

## Building Your Retirement Nest Egg

In previous articles we explained how to estimate the amount you'll spend each year once you stop working, and the size of the nest egg you'll need to support that spending. The next step is to figure out how much you'll need to save each year to build your investment portfolio. There are many interactive tools available to help you arrive at this savings number, including one accessible through the U.S. Securities and Exchange Commission website. Find the one that you are most comfortable using.

Reaching your retirement goal however depends not only on how *much* you save, but also *how* you save. The challenge is determining which combination of options will yield the greatest benefit. Here are a few suggestions:

**Start now.** Leverage the power of compounding. Compounding occurs when investment earnings generate their own earnings. To work, it requires saving, re-investing the earnings, and time. The more you save and the more time your money has to grow, the better.

**Make use of tax-advantaged accounts.** Employer retirement plans (e.g. 401k, 403b) and IRAs are powerful wealth building tools because of the special tax treatment they receive. Contributions and earnings grow tax-deferred or even tax-free for years, increasing your chances of building a substantial retirement nest egg.

These accounts come in two versions, traditional and Roth. Typically, contributions to traditional accounts can reduce taxable income and therefore your tax bill. Furthermore, investment earnings are *tax-deferred* until withdrawn. Roth contributions on the other hand are not tax deductible, but earnings and withdrawals during retirement are *tax-free*, provided you meet some basic requirements.

**Prioritize how you use your savings.** For many people, a sensible order for directing savings might be:

If your employer plan offers a matching contribution, save at least the amount your employer will match. This is "free" money and it will grow tax-deferred. You won't get a better deal anywhere.

If you don't get an employer match, or have already taken full advantage of one and still have additional savings, pay down any high interest debt next. Unpaid interest and finance charges are continuously added to your balance, so the power of compounding actually works against you, creating a snowball effect. After an employer match, eliminating this debt will provide a great return on your investment.

For any additional savings, think about funding your tax-advantaged options to the extent possible. Whether you add to your employer's plan or contribute to a traditional IRA or Roth IRA depends upon what you qualify for and your individual circumstances. Here's what you might consider doing next:

Fund an IRA. This gives you the benefits of tax-advantaged growth and a large menu of investment options your employer plan may not offer. First, consider a Roth IRA. Because retirement withdrawals are not required and are tax-free, this can be an excellent choice if you plan to let the money grow for a long time, pass it on to your heirs, or expect higher tax rates in retirement. It is a great tool to preserve assets for future generations, since your heirs will also be able to take withdrawals income tax free. If you're ineligible for, or don't expect to reap the benefits of a Roth, take advantage of tax-deferred growth with a traditional IRA. If you are unsure of which IRA is best for you, consider splitting your contributions between the two.

If you decide to fund your IRA to the limit, and still have more savings, continue funding your 401(k) up to the maximum allowed. After that, direct any retirement savings into a taxable brokerage account.

There are lots of great ways to save for retirement. Now that you have a sensible plan in place, it's time to put that plan into action!

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