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Don't Miss the Match

Are you taking full advantage of your company's 401(k)?

Provided by Christopher J. Ricci, Financial Advisor

The 401(k) plan is one of the most widely-utilized wealth creation tools offered Americans. These retirement savings plans have several advantages, including dollar cost averaging, tax savings and tax deferral. However, one of the most powerful advantages is the company match. If your company offers a match, are you making the most of it?

Not taking advantage of the company match is like passing up "free money". Most rational people don't walk past a \$5 bill on the ground without picking it up, but that's what people do every day when they don't contribute enough to their 401(k) to get the full company match. A full one-third of employees don't take advantage of this feature, and it may make their retirement less comfortable.¹

In a typical plan an employer will match 50% of an employee's contributions - up to 6% of their salary.¹ Let's say an employee with that type of plan decides he can't afford to contribute 6%, but instead chooses to put away 2% of his salary into his 401(k) account. If he's earning \$75,000 a year, his account balance (assuming no growth) will be \$2,250 by year's end. That's \$1,500 of his own money as well as \$750 of his employer's money. If the same person had contributed 6% he would end the year with \$6,750 - including \$4,500 of his contributions and \$2,250 of his employer's.

By investing just \$3,000 more dollars each year (\$4,500-\$1,500), the employee can make an immediate \$1,500 (\$2,250-\$750). It's hard to make that type of return in any other environment.

This isn't a 401(k) plan's only benefit. The higher account balances from making the most of a company match is magnified further by three other advantages of a 401(k) plan.

Regular investments into your 401(k) may help to reduce risk. Putting a pre-determined amount of money into an investment at regular intervals - as with your 401(k) - is called dollar cost averaging. This is believed, by many experts, to aid in reducing the overall risk of investing by helping an investor avoid buying at market

highs. A dollar cost averaging program allows investors to buy more shares when market prices dip. This lowers the average cost of each share purchased. If the share prices go up, the lower cost provides greater return.²

Investing in your 401(k) plan is an immediate tax savings. The reason? Every dollar put into the plan avoids being taxed as income.

For example, let's assume you decide to put \$100 per paycheck into your 401(k) plan and you pay 25% of your income in taxes. On payday, \$100 will go into your 401(k) plan. However, if you decided against investing in your 401(k), then you'll only get an additional \$75 in your paycheck after taxes. That additional \$25 is, essentially, a reward from the IRS for saving for retirement.³

Finally, contributing to your 401(k) allows those investments to growth tax-deferred. With most investments, you'll pay tax on any interest, dividends, capital gains, or proceeds from selling an investment each year. A 401(k) is a shelter from those taxes. As long as you keep the funds in your 401(k), your dollars can grow without having to give a share to the IRS. Over time, this can be a tremendous benefit.

For example, a \$10,000 account balance in a traditional investment for 30 years, with a tax rate of 30%, would only grow to \$27,970. If those same dollars grew at 6% in a 401(k), they could grow to \$33,043 over 25 years.⁴ That's an additional \$5,073 to enjoy during retirement.

Maximizing the company match with the inherent tax benefits of a 401(k) can go a long way toward helping achieve the goal of so many Americans ... a comfortable retirement.

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1. <http://www.usnews.com/money/personal-finance/retirement/articles/2008/05/13/3-mistakes-to-avoid-with-your-401k.html>

2. <http://beginnersinvest.about.com/cs/newinvestors/a/041901a.htm>

3. <http://money.cnn.com/magazines/moneymag/money101/lesson23/index2.htm>

4. <http://www.newyorklife.com/nyl/v/index.jsp?vnextoid=3e07a2b3019d2210a2b3019d221024301cacRCRD>