Callahan Newsletter

Keeping you current

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Making the Most of Your 401(k) Plan

A 401(k) plan represents one of the most powerful retirement savings opportunities available today. If your employer offers a 401(k) plan and you're not participating in it, you should be.

Contribute as much as possible

The more you can save for retirement, the better your chances of enjoying a comfortable retirement. If you can, max out your contribution up to the legal limit ($17,500 in 2013, $23,000 if you're age 50 or older). If you need to free up money to do that, try to cut certain expenses. (Note: some plans limit the amount you can contribute.)

Why invest your retirement dollars in a 401(k) plan instead of somewhere else? One reason is that your pretax contributions lower your taxable income for the year. This means you save money in taxes immediately when you contribute to the plan--a big advantage if you're in a high tax bracket. For example, if you earn $100,000 a year and contribute $17,500 to a 401(k) plan, you'll only pay federal income taxes on $82,500 instead of $100,000.

Another reason is the power of tax-deferred growth. Any investment earnings compound year after year and aren't taxable as long as they remain in the plan. Over the long term, this gives you the opportunity to build an substantial sum in your employer's plan. (Your pretax contributions and any earnings will be taxed when paid to you from the plan.)

Consider Roth contributions

Your 401(k) plan may also allow you to make after-tax Roth contributions. Unlike pre-tax contributions, Roth contributions don't lower your current taxable income so there's no immediate tax savings. But because you've already paid taxes on those contributions, they're free from federal income taxes when paid from the plan. And if your distribution is "qualified" (that is, the distribution is made after you satisfy a five-year holding period, and after you reach age 59½, become disabled, or die) any earnings are also tax free.

If your distribution isn't qualified, any earnings you receive are subject to income tax. A 10% early distribution penalty may also be imposed if you haven't reached age 59½ (unless an exception applies).

Capture the full employer match

Many employers will match all or part of your contributions. If you can't max out your 401(k) contributions, you should at least try to contribute as much as necessary to get the full employer match. Employer matching contributions are basically free money. By capturing the full benefit of your employer's match, you'll be surprised how much faster your balance grows. If you don't take advantage of your employer's generosity, you could be passing up a significant contribution towards your retirement.

Access funds if you must

Another beneficial feature that many 401(k) plans offer is the ability to borrow against your vested balance at a reasonable interest rate. You can use a plan loan to pay off high-interest debts or meet other large expenses, like the purchase of a car. You typically won't be taxed or penalized on amounts you borrow as long as the loan is repaid within five years. Immediate repayment may be required, however, if you leave your employer--if you can't repay the loan, you may be treated as having taken a taxable distribution from the plan.

And remember that when you take a loan from your 401(k) plan, the funds you borrow are generally removed from your plan account until you repay the loan, so you may miss out on the opportunity for additional tax-deferred investment earnings. So loans (and withdrawals if available) should be a last resort.

Evaluate your investment choices

Choose your investments carefully. The right investment mix could be one of your keys to a comfortable retirement. That's because over the long term, varying rates of return can make a big difference in the size of your 401(k) plan account.

Four Retirement Planning Mistakes to Avoid

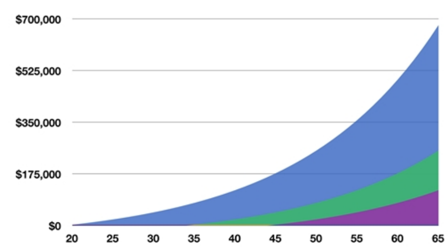
Because retirement may be many years away, it's easy to put off planning for it. The longer you wait, however, the harder it is to make up the difference later. That's because the sooner you start saving, the more time your investments have to grow.

We all recognize the importance of planning and saving for retirement, but too many of us fall victim to one or more common mistakes. Here are four easily avoidable mistakes that could prevent you from reaching your retirement goals.

1. Putting off planning and saving

Because retirement may be many years away, it's easy to put off planning for it. The longer you wait, however, the harder it is to make up the difference later. That's because the sooner you start saving, the more time your investments have to grow.

The chart below shows how much you could save by age 65 if you contribute $3,000 annually, starting at ages 20 ($679,500), 35 ($254,400), and 45 ($120,000). As you can see, a few years can make a big difference in how much you'll accumulate.



Note: *Assumes 6% annual growth, no tax, and reinvestment of all earnings. This is a hypothetical example and is not intended to reflect the actual performance of any investment.*

Don't make the mistake of promising yourself that you'll start saving for retirement as soon as you've bought a house or that new car, or after you've fully financed your child's education--it's important that you start saving as much as you can, as soon as you can.

2. Underestimating how much retirement income you'll need

One of the biggest retirement planning mistakes you can make is to underestimate the amount you'll need to accumulate by the time you retire. It's often repeated that you'll need 70% to 80% of your preretirement income after you retire. However, depending on your lifestyle and individual circumstances, it's not inconceivable that you may need to replace 100% or more of your preretirement income.

With the future of Social Security uncertain, and fewer and fewer people covered by traditional pension plans these days, your individual savings are more important than ever. Keep in mind that because people are living longer, healthier lives, your retirement dollars may need to last a long time. The average 65-year-old American can currently expect to live another 19.2 years (Source: National Vital Statistics Report, Volume 60, Number 4, January 2012). However, that's the average--many can expect to live longer, some much longer, lives.

In order to estimate how much you'll need to accumulate, you'll need to estimate the expenses you're likely to incur in retirement. Do you intend to travel? Will your mortgage be paid off? Might you have significant health-care expenses not covered by insurance or Medicare? Try thinking about your current expenses, and how they might change between now and the time you retire.

3. Ignoring tax-favored retirement plans

Probably the best way to accumulate funds for retirement is to take advantage of IRAs and employer retirement plans like 401(k)s, 403(b)s, and 457(b)s. The reason these plans are so important is that they combine the power of compounding with the benefit of tax deferred (and in some cases, tax free) growth. For most people, it makes sense to maximize contributions to these plans, whether it's on a pre-tax or after-tax (Roth) basis.

If your employer's plan has matching contributions, make sure you contribute at least enough to get the full company match. It's essentially free money. (Some plans may require that you work a certain number of years before you're vested in (i.e., before you own) employer matching contributions. Check with your plan administrator.)

4. Investing too conservatively

When you retire, you'll have to rely on your accumulated assets for income. To ensure a consistent and reliable flow of income for the rest of your lifetime, you must provide some safety for your principal. It's common for individuals approaching retirement to shift a portion of their investment portfolio to more secure income-producing investments, like bonds.

Unfortunately, safety comes at the price of reduced growth potential and the risk of erosion of value due to inflation. Safety at the expense of growth can be a critical mistake for those trying to build an adequate retirement nest egg. On the other hand, if you invest too heavily in growth investments, your risk is heightened. A financial professional can help you strike a reasonable balance between safety and growth.

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A Business Plan Is Your Vision of Success

Business plans help key stakeholders share in your vision, but even if you don't have stakeholders, they can help you identify your strengths and weaknesses for strategic planning purposes. For more information, visit the Small Business Administration's [new online resource.]()

What is your business's key to success? Unique products, flawless customer service, nimble operations--or something entirely different? As a business owner, you may instinctively know what makes your organization succeed in today's competitive marketplace. A business plan helps you share that knowledge with important stakeholders--including key employees and potential investors and lenders.

A good business plan tells the story of your company, illustrating where you are now and where you hope to be in three to five years. It provides a detailed description of your organization's current state and paints a picture of what it will look like in the future. Most important, it provides--in as few words as possible--the information others will need to make financial and strategic decisions, and is typically organized using the following sections.

Cover page and table of contents

The cover page is simply a title page for your business plan document. It should include the name of the company, address, phone number, owners' names, and contact information. It should also include the date on which the document was finalized and published.

The table of contents helps readers navigate through the document and identifies page numbers for each of the sections.

Executive summary

The executive summary is essentially your elevator pitch--an abridged version of the business plan that describes to readers why your business is worthy of their attention and possibly their investment. It should be no longer than one page, but should contain all pertinent details. (For this reason, it is often easier to write this section last.) It should answer readers' primary questions--i.e., are you looking for funding, is the document a roadmap for management, or both? As you draft your executive summary, keep in mind that many readers will decide whether the subsequent pages are worth reviewing based on this important section.

Business description

This section should provide more detail on the nature of your business. What product or service do you provide, and how is it produced? Who are your key advisors and managers, and how does their experience benefit your organization? What is your legal structure? Where are you located and why did you choose this location? You might also want to use this section to describe the genesis of your business--i.e., how and why you decided to launch the venture. Was there an industry gap you wanted to fill? A need you could meet? What makes your business idea worth pursuing?

Market analysis and marketing strategy

Perhaps the most influential section of your business plan, the market analysis is how you convince readers that your business will be successful. It should provide a specific and detailed analysis of your target market, including what you have done to maximize your opportunity within it. Who are your current and potential customers, and why?

Summarize any market research you have conducted to prove the viability of your business. How big is your potential market? Who are the major competitors, and what is your strategy for differentiating your company from them? If your business plan is intended for potential investors or lenders, this section will help convince them that you truly understand your market and are an expert in your industry. If your plan is primarily designed to educate key employees, it will provide the basic information they need to strategize.

This section should also summarize your marketing strategy, or how you will promote your products and services. Describe any planned advertising and communications tactics, as well as sales models.

Financials

This portion of the business plan is designed to help your readers understand where you are now, financially, and where you hope to be. You should include all current and projected (or "pro forma") financial statements. These should include cash flow and income statements, as well as a balance sheet and break-even analysis. This section will likely be scrutinized the most, so be sure it is completed carefully. Its purpose is to educate readers about the use of resources--including any debt and equity financing you hope to get--proving to them that your company can and will manage money effectively.

Take time and care

Many business owners--particularly entrepreneurs just starting out--loathe spending time writing business plans, preferring instead to jump into the more exciting arenas of creating, selling, and managing their business. However, a business plan represents a critical opportunity to draw key stakeholders into your vision of a future filled with success. Be sure to devote the time needed to produce an effective and engaging document.

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Securities and advisory services offered through LPL Financial member FIRNA/SIPC, a Registered Investment Advisor.

I refinanced my mortgage loan last year. Can I deduct any of the costs associated with refinancing the loan?

Now more than ever, homeowners are taking advantage of historically low interest rates and refinancing their mortgage loans. Did you pay points to your lender when you refinanced your loan? If so, you may be able to deduct them.

Points are costs that a lender charges when you take out a mortgage loan or refinance an existing mortgage loan on your home. One point equals 1% of the loan amount borrowed (e.g., 2 points on a $300,000 loan equals $6,000).

In order for points to be deductible, they must have been charged by your lender as up-front interest in return for a lower interest rate on your loan. If the points were charged for services provided by the lender in preparing or processing the loan, then the points are not deductible.

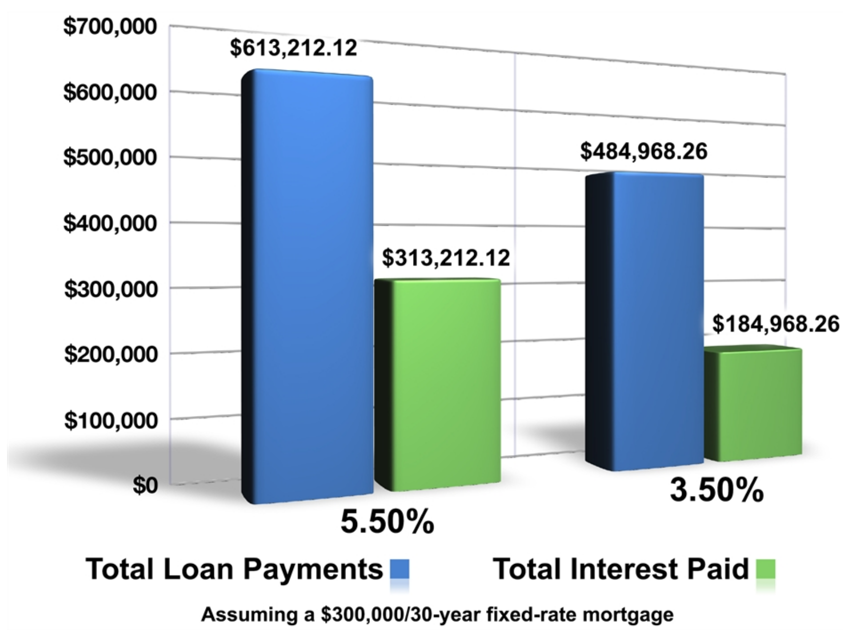
When deducting points, keep in mind that unlike points paid on a loan used to purchase a home, points paid on a refinanced loan usually cannot be deducted in the year that you paid them. Instead, the points may need to be amortized over the life of the loan.

For example, assume that you refinanced to a $300,000/30-year mortgage loan and paid $6,000 in points. You would be able to deduct 1/30 of those points each year over the 30-year loan period, or $200 per year.

The one exception to the amortization rule is if part of your refinanced loan is used to make improvements to your primary residence. In that case, you may be able to deduct the portion of the points that is allocable to the home improvements in the year that the points are paid. In addition, if you choose to refinance again or sell your home in the future, you can generally claim the entire unamortized deduction that remains. For more information on the deductibility of points, you can refer to IRS Publication 936.

As for other costs you may have incurred from refinancing, such as recording, title search, appraisal, and attorney's fees, they are not deductible. Furthermore, unlike costs associated with a home purchase, costs associated with a refinance cannot be added into the cost basis (value) of your home for income tax purposes.

The Potential Benefits of Refinancing Your Mortgage



This is a hypothetical example and does not reflect all of the costs that may be associated with refinancing. Actual results may vary.

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