# Taking Note of National 401(k) Day

*On this date, here are some actionable ways to make sure your retirement plan is keeping pace.*

Saving for retirement takes many forms, but one of the most popular ways to build a nest egg is through workplace retirement plans. Unfortunately, while most employees who are eligible do use 401(k) accounts, many choose to participate at relatively low rates.

At least that was the finding of Bank of America's 2022 Financial Life Benefits Impact Report. The study found that 58% of eligible employees participated in their company's 401(k) plan. On the other hand, it also estimated that a majority (61%) contributed less than $5,000 in 2021. [1]

Even more startling: Less than 10% of those eligible to participate in a 401(k) plan last year chose to contribute at maximum levels. By comparison, the IRS allows for 2022 up to $20,500 in elective deferrals for participants in 401(k) and 403(b) plans. Those over age 50, though, can also make a catch-up contribution of as much as $6,500 to max out a savings plan during the year.

Consider how much such a lower savings rate can mean over time. Let's use as an example someone who is 35 years old, earns $50,000 a year and plans to retire in 30 years. For simplicity, we'll assume this worker's salary doesn't go up over time. The 401(k) account in question will start with a balance of $1,000 and the employer will provide a 50% match on the first 6% of that person's annual salary contributed to the 401(k) plan.

Using such a scenario, we're also going to calculate a fairly conservative 6% annual rate of return for this person's workplace retirement plan portfolio over these 30 years. Now, using IFA's 401(k) Savings Calculator, we can see that in this illustration:

- Contributing 10% of this hypothetical employee's salary each year would wind up with a total of $536,177 after 30 years.
- At a contribution rate of 20%, the end result would be $944,194.

Note: You can find IFA's 401(k) Savings Calculator online at: https://www.ifa.com/calculators/401k-savings/

"The value of maximizing all of an employer sponsored savings plan benefits shouldn't be underestimated — a well-funded workplace retirement account can prove to be a significant tool in achieving your long-term financial goals," said Shareen Balkey, director of retirement services at Index Fund Advisors.

In order to emphasize the importance of taking advantage of such savings plans, the Friday after Labor Day is traditionally recognized as National 401(k) Day. In case it's been awhile since you've taken a look at your plan's website, this might be an ideal time for a closer inspection.

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Below are some suggestions of areas to check and possible changes to becoming a more strategic retirement saver:

### Contribution Rates

Just a little bit more can make a huge difference. In a traditional 401(k) savings account, you can reduce federal income taxes since contributions are made on a pre-tax basis. As a result, taxes on those yearly contributions are deferred until you make withdrawals. That's especially useful when combined with the power of compounding over time.

In our illustration above, we showed you how much difference contributing 10% versus 20% can make to your overall nest egg. But even smaller incremental increases can turn out to be quite significant as well. Again, using the IFA 401(k) Savings Calculator and the same hypothetical example:

– Increasing your annual contribution from 10% to 12% would improve your savings at age 65 by $81,602 to $617,779 after 30 years.

– Raising your contributions from 12% to 13% each year would increase your total another $40,805 to $658,584 by age 65.

### Enrollment Options

Some retirement plans offer automatic enrollment features, which can help nudge you forward with making contributions. In these cases, a plan sponsor will typically designate a certain fund, or set of funds, to start putting your savings to work right away.

Also, you might be able to use target-date retirement funds. These are designed to systematically adjust asset-allocation levels. The idea is that as you get closer to retirement, these funds will move towards holding a greater percentage of bonds as a means to reduce overall portfolio risk in a diversified portfolio of stock and bond funds.

### Investment Options

As circumstances change in your life, so might your savings requirements. Academics teach us that it can make a lot of sense over time to think strategically about your 401(k) savings. That's why retirement plan experts urge participants to regularly re-evaluate whether they're current rate of savings is likely to be enough to meet their longer-term needs.

Along these lines, it's also common for retirement advisors to instruct retirement savers to make sure to check their fund allocations to align with individual tolerances for risk. The IFA Risk Capacity Survey is designed to help individuals evaluate such questions. You can find it online here: https://www.ifa.com/survey/#retirement

Footnote:

1. Bank of America, 2022 Financial Life Benefits Impact Report, July 2022.