invest \$100 a month in a tax-deferred 403(b) or 457 plan that earns a 6% annual return.*

* Assumes \$100 a month invested in a tax-deferred 403(b) or 457 account at an annual average rate of return of 6%. Rate is for illustration only and does not represent the return of any actual investment. Your returns will vary. Taxes will be due upon withdrawal. Distributions from a 403(b) plan before age 59½ (age 55 upon separation from service) may incur a 10% tax penalty (does not apply to 457 plans).



Don't Delay – Start Today

Here's another reason why it makes sense to start saving earlier rather than later. When you start early, you can invest smaller amounts each month to reach your goals than if you start later, making your retirement plan contributions easier on your budget. For example, suppose two colleagues – let's call them Patricia Proactive and Patrick Procrastinator – start working at the same time. They are both 25

years old, eligible to participate in a 403(b) or 457 plan, and want to retire in 35 years, at age 60.

Patricia signs up for her 403(b) plan right away and starts investing \$150 a month. Patrick waits 10 years and starts investing \$300 a month. They choose investments that provide the same 6% average annual rate of return.* Here's how their accounts look:

Account Balance

	Patricia Proactive	Patrick Procrastinator
After 5 years	\$10,465	\$0
After 10 years	\$24,582	\$0
After 15 years	\$43,623	\$20,931
After 20 years	\$69,306	\$49,164
After 25 years	\$103,949	\$87,246
After 30 years	\$150,677	\$138,612
After 35 years	\$213,707	\$207,898
<i>Total amount contributed:</i>	<i>\$63,000</i>	<i>\$90,000</i>

To make up for the 10 years he lost, Patrick had to contribute twice as much each month as Patricia. He ended up contributing \$27,000 more and still accumulated \$5,809 less than she did.

* Rate of return is for illustration only and is not meant to represent the return of any specific investment. Your results will vary. No taxes or fees were included in the calculation. Investing in a 403(b) or 457 plan does not guarantee a profit or protect against loss in a declining market.

YOUR NEXT STEP:

If you haven't signed up for your 403(b) or 457 plan yet, look into it today!

Before Investing, Know Your Investment Options

Your district's 403(b) plan should present you with multiple options for investing your money. That's a good thing, because with investment options comes the chance to allocate your assets among different asset classes, instead of putting all of your funds in a single type of investment – a potentially high-risk move best warned against in the age-old saying: "don't put all your eggs in a single basket."

Instead, most investors use a strategy called asset allocation. The three main types of assets that will be found among the investment options in your 403(b) plan are:

- Stocks (also known as equities).
- Bonds (also often known as fixed-income investments).
- Cash equivalents (such as money market funds).

Because the investments you choose in your plan are typically mutual funds or annuities (see page 17), you are unlikely to invest in individual securities (stocks or bonds) within your 403(b) or 457 plan. Instead, you will likely choose investments that may include a variety of stocks, bonds or both. Still, it's important to understand the basics of asset allocation.

Why Use Asset Allocation?

Asset allocation is very important for investors because each of the asset classes listed above may have different performance ups and downs and at different times. By spreading your funds among different asset classes, you may be better able to smooth out fluctuations in your 403(b) or 457 plan account's overall investment performance.

In fact, a landmark study suggests that asset allocation may account for more than 90% of the variability in a portfolio's return.* The remainder of return performance is based on specific investment choices and market timing.

Just as your investment goals likely differ from those of other people, so too should your asset allocation be unique to you. It will depend on multiple factors, including your:



- **Investment goals** – essentially, how much money do you wish to accumulate, for what purpose, and by when?
- **Risk tolerance** – are you a conservative investor seeking to preserve the money you have, or are you a more aggressive investor willing to pursue potentially higher-return, higher-risk investments?
- **Time horizon** – how many years do you have to achieve your financial goals? If you have many years until retirement, even if you consider yourself risk-averse, you may want to consider being more aggressive in your allocation, depending on your financial needs and goals.
- **Tax situation** – are you in a high-tax situation, low-tax situation, or somewhere in the middle?
- **Time and skill to manage your portfolio** – do you have the knowledge, access and time to manage your funds, or are you better served by employing professionals to handle your asset allocation for you?

Your answers to each of the questions above will help you determine the asset allocation specific to your needs. You should also know the advantages and disadvantages of each of the primary asset classes to help you determine your proper asset allocation.

Check out www.ctainvest.org for Webinars and calculators that can help you determine your risk tolerance and different asset allocations that might be best for you.

* Source: "Determinants of Portfolio Performance II: An Update," Brinson, Singer and Beebower.

Asset Class Features

Stocks

Stocks are also called equities because they represent ownership (equity) in a particular company. In exchange for their ownership, stockholders receive the opportunity to participate in a company's gains, as well as its risks. Investors typically invest in stocks to provide a potentially higher investment return than other asset classes. These returns may also include income provided by companies that regularly pay dividends – a portion of earnings returned to shareholders, typically in the form of cash or company shares.

Advantages: Stocks have historically provided the greatest long-term investment returns of the three primary asset classes. From 1926 to 2008, large-company stocks (as measured by the Standard & Poor's 500 Index) posted an average annual return of 9.6%.* More recently, large-company stocks returned an average annual return of 11.0% (1979 through 2008).*

Since 1926, the stock market has posted positive annual returns in 59 years and has registered more than twice as many up years as down years. Additionally, investors have enjoyed double-digit returns in 46 out of these 59 years and returns higher than 20% in 31 years since 1926. (Past performance is not an indication of future results.)

Disadvantages: Stocks are the most volatile of the three asset classes – that is, they are more prone to extreme ups and downs. It's important to remember that some years will have above-average returns and some years will have below-average returns. A classic example of volatility can be found in the early years of the Great Depression. Between 1926 and 2008, the stock market experienced its worst year in 1931, declining 43.3%; two years later, in 1933, it had its best year, increasing 54.0%.* Because stock returns are never guaranteed, shareholders have the potential to lose some or even all of their investment.

In 2008, more than half the days between September and the end of the year resulted in a change of greater than 1% up or down. And there were several days in October 2008 when the market moved 10% or more in a single day. Investors who have only a few years until they need to tap their money, or those

who have low risk tolerance, may need to consider allocating a small portion of their 403(b) or 457 plan contributions to stocks. Generally speaking, the closer you get to the retirement, the less risk you want to take. Otherwise, like many retirees in 2008, you will be faced with having to take money out of your investments at a time when their prices are low.

Bonds

Bonds are known as "fixed-income" securities because the amount of income they generate each year is usually "fixed," or set, when the bond is issued, although that is not always the case. In general, bonds make payments to the bondholder on fixed contract terms that are stated in advance of issuance.

Bonds are essentially loans to issuers. They may be issued by governments, states, municipalities, agencies, institutions or corporations. Investors typically invest in bonds to provide interest income and help smooth the volatility of their total portfolio, because bonds usually move up and down at different times than stocks, and the price movement is generally (but not always) less extreme than with stocks. When investing in bonds, it is important to know that, all things being equal, bond prices and interest rates move in opposite directions. When interest rates rise, bond prices usually fall; when interest rates fall, bond prices rise (there are exceptions, such as with Treasury Inflation-Protected Securities (TIPS)). If you hold an individual bond, this usually doesn't matter unless you sell it before maturity. But if you hold bonds in a bond fund, as most retirement investors do, the bond manager will buy and sell bonds within the fund and that will have an impact on your return.

Advantages: Bonds typically deliver a higher return than cash investments and are generally less risky than stocks. From 1926 to 2008, long-term corporate bonds delivered an average annual return of 5.9%, and long-term government bonds returned an average of 5.7%.* During this same period, the best year for long-term government bonds occurred in 1982, when they returned 40.4%; the worst year came in 1967, when bonds fell 9.2%.*

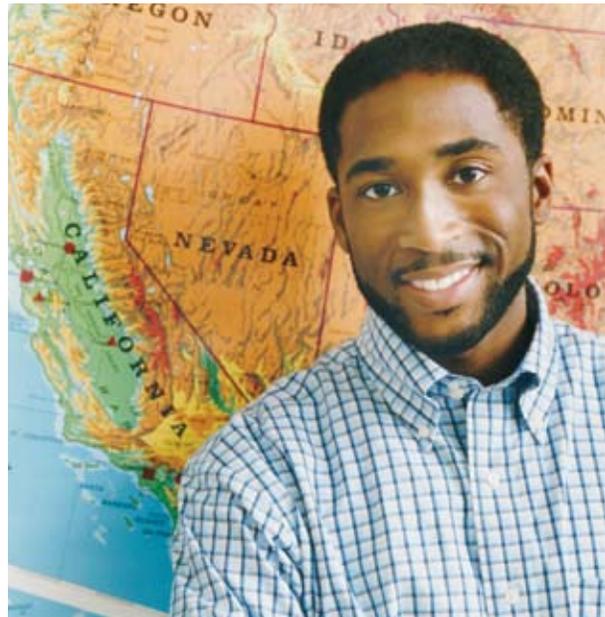
Disadvantages: Bonds are issued with a fixed period of time to maturity, and selling bonds before

they mature may result in a loss. Additionally, if the issuer of the bond declares bankruptcy, investors may lose money, since the bonds they hold may not be fully repaid. To help bond buyers assess the potential risk that a bond issuer is unable to make (defaults on) payments, ratings agencies such as Standard & Poor's (S&P) and Moody's assess the financial strength of bond issuers. S&P rates bonds from AAA (highest) to D (lowest). Moody's rates bonds from Aaa (highest) to C (lowest). The lower a bond's rating, the higher the likelihood that its issuer will default. To compensate for the risk that an investor takes when purchasing a lower-rated bond, the bond will pay a higher interest rate. The other disadvantage of bonds is that, if a company grows quickly and becomes very profitable, bondholders don't benefit, whereas stockholders may receive dividends or be able to sell their stocks at a gain.

Cash Equivalents

Cash equivalents include interest-bearing savings accounts, money market funds and U.S. Treasury bills. What these investments have in common is that they can be readily converted into cash – hence their name.

Advantages: Cash equivalents are good for meeting short-term financial goals (six months or less). They can also provide peace of mind to investors who are concerned about the potential volatility of their stock and bond investments, since cash equivalents are designed to provide price stability and protect your principal while providing a modest return. Because of these attributes, cash equivalents may provide an appropriate short-term “parking place” for some of your assets until you decide what you wish to do with them longer-term.



Disadvantages: For long-term investment goals, such as retirement, the return of cash equivalents is likely too low to meet your needs. Between 1926 and 2006, a hypothetical portfolio of 100% U.S. Treasury bills would have significantly underperformed an alternative all-stock or all-bond portfolio, returning an annualized average of 3.7%.*

To Learn More

Visit www.ctainvest.org and use the historical returns calculator to determine how different hypothetical asset allocations would have performed historically. But remember, past performance cannot predict future returns.

* Source: 2009 Ibbotson® Stocks, Bonds, Bills, and Inflation® (S&P®) Classic Yearbook. Past performance is not an indication of future results.

Visit www.ctainvest.org and use the historical returns calculator to determine how different hypothetical asset allocations would have performed historically.

403(b) and 457 Plan Investment Options

As a 403(b) and 457 plan investor, it's good for you to know about asset classes as the basis for your investment strategy. However, it may be difficult (if not impossible) for individuals in a 403(b) or 457 plan to invest directly in stocks or bonds. Instead, your 403(b) or 457 plan probably offers a range of mutual funds and annuities. Learning more about these investing options can help you make the most of your 403(b) or 457 plan.

About Mutual Funds

A mutual fund is a collection of stocks and/or bonds and/or money market instruments that have been purchased by a professional mutual fund manager with money pooled from individual investors. Mutual funds provide individual investors with enormous buying power – the chance to directly invest in a wide variety of investment types.

That sort of investment accessibility explains why mutual funds have become enormously popular with investors. Currently, there is more than \$9.5 trillion invested in mutual funds in the United States – that's approximately the annual gross domestic product of China and France combined! Compared with individual stocks, mutual funds are easier to buy and typically require a much lower dollar threshold for purchase.

Mutual funds offer the advantage of:

- Diversification at lower asset levels (it would require a significant amount of money to develop a well-diversified portfolio with individual stocks and bonds).
- Professional investment management.
- Pooling of transaction costs to achieve lower average trading costs.

When purchasing a mutual fund, you're in essence buying the financial decision-making of the professional money manager (or managers) who run that particular mutual fund. If you're like most investors, you probably lack the time, knowledge or resources to sort through dozens if not hundreds of potential investment selections. Instead, with a mutual fund, you're ceding that decision-making authority to a professional who handles these tasks every day.

Diversification

Stock-holding mutual funds potentially provide enormous diversification, because a mutual fund

includes stocks from several different companies. While this may limit the upside potential of a mutual fund (as opposed to owning a single high-performing stock), it also helps protect investors from the poor performance of any individual stocks.

For example, let's say you owned shares in the XYZ Stock Fund, which includes holdings in the fictional companies Acme Industries, Beta Beverages and Core Commodities. For the prior year, Acme delivers a return of 25%, Beta returns 0% and Core provides a return of negative 10%. Assuming that the XYZ Fund has had the same amount invested in each company, and no other investments, it would have returned 3.3% to investors for the year, based on the returns of these three companies.

Now, if you had invested all of your funds in Acme stock instead of the XYZ Fund, you would have earned 25% for that year. However, if instead you had invested all of your funds in Beta stock, you would have earned nothing; if you had selected Core stock, you would have suffered a 10% loss.

It's important to note, however, that diversification cannot guarantee a profit or protect against loss.

Trading Your Funds

When it comes time to sell or make investment changes, mutual funds are typically very liquid (easily sold), meaning you can quickly make changes. With just a phone call or online transfer, you can sell some or all of your mutual fund holdings in your 403(b) or 457, transfer assets from one fund to another, or change the way your contribution dollars are invested. (But be aware that your 403(b) or 457 plan has specific rules about transfers – see page 39.) Best of all, the 403(b) or 457 plan provider records all of these transactions on your behalf and provides you with periodic statements and reports, reducing the amount of recordkeeping and paperwork that you would need to perform yourself.

On the downside, mutual funds provide investors with no control over specific investment decisions – that is, buying or selling individual securities. Unlike picking your own individual stocks, having a mutual fund means letting someone else pick your investments for you.

Types of Mutual Funds



As discussed earlier, individual factors such as your age, investment goals, risk tolerance and tax situation will indicate your optimal investment choices. That's why mutual fund companies offer such a wide variety of choices to investors – to accommodate individual preferences and financial goals.

Once you've identified your financial goals, you'll want to determine which fund types may be best for you. There are literally dozens of types of funds available, but in general, the fund(s) you choose will likely come from one (or more) of the following types. Remember, however, that there are funds that combine some of these investments and/or investment styles. Read more about the funds you are choosing in the prospectus offered by the mutual fund.

Money Market Funds

Money market funds invest in high-quality, short-term debt instruments (typically issued by the federal government and corporations) that are generally considered to be conservative investments. They are typically considered to be the safest of all mutual fund investments because they provide a high stability of the principal amount invested. Money market funds typically keep a constant share price (usually \$1, but this is not guaranteed) but offer a variable yield (return on investment) based on how they're invested. They are most appropriate for short-term financial goals (six months or less), as a haven for emergency funds (three to six months of living expenses) or as a "parking place" for assets you intend to invest elsewhere.

Bond Funds

Bond funds (also known as fixed income funds) invest in corporate and government bonds in order to provide shareholders with a fixed rate of income. They typically have more risk than a money market fund, but less risk than a stock fund. There are many different types of bond funds available; the most popular include:

- **Municipal bond funds**, which invest in bonds issued by state and local governments. "Munis," as these bonds are called, are typically exempt from federal taxes, and may also be exempt from state and local taxes. (Note that holding municipal bond funds within your tax-deferred 403(b) or 457 plan account does not result in any additional tax benefits.)

- **Corporate bond funds** include bonds issued by corporations. Funds that invest in riskier bonds (those at higher risk of default) generally have to pay a higher rate of return than other bonds in order to attract investors.
- **U.S. government bond funds** invest in debt instruments issued by the federal government. They are exempt from state and local income taxes. Again, you receive no additional tax advantages by holding a tax-exempt investment in your 403(b) or 457 plan.
- **Core bond funds** may hold a mix of long-and short-term government (Treasuries/agencies) and investment grade corporate securities. They may also hold highly rated residential mortgage-backed, commercial mortgage-backed and asset-backed (like credit cards and car loans) securities.
- **International bond funds**, which may invest in bonds issued by a single country or region, a number of different foreign countries or a mix of foreign and domestic (U.S.) bonds.

Stock Funds

Stock funds invest in the stock of companies. They are typically riskier than money market and bond funds, but also provide a potentially higher rate of return than other types of funds. There are many different types of stock funds available. They can be categorized as follows: strategic stock funds; size-based stock funds; and international-based stock funds.

Strategic Stock Funds

- **Aggressive growth funds** aim to maximize capital gains (appreciation) by investing in companies with potential for rapid growth. Aggressive growth funds are typically the most volatile of all fund types.
- **Asset allocation funds** typically invest in a mix of stocks, bonds and other investments, such as money market investments. The purpose of these types of funds is to provide you with the same type of diversification you would create by holding your own portfolio of different asset classes, but in an all-in-one investment.
- **Balanced funds** generally invest in a mix of stocks and bonds. Like asset allocation funds, they are designed to provide diversification among the

asset classes in a single investment. Note that the definition of asset allocation and balanced funds will differ somewhat among different fund providers.

- **Blended funds** hold a combination of growth stocks (see growth funds, below) and value stocks (see value funds, below).
- **Growth funds** are similar to aggressive growth funds in their goal for capital appreciation, but in general, do not invest in stocks which are as small and/or as speculative as those held by aggressive growth funds.
- **Growth and income funds** typically hold “blue-chip” stocks – those issued by larger, well-established companies that pay dividends, thereby providing shareholders with the potential for income as well as limited growth. These funds often invest in larger companies that pay dividends, including utilities and companies that are found in the Dow Jones Industrial Average. Growth and income funds are generally less volatile than growth funds and more volatile than income funds.
- **Income funds** focus on providing shareholders with dividend income by investing exclusively in large, dividend-paying stocks. Any capital appreciation in these funds is an additional benefit. These funds are particularly favored by conservative investors seeking income.
- **Target-date funds** are a relatively new fund type. Like balanced funds, they invest in a mix of assets. Unlike balanced funds, however, they adjust their allocations based on the projected year of retirement. For example, a “2040 fund” may start out with an equity-oriented portfolio of large and small domestic stocks, international stocks and some bonds. It may gradually transition to a more conservative portfolio with fewer stocks and more bonds and cash equivalents as the target date nears.
- **Lifecycle funds** are usually risk-based (aggressive, moderate, conservative), but some lifecycle funds combine a time horizon plus risk level.
- **Value funds** are invested in the stocks of companies believed to be undervalued in the current market compared to their peers, as well as those that are likely

to pay dividends. Value fund managers seek to identify companies that they believe are underpriced in the hope that these stocks will gain once the market realizes the true value of these stocks. By purchasing stocks with lower prices, it is possible to have a higher dividend yield and greater potential for appreciation later on.

Size-Based Stock Funds

Although not strictly style-based, size-based stock funds typically also have a strategic and/or international component. For example, you might see a small-cap growth fund or a large-cap global fund.

- **Large-cap funds** generally invest exclusively in companies with a market capitalization (market value of outstanding stock) of \$8 billion or greater. They are generally more conservative and less volatile than small-cap funds.
- **Mid-cap funds** typically invest exclusively in companies with a market capitalization (market value of outstanding stock) of \$1 billion to \$8 billion. They are usually more conservative and less volatile than small-cap funds.
- **Small-cap funds** invest exclusively in companies with a market capitalization (market value of outstanding stock) of \$1 billion or less. Small-cap funds are generally less conservative and more volatile than large and mid-cap funds.
- **Micro-cap funds** usually invest exclusively in companies with a market capitalization (market value of outstanding stock) of \$250 million or less. These are companies that are start-ups, takeover candidates and/or poised to exploit new markets. Micro-cap funds are generally more volatile than all other size-based fund types.

International Funds

International funds primarily hold securities from foreign countries. They may be an appropriate selection for investors interested in diversifying their portfolio internationally. The primary types of international funds are as follows:

- **Country-specific funds** invest only in companies located within a specific foreign country and are designated as such: for example, a Japan Fund or a Brazil Fund.

- **Emerging market funds** may invest within a single country or a larger region, but typically only invest in countries and/or regions considered to be emerging economically. For example, India may be considered to be an emerging market.
- **Foreign funds** invest exclusively in companies based in foreign countries. They may be invested in companies within a certain region of the world (an “Asia fund”) or invested in any non-U.S.-based company.
- **Global funds** invest in companies around the entire world, including those which are based in the United States.

About Index Funds

Index funds are mutual funds that seek to duplicate the performance of a particular benchmark index (see page 23). The fund may hold all of the same securities that are in the index, in the same proportion, or it may include a statistical sampling of the securities in the index. These funds are passively managed – that is, securities are bought and sold only in response to changes in the index. With actively managed funds, the fund manager buys and sells securities in an attempt to outperform the market rather than match a particular index.

Most of the types of funds we’ve discussed are available in both actively and passively managed forms. For example, there are large-cap index funds that seek to track the performance of a corresponding

large-cap index, and there are large-cap funds that are actively managed and thus seek to outperform the index by buying and selling large-cap companies based on research and analysis.

Other Investment Vehicles

These are investments which are not as readily categorized as the funds listed above and/or are intended for special investment situations.

- **Stable value investments.** These types of investments are considered lower risk than stocks, and are generally high-quality, low-maturity bond funds that offer a steady investment value through the use of an insurance contract. Stable value funds typically stress preservation of capital and provide a steady stream of income.
- **Real estate investment trust (REIT) funds** invest in commercial retail property, such as shopping malls, hotels, office buildings and apartment complexes. They enable shareholders to invest indirectly in real estate. Because they are invested in real property, and not stocks, REIT funds may move in a different direction than the stock market.
- **Precious metal funds,** as their name implies, invest in gold, silver, platinum, palladium and other precious metals. Precious metal prices often move in the opposite direction of the stock market, and thus these funds can provide a hedge against investments in common stocks and stock funds.

check out the “Understanding Mutual Funds”
Webinar at ctainvest.org.

Mutual Funds – The ABCs of Fees and Share Classes

Mutual funds are generally categorized into those which assess a sales charge on the purchase or sale of shares, which are called “load” funds, and those which do not assess a sales charge, which are called “no-load” funds. Additionally, all mutual funds have expenses that they pass along to shareholders, including investment advisory fees, shareholder transaction expenses and marketing and distribution costs. It’s important to know about these fees before purchasing mutual fund shares. You will find information on mutual fund fees and expenses in a fund’s prospectus, a legal document that prospective shareholders must receive before purchase.

The fees assessed on mutual fund shareholders will consist of at least some or potentially all of the following:

- **Management fee** – Paid out of the fund’s assets (and thus indirectly paid by shareholders), these are fees paid to the fund’s investment advisor for portfolio management (including security selection), miscellaneous management fees and administrative expenses. All funds assess a management fee, which can vary widely in amount between fund families and types of funds.
- **Account fee** – Some funds also assess an account fee, charged for the maintenance of the account. For example, some funds assess an account fee on accounts that are below a certain dollar amount.
- **Purchase fee** – Some funds assess a fee for the purchase of shares. Unlike a front-end sales load (described below), which is paid to a broker (a regulated professional who buys and sells shares), a purchase fee is assessed by the mutual fund company to defray up-front purchase costs.
- **Redemption fee** – Some funds assess a fee for the sale of shares. Unlike a back-end sales load (described below), which is paid to a broker, a redemption fee is assessed by the mutual fund company to cover the costs of share redemption. Some fund companies assess a redemption fee only on shares held less than a certain time period (for example, 90 days or less) to discourage shareholders from quickly selling their shares after purchase.
- **Exchange fee** – Some funds assess an exchange fee in order to cover their costs when shareholders exchange (shift) funds from one fund to another within the same fund family.
- **Distribution and/or service (12b-1) fees** – 12b-1 fees, which get their name from the SEC rule that authorizes a fund to charge them, cover distribution expenses and sometimes shareholder service expenses. Distribution fees include fees paid for marketing and selling fund shares, such as compensating brokers and others who sell fund shares, and paying for advertising, the printing and mailing of prospectuses to new investors, and the printing and mailing of sales literature. Some funds also authorize and include 12b-1 shareholder service fees, which are paid to cover the cost of responding to investor inquiries and providing investors with information about their investments.
- **Other expenses** – these include expenses not included under “management fees” or “distribution and/or service (12b-1) fees,” such as shareholder service expenses not already included in 12b-1 fees, custodial expenses, legal and accounting expenses, transfer agent expenses and other administrative expenses.

About Mutual Fund Share Classes

Load mutual funds (those with a sales charge paid to a broker) are available in what are called share “classes.” Each class of a single mutual fund will have the same portfolio manager, investment goals and portfolio. The difference between share classes is that the mutual fund company will charge you different fees and expenses depending on which type of share class you own.

A single mutual fund may have many (six or more) classes of mutual fund shares. There are many different share classes, but A, B and C are among the most common. Note that, when investing in your 403(b) or 457 plan, you do not generally get to choose which share class to buy. However, it is important to be aware of the share class that is being offered in the fund you are choosing, because it will have an impact on your fees.

Share classes do not have consistent definitions across providers, and some providers lack them or attach different terms to them. Following are typical definitions of A, B and C share classes. However, these definitions are provided for illustration only. You should carefully read the terms and conditions for each fund, and confirm with your plan what the relevant fees and restrictions are before making a purchase.

Class A Shares

Class A shares may or may not assess a sales charge when you buy the shares. Front-end loads are not common in 403(b) plans; however, if you buy Class A shares with a front-end sales charge, a portion of your investment goes to pay this sales fee, and is not invested. For example, suppose you decide to spend \$1,000 on Class A shares with a front-end sales load of 5%. You will be charged \$50 on your purchase, and the remaining \$950 will be invested.

You may be eligible for what's called a breakpoint discount on a front-end sales charge if you make a large purchase of fund shares, already hold other mutual funds offered by the same fund family or commit to regularly purchasing the mutual fund's shares.

Class A shares typically have lower 12b-1 fees than other share classes, making them more attractive if you hold them for a longer time. In general, Class A shares are most attractive if you plan to invest a large sum and intend to hold these shares for a long time.

Class B Shares

If you buy Class B shares, you will not pay a sales charge up-front, but you will pay a back-end sales charge when you sell your shares. This back-end load, called a contingent deferred sales charge (CDSC), will usually decline over a certain time period (usually six to eight years). At the end of this time period, no charge applies, and your shares typically convert to Class A shares.

Unlike with Class A shares, Class B shares are not eligible for breakpoint discounts. In addition, the 12b-1 fees on Class B shares are typically much higher than with Class A shares. As a result, Class B shares may be most appropriate if you plan to invest a smaller amount of money for a long period of time.

Class C Shares

Class C shares do not impose a front-end sales charge on the purchase, so the full dollar amount that

you pay is invested, and the CDSC is typically smaller than with Class B shares. As with Class B shares, the 12b-1 fees on Class C shares are higher than with Class A shares. Unlike with Class B shares however, Class C shares do not convert to Class A shares after a certain period of time, meaning your expenses in Class C shares will not decrease while they are held.

As a result, Class C shares may be more appropriate for investors who have a large amount to invest for a short period of time (five years or less).

Deciding on Share Class

If you are investing in an account outside your 403(b) or 457 plan, you generally will need to determine which share class is most appropriate, based on how long you plan to hold the shares and the expense ratio (total expenses) of each of the share classes. That's important because the share class with the lowest expense ratio will have the highest return of all the share classes (since fund expenses are deducted as a percentage from share assets). Class A shares typically have the lowest annual expense ratio, and Class C shares have the highest. Class B shares, which usually convert to Class A shares after a period of time, will eventually have a lower expense ratio. Class C shares never reduce their expense ratio.

Inside your 403(b) or 457 plan, you may not have a choice, but it's important to understand what you are purchasing. In some cases, the vendor may offer the same fund with different share classes.

In general, if you are planning to hold your shares for 10 or more years, you may want to consider Class A shares. If you believe you will hold your shares for 5 years or less, Class C shares may be more appropriate; between 6 and 10 years, Class B shares may be appropriate. You should consult with your financial advisor before deciding.

What Do Indexes Measure?

Market indexes (or benchmarks) are useful tools for comparing an investment's returns with overall market trends. It's important to know what the appropriate index for your investment is. Indexes can be used to benchmark actively managed funds as well as passively managed funds – called index funds – which are designed to track the performance of a particular index. There are hundreds of indexes, all of which use different methodologies for construction and calculation returns. The following are a few popular indexes, each measuring a different segment of the market.

Dow Jones Industrial Average	This is the oldest and most well-known stock market index, made up of 30 actively traded blue-chip stocks. The Dow tends to be used as an indicator of market trends, rather than as an index against which to measure performance.
Standard & Poor's 500-Stock Index (S&P 500)	This index measures the performance of 500 widely held common stocks of large-cap U.S. companies. This may be a good index to use if you invest in a large-capitalization equity mutual fund.
Russell 2000 Index	This index tracks the smallest 2,000 companies out of the top 3,000 in domestic equity capitalization. It represents a cross-section of the U.S. small-cap equities market and may be a good index to use if you invest in a small-capitalization fund. <i>Note that this is a sub-index of the Russell 3000 Index, which measures a broader market. There is also a Russell 1000 Index, which is the large cap sub-index of the Russell 3000.</i>
Standard & Poor's 400-Stock Index (S&P 400)	This index follows 400 common stocks of industry, transportation, financial and public utility companies in the mid-range of capitalization. This may be a useful index if you invest in "defensive" funds (funds that tend not to fluctuate as much with the economy) such as utility funds.
Nasdaq Composite	The Nasdaq Composite Index is the "tech stock" index. It tracks stocks traded over-the-counter. It is a broad-based index including more than 3,000 companies, many of which are in the high-tech industry. This may be a good index to use if you invest in growth or technology funds.
Barclays Capital Aggregate Bond Index	This index measures the performance of government and corporate bonds and mortgage-backed securities. Consider this index if you invest in a diversified bond fund.
Barclays Capital U.S. Corporate High-Yield Index	This index tracks domestic non-investment grade ("junk"), fixed-rate corporate bonds, and may be useful if you invest in riskier bond funds.
MSCI (formerly known as Morgan Stanley Capital International) EAFE	This index tracks stocks traded on the largest developed international markets (Europe, Australia and Far East). It may be suitable if you invest in established foreign market funds.
MSCI ACWI (All Country World) ex-US Index	This index provides a broad-based measure of stock performance in both developed and emerging markets throughout the world, with the exception of U.S. companies.

In your mutual fund prospectus, you may find information about a suitable index against which to measure your fund. But it is also important to note that your returns will not be exactly the same as the index. That's because indexes aren't managed, as a mutual fund is. They measure performance during a specified period, which may not match the period during which you hold the investment. And finally, there are no fees deducted from indexes, as there are from your mutual fund and annuity investments.

An individual investor cannot invest in an index. But you can invest in an index fund that is designed to track the performance of a specific index. (See page 20).

About Annuities – Fixed and Variable

Annuities are another investment vehicle available in your 403(b) or 457 plan. Annuities are investment contracts with a life insurance company ultimately designed to provide a steady stream of income. Your investment grows tax-deferred until withdrawal. However, investing in a tax-deferred annuity within your tax-deferred 403(b) or 457 plan offers no additional tax advantages, so you will likely end up paying fees for a feature that doesn't benefit you (see page 26 for more on fees).

There are two basic types of annuities:

- **Fixed annuities** have a fixed rate of return and generally are available through your 403(b) or 457 plan as either a traditional fixed or equity-indexed annuity.
- **Variable annuities** are similar to mutual funds paired with an insurance component. As the name implies, the return varies with the market.

Whether you hold a fixed or variable annuity, there are two basic phases to an annuity contract: the accumulation (pay-in) stage and the distribution (pay-out) stage. During the accumulation stage, you put money into the annuity, either all at once or gradually over time, where it grows tax-deferred. During the distribution stage, which can start as early as age 59½ (earlier in a 457 plan, if desired, or as early as age 55 with a 403(b), if leaving your job), you can begin taking income from your annuity or convert your annuity to a plan that provides a guaranteed income stream over a specified amount of time (for a set number of years, or for life).

About Fixed Annuities

With a traditional fixed annuity, the insurance company guarantees you will earn a minimum rate of return during its accumulation period – the time your account is growing.

The insurance company also guarantees that your periodic payments will be for a guaranteed amount for each dollar in your account. These periodic payments may last for a fixed period, such as 20 years, or for an indefinite period, such as your lifetime or for the lifetime of you and your spouse.

With a fixed annuity, if you die during the accumulation stage (while you are making contributions), your beneficiaries will receive the total of all the contributions you've made or the account value at the time of death, whichever is greater. The cost is generally figured into the rate of return rather than as a separate fee.

Another type of fixed annuity, called an equity-indexed annuity, operates somewhat like a variable annuity. When you own an equity-indexed annuity, the issuer agrees to pay you a fixed rate of return based on a percentage (often 75%) of a stock market index (such as the S&P 500). The issuer also agrees to pay at least a minimum return, in case the stock market index falls short of the guaranteed minimum. Thus, you have potential to receive some (but not all) of the upside of return in a stock market index, and are protected on the downside. To provide these benefits, equity-indexed annuities typically charge higher fees than other types of fixed annuities.

When shopping for a fixed annuity, compare the rate of return, the surrender charge (the fee imposed for terminating an annuity contract prior to maturity), the sales charge and annual maintenance fees and charges. Avoid fixed annuities that charge front-end contract fees and sales loads, or excessive annual maintenance fees or charges. They reduce the amount of money that goes to work for you. Also, consider the length of the surrender charge period (in addition to the surrender amount); a surrender charge period of five years or more may be overly long.

About Variable Annuities

A variable annuity is similar to a fixed annuity in the sense that it's a contract between you and an insurance company, in which the insurance company agrees to make payments to you (in exchange for your investment) either immediately or at some future date. You can purchase a variable annuity either by investing a lump sum or by making periodic payments over time.

With variable annuities, your contributions (“premiums”) are allocated to subaccounts held by the insurance company. These subaccounts are invested in underlying portfolios that may be composed of stocks, bonds, money market funds or a combination. A variable annuity offers a death benefit (based on the amount that you’ve paid in, or a guaranteed minimum), and provides the opportunity to receive periodic payments for the rest of your life (or for the lifetime of any other beneficiary you designate).

The death benefit of a variable annuity may also sound appealing, but keep in mind it typically consists of simply returning money that you’ve already paid into the annuity. You will pay an additional fee, called a mortality and expense fee (typically a percentage of the assets you’ve invested) in order to receive this death benefit. In reality, these fees become more expensive as their benefit becomes more remote. If

you are earning positive returns over time, you are less likely to have your account balance be close to or less than the amount you originally invested. Since the fee is asset-based, you end up paying more for the protection as the protection’s value relative to your balance declines. You may wish to consider the cost and return potential of an annuity’s death benefit versus the cost and return potential of investing directly in mutual funds and purchasing low-cost term life insurance.

You should also closely examine a variable annuity’s overall sales charges and fees. Some variable annuities have fees that are up to eight times more expensive than comparable mutual funds. Additionally, surrender charges on a variable annuity may last for up to 10 years.

If you are considering an annuity for your 403(b) plan, be sure to check out the fees at 403bcompare.com.



Final Analysis of Annuities

As noted, annuities are able to grow tax-deferred. Your 403(b) or 457 plan also grows tax-deferred. When weighing retirement plan options, does it make sense to pay for an annuity sales charge to receive a double-dose of tax deferral?

Generally speaking, annuities make the most sense only after you have contributed the maximum amount

(currently, \$16,500 a year) to your 403(b) and/or 457 plan, and to individual retirement accounts (IRAs). Annuities may also be appropriate for high-income investors in a high tax bracket who may benefit from their tax deferral. Consult with your tax advisor for details.

The tax deferral of annuities may sound appealing, but keep in mind that if you hold it within your tax-deferred 403(b) or 457 plan, you'll be paying extra (sales charges and fees for the variable annuity) for a benefit you already have.

What You Need to Know about Fees

There's no escaping fees, whether it's to register your car or spend a day at a state park. Investing in your 403(b) or 457 plan is no exception. Someone needs to be paid to manage the investments and administer the plan.

Fees are an important consideration when choosing investments for your plan. Although fees may seem small when expressed as a dollar amount or percentage of assets, the reality is that they can have a significant impact on the ultimate balance of your nest egg when they are paid year after year.

When reviewing fees, also consider the level of support you receive from your 403(b) vendor and your personal preference. For example, some 403(b) vendors use a toll-free number to support operations, while other 403(b) vendors rely on individual agents or employees. Those services are reflected in the overall expense of the program and hence the fees.

Typically, a 403(b) or 457 plan has two kinds of expenses: administrative costs and investment management fees. The latter is often expressed as an **expense ratio**, or the amount of the fees as a percentage of your net assets. For example, if you had \$1,000 invested, a fee of 0.2% would cost you \$2 a year, while a fee of 3% would cost you \$30 a year. Review the chart on page 27 to see the impact of various expense ratios.

Investment Options

As you know, your 403(b) or 457 plan typically allows you to purchase two types of investment products: **mutual funds** and **annuities** (including fixed, variable and equity-indexed annuities).^{*} The fees will vary depending on which of these options you choose and also – if you select a variable annuity or mutual funds – on which investment choices you make within those products. In general, annuities offer more features – many of which you don't need – and charge more fees than mutual funds do.

Each of these types of investments charges fees. It's important for you to understand the fees charged, because they will have a significant impact on the amount of money you can accumulate toward your nest egg.

Explicit fees are the ones that are spelled out for you (see the previous section). They may include things

like an upfront sales fee, usually a percentage. Or there may be an annual fee for administering the account or a contingent sales fee, which is a sales fee that is imposed when you sell the investment, instead of when you buy it.

With variable annuities, the explicit fees can be all of the above, plus a mortality and expense (M&E) fee that covers the death benefit. Most annuities also charge a surrender fee if you decide to sell the annuity before a specified period.

You should be able to find out about the explicit fees pretty easily. They should be spelled out at *403bcompare.com*, or in the insurance contract or prospectus. You can ask your 403(b) or 457 plan representative to identify all explicit fees. But watch out for implicit fees!

Implicit Fees

Implicit fees are the ones that aren't spelled out, but will still have an impact on the return on your investment. For example, most mutual funds have turnover (selling investment shares within a fund). If a mutual fund manager sells a stock within a mutual fund, there will be a commission or other sales charge (called the spread) on the transaction, which will be deducted from the balances of everyone who owns shares in the fund.

In general, funds that are not actively managed (such as index funds that seek to track the performance of a particular index of stocks) have lower implicit fees because there is lower turnover in the fund. However, it is important to realize that paying fees for an actively managed fund may be worth it if the fund manager is successful in beating the overall market. If the outperformance of the fund is greater than the transaction costs and management fees, an actively managed fund may be more desirable than an index fund, which will not beat the market by its nature.

It may be difficult to figure out implicit fees, but you can estimate the impact of fees by using the Financial Industry Regulatory Authority (FINRA) mutual fund analyzer at <http://apps.finra.org/fundanalyzer/1/fa.aspx>.

^{*} A 457 plan may also allow you to purchase separate accounts and collective investments trusts. Each plan will offer different investments.

Typical Fees

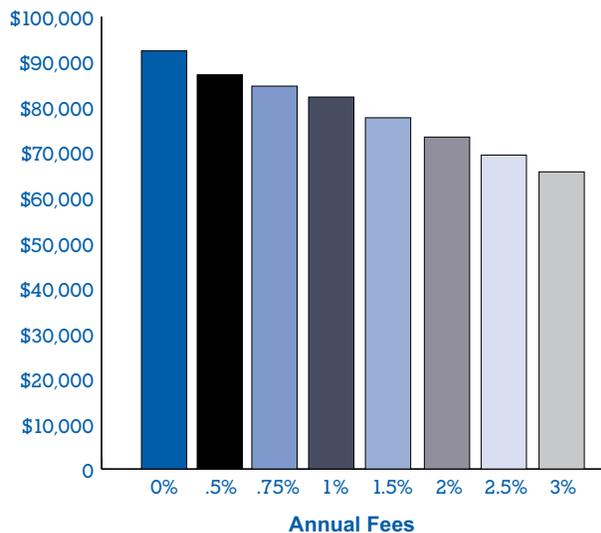
	Variable Annuity	Mutual Fund in a 403(b)7
Operating/administrative expenses	0.15% or flat fee	0.0-1.0%/year
Investment management	0.5-1.0%/year	0.5-1.0%/year
Mortality & expense fee	1.25%	0.0%
Trading costs	Vary	Vary
Surrender fees	6% to 0% after six years	0.0%

Note that the fees you will pay will vary based on the vendor and investment vehicle you choose within your 403(b) or 457 plan.

How Fees Reduce Earnings

The chart on the next page shows how various expense ratios reduce the ending balance of a portfolio. It assumes that you invest \$200 a month for 20 years and earn an annual average return of 6%.*

Value of Investment Averaging 6% Annual Gross Return, Minus Fees



In general, actively managed investments and annuities charge higher fees than passively managed investments, such as index funds. Since fees have such a large impact on your return, it is important to compare both historical performance rates (but keep in mind that past performance is not an indication of future results) and the investment fees. Go to 403bcompare.com to review the explicit fees charged by the investments available in your plan.

* Rate of return is for illustration only and is not meant to represent the return of any specific investment. Account value shows value after 20 years of a \$200 monthly investment earning an average annual rate of 6%, minus the deduction of various annual fees.

What Is 403bcompare.com?

403bcompare.com is a Web site maintained by CalSTRS that lists the approved 403(b) vendors in your district, the products they offer and the fees charged. Here's how to use 403bcompare.com to find fees:

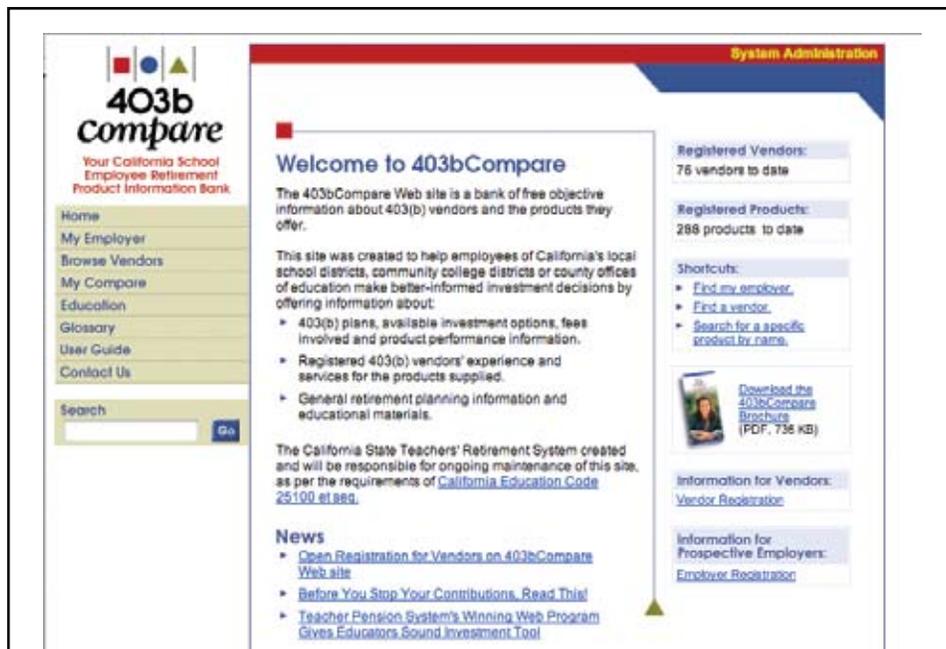
Here's How to Find the Fees at www.403bcompare.com

1. Go to www.403bcompare.com.
2. Click on "Browse Vendors" on the left-hand-side menu. (Note: You can also search for vendors using the search tool, in which case you would skip steps 3 and 4.)
3. Click on the letter corresponding to the vendor's name.
4. A list of vendors will appear. Click on the vendor of your choice.
5. Choose the tab at top that says "Product List."
6. Select the product you are interested in.
7. Choose the tab at top that says "Fees and Charges." You can then review the fees and expenses charged by this investment product.

If you'd like to compare the fees and charges of this investment product to others:

8. Select the "Add to My Compare" link. This will save the information to your "My Compare" box, similar to a shopping cart on a retail Web site.
9. Choose the next product, following steps 1-7 above, and select the "Add to My Compare" link.
10. When you are ready to compare the products, click on the "My Compare" link in the blue bar at the upper right-hand side of the Web page.
11. Your selections will be listed. Check the products that you would like to compare. You can compare only three at one time, and they must be in the same category (for example, you can compare different mutual funds, but you cannot compare a mutual fund with an annuity).

You may also choose to have your information e-mailed to you if you'd like to keep it for future reference. Otherwise, when you leave the site, your My Compare information will be deleted.



The Nitty Gritty: Choosing the Investments in Your Plan

When it comes time to invest your assets in your 403(b) or 457 plan, you'll want to gain answers to several important questions, including: What is my risk tolerance? Where should I invest? Who can I turn to for help? In this section, we highlight the primary factors you'll wish to consider before you invest.

Risk Tolerance

It's important to determine your risk tolerance before you invest. Essentially, risk tolerance is the degree that volatility (changes up and down) in the value of your portfolio affects you. More simply put, if changes in your account value keep you up at night, your risk tolerance is probably low. If you shrug it off as the inevitable ups and downs of investing, your risk tolerance is probably high.

Your risk tolerance is unique to you, and will depend on factors such as your age, amount of assets, income goals and more. Generally speaking, a 30-year-old saving for retirement will have a greater tolerance for investment risk than a 70-year-old seeking retirement income.

It's important to also know that there are different types of risk to consider when investing. Among the many types of risk, these are the most important:

- **Market risk** (or volatility risk) is the chance that a broad investment market, such as the bond or stock market, will decline in value. You should know about this risk if you have assets invested in these markets.
- **Inflation risk** is the chance that the value of your money will decline as rising prices shrink the value of the dollar. This type of risk is relevant if you have funds invested in cash equivalent investments (savings accounts, money market accounts and mutual funds, etc.) that do not keep pace with inflation.
- **Principal risk** is the probability that your original investment will decline in value or be lost entirely. Similar to market risk, this type of risk pertains primarily to investments that stand a greater chance of losing principal, such as stock investments.

- **Credit risk** is the chance that a borrower will default on a debt obligation. This type of risk pertains specifically to fixed income (bond) investments.
- **Liquidity risk** is the chance that you won't be able to sell or convert a security into cash when you need the money. Technically, this risk applies to any type of investment, but is most applicable to thinly traded investments that lack a market. Both credit risk and liquidity risk apply less to mutual funds in a defined contribution plan such as your 403(b) or 457 plan than they do in general investing.

To help you determine your own tolerance for risk, we've prepared a brief risk assessment quiz on page 47. Please take a few minutes to complete and rate your answers. Note that this quiz is intended only to provide an idea of your tolerance for risk, based on emotional responses. For a more in-depth assessment of your risk tolerance, you should consult with a financial professional. You can also use the tools available at www.ctainvest.org.

When determining your risk tolerance, you should also take into account anticipated income (such as your CalSTRS or CalPERS pension benefit) and the amount of income you will need to replace over and above your pension. Once you determine that amount, you should develop an investment strategy designed to help you reach that goal. If you fail to meet your investment goals, you may need to work additional years or accept a lower standard of living in retirement. Use the projected retirement income and projected retirement expenses calculators at www.ctainvest.org to help you with your retirement goals.



Selecting a 403(b) or 457 Plan Vendor

CTA helped secure a California state law that requires the California State Teachers' Retirement System (CalSTRS) to provide 403(b) plan participants with an online information bank of eligible 403(b) program vendors and products, www.403bcompare.com. This site's purpose is to provide eligible employees with "a bank of objective information about various 403(b) vendors and the products they offer." Only vendors that are approved to provide 403(b) plans in California may appear on this site. To learn more about using www.403bcompare.com, go to page 27.

The 403(b) vendors appearing on [403bcompare.com](http://www.403bcompare.com) provide performance and cost information for the products they offer to retirement plan participants, including: (1) the investment's average annual total return for a period of not less than a year (as measured by a rating service selected by CalSTRS); and (2) a fee table showing the total cost in dollars that would be incurred by an investor based on an initial \$10,000 investment (assuming a 5% return for time periods of 1, 5, 10, 15 and 20 years).

Given the dozens of vendors and hundreds of product choices available through www.403bcompare.com, you should know what to look for and what to ask before deciding where and how to invest your retirement plan assets. Specifically, you should research and/or ask about vendor fees and sales charges, product performance information and insurance company ratings (for insurance company vendors). Let's look more closely at each assessment category.

403(b) and 457 Plan Fees

After your asset allocation, fees may have the biggest impact on the return of your 403(b) or 457 plan. Fees cut directly into your rate of return. For a mutual fund held in a retirement plan, these fees can include sales charges and annual expenses which are passed along to shareholders. Mutual fund fees are explained in-depth on page 21.

For an annuity within a 403(b) or 457 plan, fees can include the following:

- **Mortality and expense risk fees:** These are fees that participants pay each year to the insurer to offset the risk of investment loss, plus fees involved to pay annuity provider expenses. "M&E" charges are set as a certain percentage of an account's value – generally an average of 1.25% annually, according to the Securities and Exchange Commission. That's \$250 per year on a \$20,000 account.
- **Administrative fees:** These can be flat fees of, say, \$25 a year, or a percentage of someone's account. Typically that's 0.15% – or \$30 for a \$20,000 account.
- **Initiation fees:** These are one-time start-up fees that may be waived at the time of sale. Prices vary but can run approximately \$60.
- **Sales loads:** These are sales commissions you typically pay up-front (front-end load) when you buy an annuity, and cut directly into the actual amount available to invest. For example, a 7% front-end load on a \$10,000 investment will cost you \$700, meaning you've effectively only invested \$9,300. In 403(b) plans, back-end sales charges are more common.
- **Death benefit charges:** These are used to pay for an annuity's death benefit, a feature that guarantees your heirs will get a certain amount if you die prematurely. This amount is based on the total account value at a certain date in time or, alternatively, the value of the payments you've made minus any withdrawals.
- **Surrender charges:** These may apply if you sell an annuity within a certain period of time, known as the surrender period, which can last up to 15 years after purchase. This charge, also called a contingent deferred sales charge (CDSC), is a percentage of the asset balance at the time you withdraw or transfer and depends on how long you've had your money in place. For example, if you have a seven-year surrender period, and you withdraw money early – say, in the first year – you might pay a 7% surrender charge. The surrender charge typically decreases by 1 percentage point each year until the surrender period finally expires in the seventh year.

To give you an idea of the effect of fees on retirement plan assets, see page 26.

Ask for Fee Disclosure

To evaluate the fees of the investment products you're considering, ask about them. If you're working with an advisor, ask if he or she receives a commission based on the sale of the product, and the amount of this commission. Ask if the advisor will receive any additional compensation (such as a bonus or incentive gift) as a result of selling this particular product. Finally, ask if the advisor will receive a greater sales commission by recommending one particular product over another, and whether or not your needs would be equally served by the lower-priced product.

Performance Information

Fees can dramatically affect an investment's potential performance. When comparing investments, it is also useful to review, compare and contrast prior investment performance information. However, keep in mind that past performance is not an indicator of future returns.

A good way to assess past performance is to compare it versus a comparable benchmark index. This information can be found in a fund's investment prospectus. For example, if you're considering a large-cap growth fund, how does its performance compare with the Standard & Poor's 500 Index? If the fund has come close to matching the index performance, it may be worth considering. On the other hand, if the fund has significantly underperformed the index, you may wish to look elsewhere.

Financial Strength and Stability

If you're considering an insurance company as your 403(b) or 457 plan vendor, you'll want to review and compare its financial strength and stability before purchasing a product. Since these companies are selling insurance products that obligate the insurer to pay a return sometime in the near to distant future, you'll want to be sure that the insurer is in good financial health and able to pay on this obligation.

Various insurance rating companies, including Moody's, A.M, Best and Standard & Poor's, each rate insurers based on their financial health. Each ratings agency has its own particular alphanumeric ratings system, which you can learn more about by consulting

the Web sites of each company. However, the ratings are fairly intuitive. For example, S&P insurer financial strength ratings go from AAA (extremely strong) to CC (extremely weak). Any rating below an "A" should be a source of concern.

Balancing (and Rebalancing) Your Assets: Do It Yourself vs. Target-Date Funds

If you're selecting mutual fund or variable annuity investments for your retirement plan, you will likely be presented with a choice of several different types of funds (large-cap growth, small-cap value, etc.) and the opportunity to assemble a portfolio from these funds that matches your age, risk tolerance and financial goals. You can select these funds yourself to create a balanced portfolio to meet your investment needs. Or, you can turn the reins of investment selection over, so to speak, to the manager charged with running a so-called target-date or lifecycle fund. Let's look more closely at the advantages of each approach – do-it-yourself versus a target-date fund.

When you select funds yourself from an array of options, you are able to exercise greater freedom of choice than possible with a target-date fund. For example, let's say you're presented with multiple fund options, including an attractive stock fund, a top-performing bond fund, and a target-date fund. If you believe that your financial goals would be better served owning the appealing stock and bond funds, these may be better options for your portfolio.

The key to selecting and owning individual funds is to understand the investment strategy and choose funds that suit your goals, timeline and risk tolerance. Be sure that the funds fit in with a fully diversified portfolio that takes into account all of your investments, in and outside the plan.

By contrast, target-date funds, which were also discussed on page 19 of this guide, automatically adjust each year to match your age and presumed investment needs for someone in your age group. Generally, the younger you are, the more aggressively your assets will be invested in a target-date fund. Over time, a target-date fund's manager will reallocate the fund's holdings – from higher-return, higher-volatility

assets classes to those which are lower-return and have lower volatility – based on a predetermined “glide path” that reflects investors’ presumably changing risk tolerance.

For investors, the primary advantage for target-date funds is that their owners no longer have to worry about when and how to adjust their portfolios to account for changes in their risk profile over time. The fund does the work for you. In addition, you don’t need to put together a portfolio of multiple asset classes and monitor them each individually; target-date funds are designed to be an all-in-one solution. That can be a significant advantage to busy working educators when it comes to managing their retirement plans. Young adults, in particular, seem to be particularly interested in purchasing target-date funds.

Keep in mind, however, that target-date funds — like all mutual fund investments — do not insure your 403(b) or 457 plan assets, nor do they guarantee that you will have all the money you need to retire by the target date. For example, let’s say you’re 25 years old in 2010 and want to begin receiving

benefit payments at the age of 60. You would likely invest in a 2045 target-date fund, which would be heavily invested in higher-risk and potentially higher-return investments – specifically aggressive stocks. Although, over the long term, stocks have historically returned an average of close to 10%, there is no guarantee that in 2045 your assets will have increased at a rate of 10% annually.

Between investing in mutual funds yourself versus investing in a target-date fund, there is no right or wrong answer to which type of approach is best. You simply need to pick the approach that’s best for your investment goals and personal approach toward money management. If you have neither the time, interest nor expertise to monitor your investments and rebalance as necessary, a target-date fund may be a good choice for you. This takes some of the emotion out of your investment choice. On the other hand, if you have a risk-return goal that is different from the available target-date funds and are capable of regularly monitoring and rebalancing your 403(b) or 457 plan investments, than a do-it-yourself approach may make more sense.



Changing Your Investments

If you've invested in a variety of mutual funds yourself, you'll want to periodically review them when your account statements arrive in the mail each quarter (or do so more frequently, online) to determine if they still match your investment needs. If not, you'll want to make some investment changes, potentially to how your current assets are invested and/or how your future investments are allocated.

With a 403(b) or 457 plan invested in mutual funds or in funds invested in a variable annuity, changing your investments with your current vendor, if approved by your plan, is typically easy. You simply request (online or by phone) that your plan administrator shift assets from one fund to another and/or reallocate your future asset allocations to your newly selected funds. Because you are making these changes within a tax-deferred account, there is no current tax liability as there might be in a taxable account. (Taxes will be due at ordinary income tax rates upon withdrawal at retirement.)

If you wish to change your 403(b) vendor for your retirement plan you need to check the employer's

plan document to see if you can exchange. You will need to complete a new account form for your new fund company, as well as a fund exchange form. You'll also need to specify which fund(s) at the new company should receive your transferred assets. Once you submit this paperwork, the two respective fund companies (old and new) ought to work together to ensure a smooth transition of your funds. However, be aware that there may be tax implications if you intend to transfer funds to a nonapproved vendor. See page 40 for more information.

If you seek to change your retirement plan assets from one insurance company to another, things potentially become more complicated – and costly. Bear in mind that an annuity is an insurance contract, and as such contains stipulations made by the insurer as to the length of time you're to remain in the contract, and the financial consequences of making changes (or withdrawals) from your account.

Whether or not you're assessed charges when making an investment change in an annuity will depend on



the type of product you initially chose and when you purchased it for your account. For example, if you take money out of a variable annuity within a certain period after a purchase payment (typically within six to eight years, but sometimes as long as 10 or even 15 years), the insurance company will generally assess a surrender charge, which is a type of sales charge that compensates the financial professional who initially sold the variable annuity to you.

Generally, the surrender charge is a percentage of the amount you sell or exchange, and it will decline gradually over a period of several years, known as the

surrender period. For example, a 7% charge might apply in the first year after a purchase payment, 6% in the second year, 5% in the third year, and so on until the eighth year, when the surrender charge no longer applies. Some variable annuity contracts will allow you to withdraw part of your account value each year, such as 10% or 15% of your account value, without paying a surrender charge.

Bottom line, you'll want to be familiar with the rules and potential fees of making investment changes in your retirement account before doing so. In addition, exchanges and transfers have to be permitted as noted in the district's plan documents.

Impact of Surrender FEES

The following shows the impact of surrender fees in various years on a hypothetical annuity balance. The chart assumes the following: a variable annuity of \$10,000 with a surrender charge of 6% the first year, declining by 1% per year until it reaches 0%; the annuity earns an average annual return of 5%;* you are allowed to take out 10% of the balance each year not subject to a surrender fee.

	Balance at End of Year	Surrender Fee	Amount Subject to Surrender Fee	Net Balance after Withdrawal	Total Fee
Year 1	\$10,500	6%	\$9,450	\$9,933	\$567
Year 2	\$11,025	5%	\$9,923	\$10,530	\$495
Year 3	\$11,576	4%	\$10,418	\$11,159	\$417
Year 4	\$12,155	3%	\$10,940	\$11,827	\$328
Year 5	\$13,401	2%	\$12,061	\$13,160	\$241
Year 6	\$14,071	1%	\$12,664	\$13,944	\$127
Year 7	\$14,775	0%	\$0	\$14,775	\$0

* Annual rate of return is for illustration only and does not represent the return of any specific investment.

Working with a Financial Professional

When considering where to invest your 403(b) or 457 plan assets, you should also consider the merits and attributes of the financial professionals representing the 403(b) or 457 plan vendor(s) you're considering. After all, these will be the individuals charged with helping you achieve your financial goals and entrusted with your assets. You'll want to make sure that the financial professional you ultimately select to help manage your assets is knowledgeable, trustworthy and familiar with your retirement plan goals.

What criteria should you use when evaluating a financial professional? Consider asking the following questions to learn about your candidate's attributes.

Q: What are your qualifications?

A: Financial professional should be prepared to discuss their professional training and qualifications, such as whether they've completed training to become a Certified Financial Planner (CFP) or a Chartered Financial Consultant (ChFC). You should look for a professional with proven experience in financial planning for retirement, including on such topics as investments, insurance, tax planning and estate planning. You should also seek someone with specific expertise in 403(b) plans. Also, inquire about how the professional stays current (courses, books, etc.) in his or her field of expertise.

Q: What experience do you have with 403(b) or 457 plans?

A: Find out how long the financial professional has been advising clients on the specific type of retirement plan you wish to purchase and have him or her describe this experience to you. You want someone with experience addressing retirement needs such as yours.

Q: How do you approach financial planning?

A: Learn how the financial planner handles clients and investment goals similar to you and your situation. Some financial professionals want to get an idea of your complete investment picture; others are more interested in addressing your specific financial planning needs. For example, ask how regularly this professional formally meets with clients. Does he or she do so each quarter, twice a year or annually? Is he/she open to regular calls from clients? Will he or

she contact you on a regular basis to inquire about your financial needs? Be sure that the professional's investment philosophy and approach are similar to yours. You literally want to be "on the same page" as the person you ultimately hire to handle your finances.

Q: What type of products and services do you offer?

A: The type of products and services that a professional may offer depend on factors such as the company the individual represents, as well as his/her credentials, licenses and areas of expertise. In general, you want someone more interested in addressing your specific needs, as opposed to trying to sell you a certain product from a specific company.

Q: How much do you charge and how do you charge?

A: Financial professionals are entitled to receive a fee for the services they provide. However, these fees should be fair and comparable to what similar financial professionals charge. The financial professional you're considering should be able to provide you with a general estimate of costs, in writing, before doing any work on your behalf. Many financial professionals provide a complimentary initial visit with prospective clients, as a way to get to know you better, and vice-versa. Financial professionals can be paid in multiple ways:

- **A straight salary** – the professional is paid a salary by the company he/she represents, based on the commission (or fee) you pay on products you purchase from the company.
- **Fees** – based on an hourly rate or a percentage of your assets invested. The advantage of fee-based financial professionals is that they are paid based on a pre-determined rate, not based on the type or amount of product(s) sold, as with a commissions-based financial professional. Keep in mind that professionals who are paid based on a percent of your assets have a vested interest in increasing your assets, since the more your account increases in value, the more income they ultimately receive. It's important to note that they will be compensated more as your account balance grows due to your deferrals and returns, even if they don't provide more work or advice. Those paid a flat fee generally have no conflict of interest.

- **Commissions** – paid by a third-party provider of financial products, based on sales made of the provider’s products.
- **A combination of fees and commissions** – for example, fees may be assessed to complete a financial plan, and commissions are paid based on products recommended and sold to you.

The type of fee arrangement that’s best for you will depend on your individual circumstances and interests. For example, if you’re a savvy investor who had already done considerable research on your available investment options and you know what you want (you simply need someone to execute the transaction for you), you may not want to pay extra for consulting services from a financial professional.

Make sure that the financial professional you’re considering specifies his/her compensation arrangement with you in writing. You may also wish to ask if the professional’s compensation structure is negotiable. For example, if you’re trying to decide between two comparable financial professionals, you might ask the one you prefer if he or she is willing to reduce his/her fees in exchange for your business.

Q: Will I be working exclusively with you?

A: Some financial professionals work alone; others have assistants to help with their work. You should know up-front how your finances will be handled and by whom. If others will be assisting with the handling of your account, you should meet them also, get their names, and assess their qualifications independent of your assessment of the financial professional you’re considering.

Q: Who else, besides me, may benefit from your recommendations?

A: If other parties, such as individuals or companies, stand to gain from the recommendations made by your financial professional, you deserve to know this information. Your financial professional should always place your financial interests first. If he/she recommends products and/or services from others, these recommendations should be made because they are in your best interests, not based on the interests of the financial professional and/or the other parties recommended.

In addition to asking these questions, you may also wish to check with federal and/or state agencies charged with licensing the financial professional you’re considering. The Financial Industry Regulatory Authority (FINRA) maintains a free national database of firms and brokers licensed to sell securities, called FINRA BrokerCheck, and has information on any disciplinary action taken against specific firms and/or individuals. Go to brokercheck.finra.org to learn more.

To check on insurance licensing in California, go to the Web site of the California Department of Insurance at www.insurance.ca.gov/license-status/. The site allows you to search by individual name and contains information on each individual’s continuing education and certification status.

Once you have decided on a financial professional, be sure to keep copies of all documents and correspondence provided by this individual. You should start an online and/or paper-based file to keep track of these records. Not only will this help you keep better track of your financial professional’s performance, but it will also serve as a “paper trail” in case any questions, concerns or issues arise during the course of your business with this professional.

caution about product sales

The majority of financial professionals who sell products and provide services related to 403(b) or 457 plans are ethical, trustworthy and deserving of your business consideration. However, as with any profession, there are some individuals who do not reflect well on their profession. Typically, these are sales representatives more interested in making a “quick buck” than in serving your specific financial needs and interests.

How do you recognize such self-serving individuals? For starters, beware of any financial professionals who begin their conversation with you by trying to sell you specific products and/or bragging about the returns of the products they represent, before they have taken the time to get to know you and your financial needs. More than likely, these individuals are more interested in collecting a sales commission than in establishing a long-term relationship with you.

Be cautious also of any financial professional who does not fully disclose answers to any of the financial professional screening questions posed above. In particular, pay attention to the professional's answers to questions on compensation and potential conflicts of interest. You want someone who is working primarily on your behalf, not someone more interested in representing the interests of themselves or others.

Also be careful not to rely too heavily on a referral or recommendation from a friend or colleague. Referrals and recommendations are useful as a starting point when considering who to hire to manage your money. But know also that less-than-scrupulous financial

professionals often seek to ingratiate themselves with those in positions of power, stature or authority, like senior business leaders, government officials or even members of the clergy. They then seek referrals from these individuals as a means to maneuver their way into meetings with sales prospects.

On the positive side, by taking the necessary due diligence screening steps for financial professionals that have been outlined above, including asking the right questions and conducting necessary research, you can be better assured that the financial professional you hire will ultimately be the best choice for your financial needs.



Tapping Your Retirement Account – Now or Later?

Income Options When You Retire

If you're at or near retirement age, you'll want to begin thinking about how to begin tapping your retirement account for income. But don't act too rashly. There are specific guidelines as well as potential tax advantages associated with properly taking distributions from retirement plans such as 403(b) or 457 accounts.

403(b) Distribution Requirements

In general, qualified distributions (distributions without penalty) can be made from a 403(b) plan when one of the following triggering events occurs:

- The employee becomes disabled
- The employee dies
- The employee is under retirement age and leaves employment, but only if the distribution is rolled over into another qualified plan or an IRA
- The employee reaches age 59½
- The plan is terminated; but only if the distributions are rolled over into another qualified plan or an IRA

While most 403(b) plans allow participants to begin tapping their account without penalty at normal retirement age, some plans may allow you to annuitize payments earlier. You should check with your specific plan to see if it qualifies. Distributions made to individuals before they turn age 59½ may be subject to an additional 10% early-withdrawal penalty, but several exceptions to this rule apply. Consult with your tax advisor for details.

Withdraw From Taxable Accounts First

Because a 403(b) plan's earnings potentially grow tax-deferred until withdrawal, it may be in your best interest to postpone your plan distributions for as long as possible (until age 70½). Keep in mind that in general, distributions from a 403(b) account are taxable as ordinary income (at federal income tax rates as high as 35% and California state income tax as high as 9.3%, depending on your tax bracket), which is another reason not to immediately tap these assets.

Instead, it's usually best to withdraw assets from your taxable accounts first. Try to first withdraw taxable assets held for one year or longer, because of their

preferential tax treatment. Long-term gains – profits from assets sold after being held for more than a year – are taxed at 15%, which is lower than the tax for most people on ordinary income. If you sell assets held one year or less, they are taxed at short-term capital gains rates, which are the same as ordinary income tax rates.

At age 70½, the IRS requires that you begin taking required minimum distributions (RMDs) from your tax-deferred retirement accounts. In fact, if you fail to take an RMD by April 1 of the year after you turn 70½, not only will you be required to take an IRS-specified amount out of your retirement account, you'll may be hit with a 50% excess accumulation tax on the amount of the distribution that should have been taken, but wasn't. In a simplified example, suppose you have a balance in your 403(b) plan of \$100,000 and you are subject to RMDs. According to the IRS Uniform Life Expectancy table, you are expected to live another 26.5 years. That means you would need to divide \$100,000 by 26.5 and take a distribution of about \$3,775. If you fail to take the distribution, you may have to pay a penalty of up to half that amount, or \$1,887.50.

Note that in 2009 only, anyone age 70½ or older will not have to take a RMD, thanks to a one-time federal law designed to help retirees conserve their assets. After 2009, you will need to take RMDs. When it's time to do so, consult IRS Publication 590: "Individual Retirement Arrangements" [<http://www.irs.gov/pub/irs-pdf/p590.pdf>] and check with your tax advisor.

Annuity Distribution Options

If your 403(b) assets are held in an annuity, you will likely have multiple distribution options. You can choose to simply withdraw your earnings (or earnings and principal) in a lump sum, or over a period of time through regular or irregular withdrawals. Or you can choose to "annuitize" your assets, meaning that the current value of your annuity is converted to a stream of payments distributed over a specified period of time (such as for 20 years) or for the remainder of your life and the lifetime of another individual (called a joint and survivor annuity).

If you elect to simply withdraw assets from your annuity periodically, it's almost as if your annuity

acts like a bank savings account. Keep in mind that if you're age 70½ or older you will need to take at least the annual RMD in order to avoid penalties. In addition, if you withdraw too much from your annuity, it may not last as long as you had hoped.

If you choose the annuitization option for your annuity, it's impossible to withdraw too much from your annuity, which is why this is also called the guaranteed income option. The amount you receive each month, quarter or year (whichever you choose) from your annuity will depend on the cash value of your annuity, how earnings are credited to your account, the age when you begin receiving payments and the length of the distribution period.

Thus, if you're age 65 and elect to receive monthly payments over the remainder of your lifetime, the amount you receive will be less than if you were to receive monthly payments over, say, a five-year time period.

If the annuity is a fixed annuity with a fixed rate of return, the payments you receive will remain the same over the entire time of the annuitization. If instead you have a variable annuity, your payout

amount may vary depending on the market value of the assets in the account. The payment amount is determined by the investment performance of the annuity's investment portfolio. However, the variance in these distribution amounts may likely be minimal, since at retirement your variable annuity account will likely be primarily (or entirely) invested in low-risk and relatively stable-return investments.

Distributions from a 457 Plan

Generally, you can take distributions from your 457 plan only when the following occurs:

- The employee separates from the employer due to death, termination, voluntary departure, retirement, etc.
- The employee is still working, but has attained age 70½
- The employee has an unforeseeable emergency

Distribution options are similar to those for a 403(b) plan. However, there is no 10% tax penalty on distributions before age 59½ (or age 55 if separating from employment), as there is with a 403(b) plan.



How the New 403(b) Regulations Affect You

In the past, finding the information you needed about the 403(b) plans available to you was difficult. Perhaps you found out about these options when you were hired by your district, but haven't received any formal communications since. Maybe you learned about them from co-workers, or the insurance agent selling annuities in the break room, or a friend or family member.

New IRS regulations are intended to move 403(b) plans closer to 401(k) plans in the private sector. Districts will now have to have a written plan document that spells out eligibility for participation, the form and timing of distributions, contracts available under the plan, who is responsible for administration and compliance of the plan, and what optional provisions, such as plan loans or hardship withdrawals, are available. They must also include a list of approved 403(b) vendors. Districts are required to make a best-faith effort to comply with the new regulations on Jan. 1, 2009, but have been granted a grace period (through Dec. 31, 2009) to fix errors in the plan's operation.

The regulations also spell out that your deferrals must be submitted within a reasonable period by your employer (generally no later than the fifteenth business day of the month following the month in which the amount was taken out).

Failure to comply with the new regulations is a serious issue and could result in disqualification of the district's 403(b) plan, triggering tax consequences for participants.

What the Changes Mean for You - Technically

Transfers and exchanges will be different under the new regulations. Moving assets between vendors and between 403(b) plans must be permitted by the Employer's Plan Document. An exchange is the movement of your money between vendors that are approved by the employer and noted in the Plan Document. The new regulations require that there be information sharing agreements or a protocol in place between the approved 403(b) vendors and your employer. A plan-to-plan transfer is an in-service transfer of your account balance from one employer-sponsored 403(b) plan to another unrelated employer-

sponsored plan (used if you transfer to a new district). Any exchanges or transfers completed that conflict with the IRS regulations can be treated as a taxable event.

In addition:

- Your district is now responsible for and involved in the management of your 403(b) plan, including distributions such as loans and withdrawals.
- Your district's 403(b) plan provisions may differ from benefits you've had in the past.
- You may have a new list of approved 403(b) vendors. If your current vendor is deselected, you will need to find out if there is an opportunity to have them included or choose a new vendor from your list of approved vendors.
- Your district may have contracted with a third-party administrator (TPA) for some of their recordkeeping and compliance work. This cost may be passed on to you directly or deducted from your plan assets. Note that some third-party administrators are affiliated with 403(b) vendors, which can create a conflict of interest.

You can expect to receive an annual notice from your employer informing you of the right to participate in the district's 403(b) plan or change your election if you are a current participant. As noted above, some districts may outsource this communication requirement to a third-party administrator, which may be a potential conflict of interest if the TPA also sells products. CTA has partnered with CalSTRS and its endorsed TPA, 403(b)Comply. This is a TPA that can provide help to districts that need help with the new IRS compliance responsibilities without ties to any 403(b) product sales.

- Since 403(b)s must be universally available, they are, in most cases, open to part-time eligible workers.
- The district's new list of approved 403(b) plan vendors may result in new sales solicitations to you. It's important that you understand the investments available in your plan BEFORE signing up, which is one reason we've developed this booklet and the California Educators Investment and Retirement Guide Web site at www.ctainvest.org.

Who Does What?

The change in 403(b) regulations may have you wondering who is responsible for what. Here's a quick review.

District

The district is the sponsor for the 403(b) plan and:

- Creates plan document and list of approved vendors
- Offers a 403(b) plan to employees
- Is ultimately responsible for the operation and compliance of the 403(b) plan
- Complies with IRS regulations

Third-Party Administrator (TPA)

May be hired by the district to provide IRS compliance responsibilities, including:

- Remitting employee salary reductions to 403(b) vendors
- Maintaining Information Sharing Agreements (ISA) with 403(b) vendors
- Recordkeeping and other compliance duties contracted by district

403(b) Vendors

403(b) vendors offer various types of products such as fixed annuities, variable annuities and mutual funds through 403(b)7 custodial accounts. They:

- Provide investment options from which 403(b) participants choose
- Employ sales agents to market their 403(b) products
- Examples are Pension2 (CalSTRS), Vanguard, Fidelity, MetLife and others

You

As the 403(b) plan participant, you:

- Elect to participate in a 403(b) plan
- Choose and contribute to one of the 403(b) vendors offered by the district plan sponsor
- Select investment or annuity options available with the vendor you have chosen
- Complete a salary reduction agreement



So Now What Do I Do?

Ideally, reading this booklet has alerted you to the importance of retirement planning and given you some steps to follow.

If you're a new educator or school employee:

- Read the information given to you from your district about your 403(b) or 457 plan options.
- Use the valuable calculators at ctainvest.org, such as the asset allocation calculator to help estimate the impact of a particular asset allocation, to help you decide how much you need to save each month to reach your retirement goals.
- Determine what type of investor you are (conservative, moderate or aggressive). The risk tolerance quiz in the back of this booklet and at ctainvest.org can help.
- Think about the type of 403(b) or 457 product that makes sense for you. You can invest through an insurance company via a fixed or variable annuity or directly in mutual funds through a custodial account. Don't let the 403(b) vendor steer you into a product that isn't right for you.
- Review the investments available in your district's plan at www.403bcompare.com. Be sure to compare performance, fees and expenses, as well as whether the investment suits your goals, timeline and risk tolerance.
- Complete a salary reduction form and submit it to your district.
- Review your plan whenever you change jobs or have a major change in your personal or financial situation.

If you're an experienced investor:

- Review your current investment strategy and decide whether it still meets your goals, timeline and risk tolerance.
- Rebalance your investments, if necessary, to return to an asset allocation strategy that makes sense for you.
- If you have selected annuities in your plan, consider whether they are the best investment for you. If you decide to sell your annuity, be sure to

look into the impact of surrender fees, if any.

All investors:

- Find out if your school district has finalized its list of approved vendors.
- If your vendor is no longer listed, ask your district and current vendor about your options. If you must make a plan exchange, be sure to investigate any fees, taxes and/or penalties that could result.
- If you had transferred any 403(b) assets to a new 403(b) provider between Sept. 24, 2007, and Dec. 31, 2008, confirm that the new provider has an Information Sharing Agreement with the district.
- If you are selecting a new vendor, be sure to ask questions about the new product (especially fees) and do the research, including reviewing the information on www.403bcompare.com.
- Take advantage of the California Educators Investment and Retirement Guide Web site at www.ctainvest.org, where you'll find a wealth of information that can help you plan for and work toward a financially secure retirement.
- Attend California Teachers Association training sessions on retirement planning when offered.
- Check out the retirement education workshops given by CalSTRS and CalPERS at www.calstrs.org and www.calpers.ca.gov.

Next steps:

- Use the calculators at www.ctainvest.org to help determine how much money you will need to save for retirement to supplement your CalSTRS or CalPERS pension.
- Review the Webinar on asset allocation and check out the historical returns calculator at www.ctainvest.org.
- Review the vendors and investment options available through your district's plan at 403bcompare.com.
- Keep in mind that, even if you are a conservative investor, there are mutual funds with a conservative investment strategy that may meet your needs better than an annuity, and generally with lower fees.

Glossary

Annuity. This is a contract between an insurance company and an individual that generally guarantees a lifetime income option, usually at retirement, in return for either a lump sum or periodic payments. See fixed annuity and variable annuity.

Asset class. These are the main categories of investments at the most basic level, generally stocks (also called equities), bonds and cash or cash equivalents. When participating in a 403(b) or 457 plan, you will generally invest in mutual funds (should you choose) that incorporate the risk/return profiles of one or more of these asset classes.

Asset allocation. This is the strategy of dividing your money among the three major asset classes. This helps manage risk while you pursue growth, because the three classes tend to react differently to economic conditions.

Beneficiary(ies). The beneficiary or beneficiaries you name when you enroll in your 403(b) or 457 plan are the person or persons who will receive the balance of your account, if any, upon your death.

Bonds. Bonds are loans to a government, state, municipality, agency, institution or corporation. Typically, in return for the loan, the bond issuers agree to pay interest to the bondholder and pay back the principal (the amount paid for the bond) at the end of the bond's term (maturity). With zero-coupon bonds, however, no interest is paid. Instead, the bond is purchased at a discount from its face value to be redeemed at full value at maturity.

Cash equivalents. These are liquid investments (easily sold and converted to cash) that have little or no change in underlying price. Examples are money market or stable value funds.

Compounding. With compounding, earnings on the account (which can be any combination of interest, dividends and capital gains) are added to the principal, increasing the base upon which subsequent returns are earned.

Contribution. This is the amount of money, or percentage of your pay, that you put toward your 403(b) or 457 plan through a salary reduction agreement. The contribution is also sometimes called a deferral.

Defined benefit plan. The traditional pension plan, where the employer and employee make contributions, but the benefit is guaranteed and based on a formula that is consistently applied to all participants in the plan.

Defined contribution plan. This is a plan, like your 403(b) or 457 plan, in which you (the participant) makes contributions. The account balance is dependent on the amount contributed and the performance of the investments chosen by the participant.

Distribution. A distribution occurs when you start taking money from your 403(b) or 457, either as a lump sum or in a series of periodic payments. These distributions are generally taxed at ordinary income tax rates. Early nonqualified distributions from your 403(b) plan may be subject to a 10% tax penalty (does not apply to 457 plans).

Diversification. This investment strategy is a step beyond asset allocation. It means to spread your investments among not only the three asset classes, but also among different investments within those classes. In this way, you avoid letting any single investment have an outsized impact on your portfolio. Note, however, that diversification does not guarantee a profit or protect against loss in a declining market.

Dividend. A dividend is a share of the company's earnings that is paid out to stockholders. When you receive dividends within your 403(b) or 457 plan account, they are reinvested automatically for you.

Dollar-cost averaging (also called systematic investing). With this investment strategy, you invest the same amount of money on a regular basis, regardless of what the market is doing. In this way, you help remove emotional decisions from your investment strategy and decrease the impact that timing of the purchase has on your investments, which could be positive or negative. By contributing regularly to your 403(b) or 457 plan, you are taking advantage of dollar-cost averaging. Dollar-cost averaging cannot guarantee a profit or protect against loss in a declining market.



Fixed annuity. This is an annuity that guarantees a minimum return for a specific period, as specified in the contract with the insurance company.

Individual retirement account (IRA). This is a personal retirement account that you can get through a bank, credit union or brokerage account. You may open an IRA even if you have a defined benefit and/or defined contribution plan at work.

Mutual fund. A mutual fund pools money from many investors to purchase stocks, bonds, cash equivalents or some combination that is consistent with the fund's investment objective.

Portfolio. Your 403(b) or 457 plan portfolio is the collection of investments you have in your account. You may also have an investment portfolio outside your employer-sponsored retirement plan.

Principal. This is the amount of money you invest, before earning any interest or dividends.

Prospectus. The prospectus is the legal document that describes a mutual fund's objectives, types of investments and major holdings, risks and management style. It is important to read the prospectus before investing to see if the fund is appropriate for your goals, timeline and risk tolerance.

Re-allocation. Re-allocation occurs when you change your contribution strategy based on a change in your goals, timeline or risk tolerance. For example, you may decide that, as you near retirement, you want to re-allocate your contributions from 70% in a stock fund and 30% in a bond fund to 50% in a stock fund and 50% in a bond fund.

Rebalancing. This is the act of returning your investments to your original asset allocation if it has changed due to market performance.

Stable value investments. These types of investments are considered lower risk than stocks, and are generally high-quality, low-maturity bond funds that offer a steady investment value through the use of an insurance contract. Stable value funds typically stress preservation of capital and provide a steady stream of income.

Stocks. Shares in the ownership of a company are called stocks or equities. You can buy shares of stock in an individual company or through investment in a stock mutual fund.

Tax deferral. The major benefit of 403(b) and 457 plans, it allows funds within the plan to grow without being reduced each year by taxes. Taxes are paid at ordinary income tax rates when distributions begin at retirement.

Third-party administrator. An entity hired by the district to handle salary remittances to 403(b) vendors and other compliance and recordkeeping duties as assigned.

Variable annuity. This is an annuity (contract with an insurance company) in which the performance of investments in a subaccount determines the return.

Volatility. This is the fluctuation in prices of an investment over short periods of time.

Questions to Ask Agents Who Sell Investments

- Are you registered with state securities regulator? _____
- What is your disciplinary/arbitration history? _____
- What is your training and experience? _____
- Tell me about your investment philosophy and typical clients. _____
- May I see a list of references? _____
- How are you paid? Fee-based or commission-based? Are you in a sales contest? _____
- Are you an independent agent (who represents various companies), or are you an employee of an insurance company or 403(b)/457 provider? _____
- What are your credentials? Are you a ChFP (Chartered Financial Professional), CFP (Certified Financial Planner) or AIF (Accredited Investment Fiduciary)? _____

Additional Notes:

Be sure to get the information in writing, including the advisor's basis for recommending certain investments and disclosure of fees and penalties.

Risk Tolerance Quiz

1. I plan to use the money I am investing:

- a) Within 1-2 years
- b) Within 3-5 years
- c) In 6-10 years
- d) No sooner than 11 years from now

2. I expect that my future income from wages will:

- a) Decrease
- b) Remain about the same or go up a bit
- c) Increase faster than inflation
- d) Increase rapidly

3. In the event of a job loss or medical or other emergency, I have:

- a) No emergency savings
- b) Some savings, but less than three months' worth
- c) At least three months' worth of savings
- d) More than six months' worth of savings

4. My most important investment goal is to:

- a) Preserve the money I have at the expense of growth potential
- b) Receive some growth and some income
- c) Grow my investments somewhat faster than the rate of inflation
- d) Grow my investments much faster than the rate of inflation, even if it means greater risk to my principal

5. Of my current investments, I have this much invested in stocks or stock mutual funds:

- a) Less than 15%
- b) 15-39%
- c) 40-70%
- d) More than 70%

6. When I invest my assets in stocks or stock mutual funds, I feel mostly:

- a) Anxious

- b) Cautious
- c) Comfortable
- d) Confident

7. Which would you rather have:

- a) 100% chance of receiving \$1,000
- b) 50% chance of receiving \$5,000
- c) 25% chance of receiving \$20,000
- d) 5% chance of receiving \$100,000

Give yourself one point for each "a" answer, two points for each "b" answer, three points for each "c" answer and four points for each "d" answer.

Scoring

If you scored between 25 and 28 points, consider yourself an aggressive investor with a very high risk tolerance. An aggressive investor is someone who is willing to accept a high degree of investment risk in exchange for the chance to earn a dramatically higher rate of return.

If you scored 20-24 points, you have an above-average risk tolerance and could be considered a moderately aggressive investor, or one who is willing to accept a greater degree of risk for the chance to earn an above-average return.

If you scored 15-19 points, you are likely a moderate investor with an average tolerance for risk. This means you're willing to accept some risk in exchange for a potentially higher rate of return.

If you scored 10-14 points, consider yourself a conservative investor with a below-average tolerance for risk. This indicates that you're likely unwilling to accept a greater degree of risk in exchange for the chance to earn a higher rate of return.

If you scored less than 10 points, you may think of yourself as a very conservative investor. Chances are you cannot afford to lose any amount of your principal assets and/or you do not wish to take on much risk at all with your investments.

Resources

- California Educators Investment and Retirement Guide at www.ctainvest.org. An education and information resource developed by the California Teachers Association to help you make informed choices about your finances and retirement planning. Includes calculators, case studies and more.
- CalSTRS at www.calstrs.org. For information about your CalSTRS defined benefit pension, workshops, calculators that can help you estimate your pension benefits and more.
- CalPERS at www.calpers.ca.gov. For information about your CalPERS defined benefit pension, benefit calculators and more.
- 403bCompare at www.403bcompare.com. To find the vendors available in your district and research the products they are selling, including fees.
- Financial advisor Web sites, including www.cfp.net and www.napfa.org.
- Financial Industry Regulatory Authority (FINRA) at www.finra.org for background information on financial professionals and information about mutual funds and variable annuities.
- Security Exchange Commission at www.sec.gov for investor protection information.
- A.M. Best at www.ambest.com, Moody's at www.moody.com and Standard & Poor's at www2.standardandpoors.com for independent financial ratings of insurance companies.

Visit www.ctainvest.org.



CTA Risk Management/Business Initiatives & Development Department

Manager, Carole Anne Luckenbach CEBS, ARM, AIF

1705 Murchison Drive

Burlingame, CA 94010

business_initiatives@cta.org

Phone: (650) 552-5200

DISCLAIMER

The material and information contained in this guide is provided for educational purposes only. It may not be reproduced, in part or as a whole, passed on to other persons, or published by you. The information is not intended as investment, tax or legal advice or an endorsement of any particular method of investing. This information does not take into account any individual's specific investment needs or strategy, overall portfolio composition or asset allocation. Any charts, graphs, tables, calculators, worksheets or other information are for illustration only and should not be used as a primary basis for making investment decisions, including decisions relating to an employer-sponsored retirement plan. Before making savings and investing decisions, consider all of your assets, including, for example, equity in a home, cash value of insurance policies, IRAs, savings accounts, investments, and retirement plan assets, and consulting a financial professional.

In no event shall the California Teachers Association Economic Benefits Trust, or any of its sponsors or affiliates (hereinafter "CTA EBT"), be liable for any loss or damages of any nature resulting from, arising out of or in connection with the use of, or inability to use this guide or its content.

By reading and using this guide you agree to be bound by the terms set forth above. If you do not agree to all these terms, you should not use this guide.

Copyright 2009 California Teachers Association Economic Benefits Trust

Images may be from one or more of these sources: ©Jupiterimages, ©Getty Images, ©iStock, ©SnapVillage.

ctainvest.org