



Communication Corner Newsletter - February 2014

Just What is a 401(k) Anyway?!?!

At Grinkmeyer and Leonard Wealth Management, we do our best to educate you about your company's retirement plan, the investments within it and how to utilize asset allocation; however, we realized recently that maybe we need to take a step back and address just what is a 401(k) plan. First and foremost, a lot of people we meet with mistakenly think that a 401(k) or an Individual Retirement Account (IRA) are an investment, but rather a 401(k) and IRA are just the basket in which you hold the investments. Here are some other important facts and features about both 401(k)'s and IRAs.

401(k)

A 401(k) plan is the common name for what is simply a section of US tax code that allows employers to sponsor a qualified retirement plan that allows employees to contribute a portion of their wages either on a pretax or in some cases post tax basis (known as a Roth option). A 401(k) account is portable, meaning you have the right to take your vested account balance with through either a distribution or qualified rollover if you terminate employment; it allows elective, regular contributions from both the employee and in some cases the employer up to the federal limit (\$17,500 for 2014 with an additional \$5,500 in catch-up contributions for those individuals over age 50); and the investments are participant directed which means that you have the right to select the where to put your money from the list of investment options provided in the plan.

Individual Retirement Account (IRA)

Some you may have or may have thought about opening up an Individual Retirement Account, commonly known as an IRA, as a way to save for retirement. The basics of an IRA are just about anyone under the age of 70 1/2 can open one, they offer tax-deferred earnings until you withdrawal the money after age 59 1/2, contributions to a traditional IRA can potentially be deducted on your tax return and an individual can contribute \$5,500 (\$6,500 if age 50 or older) for 2014. There are also Roth IRAs which allow you save money for retirement; however with Roth IRAs you do not take a deduction on your income taxes and you can withdrawal both the principal and the earnings and income tax free if certain requirements are met.

401(k) vs. IRA

While we would encourage you to save for retirement by any means necessary, we would also argue that there are some distinct advantages to saving money through your company's 401(k) plan. First, the contributions are consistent and reoccurring. To explain, once you establish your salary reduction agreement with your employer by telling them what percentage of your salary or dollar amount to contribute, your money is contributed every pay period without you having to do anything else; whereas with an IRA you have to make the effort to contribute. Secondly, the contribution limits are higher; \$17,500 for a 401(k) versus \$5,500 for and IRA.

Finally, and perhaps most importantly, the ability to take advantage of pretax. Let's look at an example:

	Susan Saves on a Pretax Basis	Joseph Saves on an After-tax Basis
Gross Monthly Pay	\$3,000	\$3,000
Monthly Pretax Contribution ¹	-\$500	-\$0
Monthly Taxable Pay	\$2,500	\$3,000
Federal Income Tax = 25% ²	-\$750	-\$900
Monthly After-tax Contribution	-\$0	-\$500
Take Home Pay³	\$1,750	\$1,600

This is a hypothetical example for illustrative purposes only. Rates of return, values, and assumptions are not guaranteed and are not indicative of past or future results.

1. Pretax contributions and any earnings will be taxed at the time of withdrawal at the tax rate in effect at that time. This does not take into account FICA taxes, exemptions, itemized deductions, state and local taxes, and federal taxes other than income tax. The participant's own tax bracket may be higher or lower, depending on his or her individual circumstances.
2. Your own federal tax rate may be different. State and local taxes are not included.
3. Net take-home pay after tax deductions for federal income taxes and contributions to plan or taxable account.

Want to Learn More About Utilizing Your Company's 401(k) Plan to Save for Retirement?

As the Financial Advisors who help represent the participants in your company's retirement plan, we're here to help start or enhance your road to retirement! If you'd like to learn more about how Grinkmeyer & Leonard Wealth Management can help you, contact us today or visit us online at

www.retirementplanready.com



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