

401(k) Plans

Key strengths

- ▶ You receive "free" money if your contributions are matched by your employer
- ▶ You decide how much to save (within federal limits) and how to invest your 401(k) money
- ▶ Your regular 401(k) contributions are made with pretax dollars
- ▶ Earnings accrue tax deferred until you start making withdrawals, usually after retirement
- ▶ Your Roth 401(k) contributions (if your plan allows them) are made with after-tax dollars; there's no upfront tax benefit, but distributions of your contributions are always tax free and, if you satisfy a five-year waiting period, distributions of earnings after age 59½, or upon your disability or death, are also tax free
- ▶ You may qualify for a partial income tax credit
- ▶ Plan loans may be available to you
- ▶ Hardship withdrawals may be available to you, though income tax and perhaps an early withdrawal penalty will apply, and you may be suspended from participating for up to six months
- ▶ Your employer may provide full-service investment management
- ▶ Savings in a 401(k) are exempt from creditor claims in bankruptcy (but not from IRS claims)

A 401(k) plan is a type of employer - sponsored retirement plan in which you can elect to defer receipt of some of your wages until retirement. If you make pre-tax contributions, your taxable income is reduced by the amount that you contribute to the plan each year, up to certain limits. The contributed amount and any investment earnings are taxed to you when withdrawn or distributed. If your plan allows after-tax Roth contributions, there's no immediate tax benefit, but qualified distributions are entirely tax free.

Most 401(k) plans offer an assortment of investment options, ranging from conservative to aggressive.

Bear in mind...

- ▶ 401(k)s do not promise future benefits; if your plan investments perform badly, you could suffer a financial loss
- ▶ If you withdraw the funds prior to age 59½ (age 55 in certain circumstances) you may have to pay a 10 percent early withdrawal penalty (in addition to ordinary income tax)
- ▶ The IRS limits the amount of money you can contribute to your 401(k)
- ▶ Unless the plan is a SIMPLE 401(k) plan, you may have to work for your employer up to five years to fully own employer matching contributions