focus on Retirement

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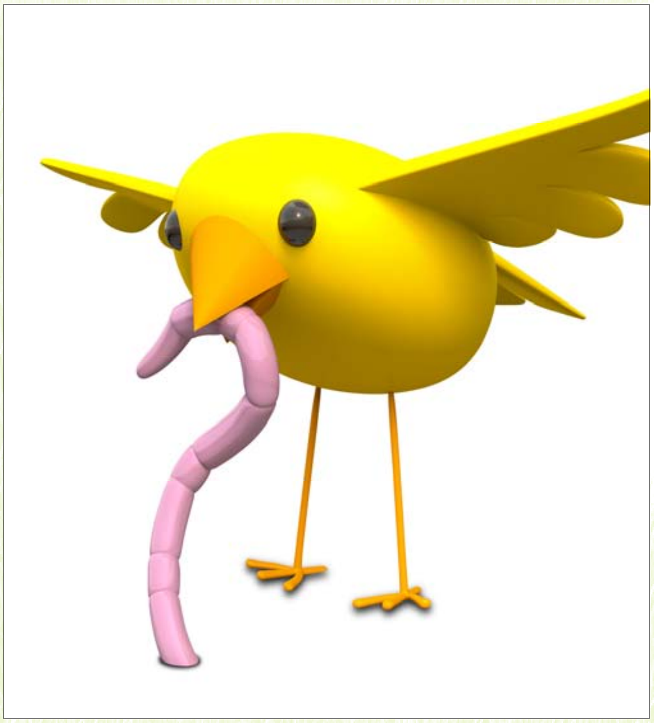
Saving Early and Often

When you are in your twenties, retirement seems like it is a long way off. However, it is proven that the earlier you start to save, the less you will need to contribute overall. A Prudential paper entitled “Planning for Retirement: The Role of 401(k)s in Retirement Income” says that saving in a 401(k) plan provides the best way to develop a good behavior of savings. Since most employers are no longer offering a pension plan that guarantees a certain income in retirement, 401(k) plans are becoming more and more crucial to retirement success.

A study for the Center for Retirement Research (CRR) at Boston College has shown a big difference in the amount of your retirement account based on when you start saving. The study indicates that if savings start at age 35 and last until retirement at age 65, an individual would need to save an average of 15%. However, if that same individual started saving at age 25 the savings rate would drop significantly to 10%. Conversely, if you wait until age 45 to start saving, you'd have to contribute 27%. As shown in the table below:



Retire at	Save at age 25	Save at age 35	Save at age 45
65	10%	15%	27%

Required Savings Rate (Source: CRR Calculations)

With so much uncertainly about Social Security, it just makes sense to take retirement savings into your own hands. In addition to saving early, another way to ensure a successful retirement is to regularly increase the percentage of income that you contribute to your 401(k) plan. If 10% seems too much right now, start at a lower percentage and commit to increasing that deferral by 1% every year or perhaps every time you receive a raise. If you can't afford to do that, then make sure that you are at least contributing enough to take advantage of the full amount of your employer’s match (if offered). If you’ve gotten a late start, then consider increasing your 401(k) contribution as much as you can or delaying your retirement past age 65. If you’re age 50 or over and you can afford it, make sure to take advantage of catch up contributions. A catch up contribution is the ability to make an extra $6,000 contribution to your 401(k) in addition to the normal dollar limit of $18,000 (limits provided are in effect for 2015 and will be adjusted for inflation).

Financial advisors agree—even small changes in savings amounts can add up to big numbers when you consider the years that your money has to grow until retirement. Taking control of your retirement savings now will help to make sure you have a secure and successful retirement.

Should I Take a 401(k) Loan?

If your plan allows loans, it may seem like a good idea to take a loan from your 401(k) plan. When you take a loan, you won't incur any taxes or penalties (unless you don't properly pay off your loan and incur a default). There is no credit check and most loans can be taken for any reason. Usually, the interest rate is lower than what a credit card would charge and you'll end up paying the interest on the loan back to yourself.

However, there are some downsides to taking a 401(k) loan. In order to access the money from your account, you'll need to remove it from the investment market where it could have made gains greater than the interest you'll be paying. You may need to reduce your current contributions into the plan in order to afford the loan payments. A study from Fidelity shows that "40% of borrowers decrease their savings rate and more than a third stop saving altogether." The money that you borrow is also taxed twice. It will be taxed as you earn the money to make your loan payments and then taxed again when you withdraw the money from your account at retirement. Lastly, most plans have a clause that your entire loan will come due within three months if you stop working for your employer. If you don't have the money to repay the loan at that time, you will pay tax on the outstanding balance of the loan as well as a 10% penalty if you are under the age of 59 1/2.

Sometimes taking a 401(k) loan is a smart bet, but it should really be considered only after considering all other options.

"I'm going to retire and live off my savings. What I'll do the second day, I have no idea."

- Unknown

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