

What is a 401(k) and Why would I want to put money into it?

This is the definition as found on the IRS website:

Traditional 401(k) plan

A traditional 401(k) plan allows eligible employees (i.e., employees eligible to participate in the plan) to make pre-tax elective deferrals through payroll deductions. In addition, in a traditional 401(k) plan, employers have the option of making contributions on behalf of all participants, making matching contributions based on employees' elective deferrals, or both. These employer contributions can be subject to a vesting schedule which provides that an employee's right to employer contributions becomes nonforfeitable only after a period of time...

Tax Savings with 401(k)

Saving on your Own			Saving with 401(k)	
Gross Wages	\$1,000		Gross Wages	\$1,000
All Taxes = 25% *	\$ 250		Invest Money	\$ 100
After Tax Wages	\$ 750		Taxable Wages	\$ 900
Invest Money	\$ 100		All Taxes = 25% *	\$ 225
Money Left Over	\$ 650		Money Left Over	\$ 675

* All Taxes = 25% is an assumed combined tax rate from all sources. Check IRS tables for your Tax Bracket.

With this example you save \$25 in taxes which results in \$25 more money left over.

Company Matching Contributions

Saving on your Own			Saving with 401(k)	
Gross Wages	\$1,000		Gross Wages	\$1,000
All Taxes = 25% *	\$ 250		Invest Money	\$ 100
After Tax Wages	\$ 750		Taxable Wages	\$ 900
Invest Money	\$ 100		All Taxes = 25% *	\$ 225
Money Left Over	\$ 650		Money Left Over	\$ 675
			5% of Wages	\$ 50
			25% match	\$ 12.50
Money Invested	\$100		Money Invested	\$ 100
			Company Match	\$ 12.50
			Total Invested	\$ 112.50

Tax Savings on Growth of Investment

Saving on your Own			Saving with 401(k)	
Money Invested	\$100		Money Invested	\$112.50
Investment Grows 7%	\$ 7		Investment Grows 7%	\$ 7.87
All Taxes = 25% *	\$ 1.75		All Taxes = 0% *	

* Taxes are paid when you take money out 401(k) typically at retirement so your money grows tax deferred