Investing in your 401(k)

"Where did the time go?". I find myself saying this year after year as soon as August comes around and it finally hits me that fall foliage and sweater weather is right around the corner. After hearing about all the exciting trips our clients have gone on this summer, it makes me want to go back and do a few more things differently, but unfortunately you cannot go back in time. However, that does not mean I can't adjust accordingly to change things for the future.

The expression "where did the time go" directly relates to retirement savings. I decided to focus on contributing to the 401(k) as my monthly educational topic because this savings vehicle is one way to sock away a decent portion of your earnings to fuel your retirement plan. For those of you who aren't aware, the 401(k) is a savings vehicle that is offered through your employer in which the employee (you) can elect to have a portion of your earnings (before taxes are taken out) invested into a variety of investments consisting of stocks, bonds, and money market funds offered by your plan sponsor. With investing in a 401(k), taxes are not paid on contributions to the plan until money is withdrawn from the 401(k) since this is tax-deferred money. The IRS currently allows the employee to contribute $18,500 per year into the 401(k) and if you are over age 50, they allow for a catch-up contribution which brings up the total contribution amount to $24,500, all of which is tax deductible in that tax year.

Again, referring to the expression, "where did the time go?", this is a great way to jump start your plan if you have not done so already before retirement is right around the corner. Sometimes employers even offer a matching portion where they too will match your contributions up to a certain amount. One great way to invest without emotion getting in the way is by using a strategy called dollar-cost averaging. By joining your 401(k) plan, you are using this strategy, but you can do it outside a plan, too. Dollar-cost averaging is just investing a set amount of money at regular intervals. For example, every pay period you invest $100, putting it into the same investment category each time. Sometimes your money will buy more shares (when the market is down) and sometimes it will buy fewer shares (when the market is up). The theory is that things will even out over time. Dollar-cost averaging lets you focus on the long term rather than worrying about which investment to pick this week, and it helps you avoid the urge to jump into the market just when it is rising and bail out when it is falling.

It should be known that a 401(k) does have early withdrawal penalties for money taken out prior to age 59 ½ as well as other tax consequences for other withdrawals. As always, we recommend consulting with a tax professional to see the tax ramifications of taking money out of a retirement savings plan or any investment for that matter.

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