Why 401(k)?

100% Savings Power

When you make a contribution to your 401(k), federal and any state income taxes are deferred until withdrawal. This means that 100% of your money goes to work for you right away! Participating in your 401(k) lowers your current income tax bill, too. Here's how:

Amanda and Jake each earn $25,000 per year, and both save 6% of their pay ($1,500) each year for retirement. Amanda saves through her 401(k) plan, so her contribution goes directly into her account pre-tax. Jake saves on his own, so he cashes his paycheck and puts away after-tax money in a savings account at his bank.

By saving through her 401(k) plan, Amanda gets a better tax deal. She lowers her taxable income, which means she pays less tax.

In this example, that translates into an annual tax savings of $225! Actually, she is out-of-pocket only $1,275 in order to save $1,500 ($1,500 - $225 = $1,275).

COMPARISON SHOPPING

Amanda's 401(k) Savings Strategy		Jake's After-Tax Savings Strategy
$25,000	Annual Pay	$25,000
-$1,500	Amanda's Pre-tax 401(k) Contribution	$0
$23,500	Taxable Pay	$25,000
-$3,525	Federal Income Tax*	-$3,750
$225	Tax Savings	$0
$0	Jake's After-Tax Contribution	-$1,500
$19,975	**Take Home Pay**	**$19,750**

*Assumes a 15% flat federal tax. State and local taxes are not included.

Your 401(k) is a key benefit offered by your employer, and it offers you one of the easiest ways to save for your retirement. Here's a closer look at the features that can help you to get the best retirement deal for yourself:

Automatic Payroll Contributions

Your 401(k) plan allows you to save each pay period up to annual limits set by the IRS. Your contribution is automatically deducted from your paycheck before you even see it. Out of sight, out of mind—what you don't have you won't spend! You will also be following a great savings principle: Pay yourself first.

It's Portable

Should you leave your company for any reason, you can take your vested account balance with you. Your money can be rolled over into an IRA or your new employer's 401(k) plan (if offered). However, there are strict rules when taking money out of your retirement plan. For instance, if you decide to take a cash distribution before age 59½, you may be subject to a 10% IRS penalty tax (in addition to current income taxes). Check with both your plan administrator and a financial advisor to make sure you understand all your options.

Tax-Deferred Growth

As your retirement account grows, you pay no taxes on any earnings until you begin to withdraw your money. This powerful feature is known as tax-deferred compounding. Investments with earnings that are tax-deferred have the potential to grow faster when they are not being "hit" by taxes each year.

Tax-deferred compounding can give a significant boost to your retirement account balance!

Comparison Savings

Let's return to Amanda and Jake to see what happens to their money after it gets deposited in their accounts:

SAVINGS COMPARISON

Amanda Earning 8% Pre-tax in her 401(k)		Jake Earning 8% Paying Taxes
Account Balance	**Year**	**Account Balance**
$23,468	10	$21,926
$43,468	15	$39,642
$74,134	20	$64,258
$118,432	25	$98,462
$183,519	30	$145,988
$279,153	35	$212,026
$419,672	40	$303,785

This illustration assumes an average annual rate of return of 8% (compounded annually) and a 15% flat federal tax. This is a what-if scenario and is not based on (or predicting the performance of) any specific investment or savings strategy. Most 401(k) investments will move up and down with the market over time, producing better or worse actual returns for you. Your returns are not guaranteed.

> *Which balance do you think would potentially provide you with the most income during retirement?*

> *Which balance do you think would potentially last longer during retirement?*

And remember, as a starting point, many financial experts feel you should save:

- In your 20s, save 7% of your salary.
- In your 30s, save 10% of your salary.
- In your 40s, save 15% of your salary.
- In your 50s, save 20% of your salary.

Source: Kmotion, Inc. 2012

Consumer Clue

Let's take a look at the difference tax-deferred compounding can make in terms of retirement income. Assume that upon retiring, both Amanda and Jake decide to divide up their account balance into 20 equal withdrawals. They plan to take one withdrawal each year over a 20-year period.

CONSUMER CLUE

Amanda		Jake
$419,672	Account Balance	$303,785
$20,984	Annual Withdrawal	$15,189
-$3,147	Taxes To Pay (15%)	0
$17,836	Money in Pocket Each Year	$15,189

Amanda has almost $2,600 more each year for pursuing her retirement dreams!

This illustration assumes a flat 15% federal tax rate and does not take into account any annual earnings or losses that may accumulate on the remaining balance of their accounts over the years.

Finding the **Money** to Save

It's hard to save for retirement and make it a priority. You could have childcare expenses, or you may be trying to save for college tuition. Maybe you're planning for a major purchase, such as a car or new home. Possibly you're supporting an aging parent. Does it seem like too many things are competing for your paycheck? The fact is, people at all income levels find themselves struggling just to make ends meet.

Budgeting for a Better Retirement

Keeping tabs on your spending is only the first step. What you do with your findings is critical in establishing the habit of saving money. The table below shows how making just a few small sacrifices can add up to a better retirement deal.

SMALL SACRIFICES

Give Up	How Often	Monthly Expense	Value if Invested 25 Years
Coffee & Bagel	Twice a week	$20.00	$19,147
Lunch Out	Twice a week	$50.00	$47,868
Dinner Out	Once a week	$100.00	$95,737
Movie Ticket	Once a month	$10.00	$9,574
Video Rental	Once a month	$6.00	$5,754
Vending soda	Once a day	$12.00	$11,488

Assumes an investment in a tax-deferred retirement account in which you hypothetically earn an average annual rate of return equivalent to 8%, compounded monthly. This is a what-if scenario and is not based on (or predicting the performance of) any specific investment or savings strategy. In the real world, most 401(k) investments will move up and down with the market over time, producing higher or lower actual returns for you. Your returns are not guaranteed.

Consumer Clue

- Savings of $60 in one week translates into $240 each month that could be invested in your 401(k) plan.
- In 25 years this could potentially add over $228,000* to your retirement savings.

* Assumes an 8% average annual return.

This chart shows how just a small increase in your contribution level could mean thousands of dollars over time. All contribution amounts are based on a $30,000 annual salary.

A SMALL INCREASE MAKES A BIG DIFFERENCE

Contribution Increase	Savings After 10 Years	20 Years	30 Years	40 Years
1% ($25)	$5,099	$17,863	$47,775	$115,520
2% ($50)	$10,180	$37,048	$102,289	$264,724
3% ($75)	$15,270	$55,571	$153,433	$397,087
4% ($100)	$20,360	$74,095	$204,578	$529,448
5% ($125)	$25,451	$92,619	$255,723	$661,809
6% ($150)	$30,541	$111,143	$306,867	$794,175

Source: Kmotion, Inc. 2012. Assumes a hypothetical 8% annual rate of return.

Track the Cash

When you look a little closer, however, chances are you'll find money that you may be spending thoughtlessly or that could be better used to save for your retirement. One of the best tools to help you find these savings opportunities is a spending journal. It can help you track where all your dollars are disappearing. A video rental or a lunch out might not seem to cost all that much, but the expense adds up over time. Try keeping a spending journal for several weeks and evaluate your spending habits.

Track the Cash

From the Desk of Amanda & Jake

Here are some excerpts from a sample spending journal.

★ = savings opportunities

Sunday

$63.00 Groceries (Forgot coupons and went in without a grocery list!)

★ $6.00 Toy action figure for Tommy while grocery shopping (He threatened a tantrum!)

★ $40.00 Pizza delivered for Sunday Pro Football (Friends dropped by; gotta remember to buy a frozen pizza next time!)

★ $10.00 Ice cream out for the family for letting me watch football!

Monday

★ $4.00 Coffee and bagel on the way to work

★ $6.00 Lunch—hot sandwich and soda at restaurant (Must start brown-bagging it!)

$50.00 Filled gas tank (I Should look into carpool or bus!)

Tuesday

★ $15.95 Bought new CD (I'll look into used CDs next time!)

$75.00 New outfit for Molly (Should buy on sale!)

★ $2.00 "Breakfast" at the vending machines

★ = $83.95 easy savings opportunities in one week

Shop Around

By shopping around and getting a better deal on basic things such as car insurance or your mortgage rate, you can uncover additional money that can be re-directed into your retirement plan each month. Here are a few ideas—along with the potential payoff for your financial future. But remember: the only way there can be a potential payoff is if you actually do re-direct the monthly savings into your retirement plan account!

GET A BETTER DEAL

Event	Monthly Amount Saved	Potential Balance if Invested for 25 Yrs at 8%
Shop around for a better cell phone plan	$15	$14,266
Receive a raise and invest $25 in your retirement plan	$25	$23,934
Shop for lower credit card interest rate*	$30	$28,721
Find a lower car insurance premium	$50	$47,868
Refinance your mortgage	$150	$143,605

This illustration is hypothetical and is not intended to reflect the actual performance of any investment or investment strategy. Actual investments will move up and down over time. This illustration assumes an 8% annual rate of return, compounded monthly, with investments made at the beginning of each period.

* Only if you absolutely must maintain a balance. You should make a plan to pay off the balance within a reasonable length of time by making more than the minimum payment each month.