Title:
Free Money for Your Retirement?

Word Count:
538

Summary:
Trying to figure out how to save more for your retirement? At least make sure you getting all the free money you're entitled to. Quicken for Dummies author and CPA Stephen L. Nelson explains.

Keywords:
IRAs, 401(k), 401k, financial planning, retirement savings

Article Body:
It can be more than a little discouraging to start making retirement planning calculations. You'll usually find that to achieve the annual retirement income you want, you need to be saving a lot more than is practical.

Suppose, for example, that you use a program like Quicken or Microsoft Money to determine that your retirement savings should equal to $5,200 a year—which is the same as $450 a month. (This savings amount will produce roughly $15,000 a year of retirement income if you save for 20 years, increase your savings with inflation, and earn 9 percent.)

Okay. That's great information to have. But practically speaking, where do you find this money? Well. first you want to get the free money that's available.

The first source of free retirement money

While $450 a month seems like a lot of money, you may be able to come up with this figure more readily than you might think. Say, for example, that you work for an employer who's generous enough to match your 401(k) contributions by 50 percent. In other words, for every dollar you contribute, your employer contributes $.50.

In this case, you need to come up with $300 a month to have $450 a month added to your retirement savings. To make this calculation, you divide the monthly savings amount, $450, by 1 + the employer's matching percentage, 50%. The formula $450/(1+50%) equals $300.

The second source of free retirement money

Also suppose that you pay federal and state income taxes of 33 percent and that you can deduct your 401(k) contributions from your income. In this case, the actual monthly out-of-pocket amount you need to come up with equals $200, not $450. To make this calculation, you multiply your share of the needed monthly savings, $300 in this example, by 1minus the 33% marginal tax rate, which equals 67%

In this case, the actual amount you need to come up with on a monthly basis equals $200 because $300 times 67% equals (roughly) $200.

Sometimes, most of your retirement savings money can come from others

Admittedly, $200 a month is still a lot of money. But it’s also a lot less than the $450-per-month savings you need to add to your retirement savings. In fact, most of the money in this example you need to save comes from other sources!

The preceding calculations argue for two tactics when saving for retirement. First, if an employer offers to match your contributions to something like a 401(k) plan, it will almost always make sense to accept the offer—unless your employer is trying to force you to make an investment that is not appropriate for you.

TIP   If you do want to contribute $300 a month to a 401(k) plan and need to reduce your income taxes withheld by $100 a month to do so, talk to your employer’s payroll department for instructions. You may need to file a new W-4 statement and increase the number of personal exemptions claimed.

Second, any time you get a tax deduction for contributing money to your retirement savings, it’s almost certainly too good a deal to pass up. As described in the preceding example, you can use the income tax savings because of the deduction to boost your savings so they provide for the desired level of retirement income.