If You Don't Look Out for Your Own Future, Who Will?

401(k): Going to the Max

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Most of us have many financial goals we wish to achieve, such as owning a house, educating children or starting a business. We think one of the most important financial goals is to accumulate enough money so that you can retire when you wish in financial comfort. To accomplish this, most of us should contribute the maximum we can to our retirement plans and start as early as possible.

With the demands of short-term financial needs, it's hard to convince some people of the importance to set money aside for tomorrow. Some who are counting on an inheritance from their parents to pay for retirement may find their parents living longer and needing the income for their own care. How much is enough to save for retirement? The answer often is, "As much as you can." You don't know how long you'll live or how much it'll cost you to live.

Some of the Benefits of Saving for Retirement

The amount you contribute is excluded from current taxation. You can have as much as 100 percent of your salary up to certain maximum annual amounts automatically deducted from your paycheck and put into your retirement account.

Whatever amount you have deducted is excluded from current federal and state taxation, so this means Uncle Sam actually helps you make the contribution.

For instance, if you contribute $100 a month for a total of $1,200 annually and are in the 25-percent federal tax bracket, your out-of-pocket cost would really be $75 a month, or $900 annually: $1,200 minus $300 in federal income taxes you would have had to pay. In addition, if you live in a state that taxes your income, you would save that amount of taxes as well.

Whatever you accumulate in your retirement account isn't currently taxed. This means your money grows faster than if it were taxed. For instance, if you contribute $40 every two weeks for 10 years and it gains 8 percent annually, at the end of 10 years you'll have accumulated $15,945. In 20 years, $40 invested every two weeks will be worth $51,389, and in 30 years it'll become $130,173.

If you'd saved that same amount in your own name instead of in a retirement account and it earned 8 percent annually, and if you had to pay taxes on your earnings at a rate of 25 percent, the results would have been dramatically different *(see table at right)*.

You may also have a Roth option in your retirement plan. If you choose to contribute to a Roth 401(k) instead of a regular 401(k), you don't get a current tax deduction. The money in this account, however, grows without being taxed and when you withdraw from this fund at retirement age, this money isn't taxed either federally or locally. Contributing to a Roth 401(k) might work well for those who are in a low tax bracket now or are expecting their taxes to rise in the future.

The maximum you can contribute to the plan has increased from 2014. The maximum amounts are shown on the table on the next page.

Future annual increases will be adjusted for inflation in $500 increments.

Your Employer's Match

Some employers match your investments in the plan up to a certain amount. For instance, an employer might match every $1 you put in a retirement plan with $0.20 of the employer's money on the first 5 percent of compensation you invest each year.

If your employer matches, it's important to contribute at least enough to get the maximum employer match. So in the case above, you'd maximize the match by contributing 5 percent of your salary but would be getting the equivalent of 20 percent return on that money.

Your employer puts the matching money in a separate account and can choose from one of two vesting schedules. The first is gradual vesting, in which a certain percentage each year for up to six years becomes yours to take if you leave the employer.

The other provides no vesting until the third year, whereupon you're fully vested. When you're fully vested, you can take all matching contributions plus their earnings with you. Note that you're always 100-percent vested in your own contributions plus their earnings.

You can increase the amount you contribute to your retirement plan. When you first start working, you might not think you can afford to contribute the maximum you're

Untaxed Versus Taxed Investment Earning

Assumes an 8% annual return

Time period	Total personal savings invested	*401(k) or 403(b) growth	25% tax bracket
10 years	$10,400	$15,945	$14,228
20 years	20,800	51,389	40,136
30 years	31,200	130,173	87,310

* *This example is for illustrative purposes only and doesn't reflect the actual return of any particular investment. There can be no guarantee that any particular yield or return will be achieved from any investment.*

allowed to contribute. As time progresses and you get raises, you can increase the amount you contribute with a goal of contributing the maximum as soon as you can. Most plans allow you to change the amount you contribute at least twice a year.

You can choose how your money is invested within the retirement plan. The employer selects the various investment choices, but you can choose from among them to determine how you want your particular plan invested. You can periodically change the amount you're having withdrawn from your paycheck and how that money is invested. Usually, you can make changes to the investments you've already made within the retirement plan at any time.

You Can Take It With You

Whatever you defer in your retirement plan is yours. If you move from one job to another, you can take whatever you've accumulated in the retirement plan with you. Although employer contributions may follow a vesting schedule, you're always completely vested in whatever amount you defer from your salary. You can roll it over either into a self-directed individual retirement account in your own name, where it would continue to grow tax-deferred or in some cases into your new employer's retirement plan. You could even cash it in, which we wouldn't recommend since whatever you take out will be taxed in your tax bracket, and if you're under the age of 59½, under most circumstances barring specific exclusions, you'll also be charged a 10-percent surtax.

You'll receive investment education. You might be overwhelmed by the various investment choices available to you in your retirement plan. Typically, the financial adviser who helped your employer select investments for the retirement plan comes in periodically to talk to employees about the various options. Attend those meetings, read the information provided and ask questions. Usually that person is available to consult with you individually. If you need help, don't hesitate to take advantage of this opportunity.

Allowable 401(k) Contributions

Year	Age 49 or younger	Age 50 or older
2014	$17,500	additional $5,500
2015	$18,000	additional $6,000

Parental Assistance

Maybe your parents can help you. Despite the many obvious advantages of contributing to an employer-sponsored retirement plan, we find many younger employees underparticipate in their retirement plans or don't participate at all. Many feel they're too young or need the money to cover current expenses. It's in these earlier years, however, that participation can be very effective later on as those early contributions have more time to grow.

It might be true that they do need the money to cover current expenses. But if they're fortunate enough to have parents who can help them out, the parents could gift them enough to make sure they can contribute to their retirement plan.

For example, a parent can gift a child as much as $14,000 a year (in 2015) without having to be concerned about filing a gift tax return. Let's say that the adult child cannot afford to contribute to her retirement plan. She could sign up to contribute $500 a month, which would lower her taxable income, and her parent could give her $500 a month, which would help her build her retirement account. But not everyone is fortunate enough to have wealthy parents who are willing to be that generous!

Start Early

Waiting to participate isn't a good decision. To illustrate why it's important to start saving early, let's look at the numbers. If you start at age 22 and contribute $100 at the beginning of each month to your retirement plan, and it earns 8 percent a year, by the time you're 65 years old the account will be worth $450,478. If instead you wait just 10 years until you're age 32 to contribute $100 per month and it earns 8 percent, at age 65 you'll have $194,654 — quite a difference.

Particularly now that Congress is talking about the strain on the Social Security retirement system, we think that saving for your retirement is more a necessity than a choice and you should make it a priority. If you start saving early and contribute the maximum amount you can, you'll help make your retirement years your "golden years" and not your "nickel-dime years"!

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