THE Wealth REPORT

# 5 STRATEGIES TO MAKE YOUR EMPLOYER-SPONSORED RETIREMENT PLAN WORK HARDER

If you have access to a 401(k) plan through an employer, that's the easiest way to save for retirement. But maximizing its potential may take a little more work.

## Overview

You work, you save, you invest. But one of the keys to successful investing is making sure your investment works hard for you.

Take a 401(k), for example: Participating in this employer-sponsored retirement plan can make it easy to invest. But there is more to a 401(k) than automatically deferring income from your paycheck, choosing a few mutual funds and letting your account ride for 30+ years. Instead, you can employ some strategies that fit your life and goals — and help make sure your retirement plan works just as hard as you do.

How can you help maximize your plan's growth and help make sure you have the income you need in retirement? Let's look at five strategies savers can use to make the most of an employer-sponsored retirement plan.

## Strategy #1: Get 'Free' Money

If your employer offers a matching contribution to your 401(k) plan, try to defer at least a percentage of your income required to take full advantage of that match. For example, if your company contributes 50 cents for every dollar saved, up to a specific percentage of your pay, then try to defer that percentage of your income each year.

To see how this "free" money works to your advantage, consider Jane, who earns $75,000 a year. If she defers 6% of her annual earnings, she'll contribute $4,500 a year. If the company contributes a 3% match, that's another $2,250 invested.

Assuming Jane carries on with this investment pace and continues to earn $75,000 per year (although her income will likely grow) for 30 years, an average annual investment return of 6% would yield $181,822 more in retirement savings because she took advantage of the company match.*

## Strategy #2: Make It Grow Faster

The nice thing about automatic deferrals from your paycheck is that your 401(k) balance may continue to grow regardless of market performance. One way to help it grow faster is to

contribute more each paycheck.

In other words, if you're contributing only the amount that allows you to take full advantage of your employer's match, you may not be contributing as much as you're permitted. In 2025, the employee contribution limit for a 401(k), 403(b), 457 or Thrift Savings Plan is $23,500, up from $23,000 in 2024. Employees age 50 and up may contribute an additional $7,500, for a total annual contribution of $31,000. And new for 2025, employees who are ages 60, 61, 62 and 63 have a higher catch-up contribution amount of $11,250, for a total annual contribution of $34,750. (Employer matches do not count toward the contribution limit.)[1]

One additional benefit of maxing out your 401(k) plan contributions: The money you contribute from each paycheck is subtracted from your current taxable income. That means you pay less in taxes each year, while your 401(k) account has the opportunity to grow — also tax-deferred — every year until you withdraw the money.[2] Since it's a retirement plan, presumably you'll be retired when you start taking withdrawals and your income tax rate could be lower.

Remember Jane from above? Since Jane is 50 and makes $75,000 per year, she can contribute as much as 41% of her income to max out her contribution limit in 2025. While that may be significantly more than she wants to save, it's still a good idea for her to evaluate her household income and see if it makes sense to change her deferral percentage this year. For example, if she had income from other sources outside of work, she may want to increase her contributions to reduce her taxable income on this year's tax return.*

If you aren't already maxing out your 401(k) plan contribution, here are some ideas to help you move in that direction:

- Seek to increase your deferral rate gradually, such as every time you receive a raise, promotion or bonus. This way, you can save more without reducing the amount you take home. However, ensure that any adjustment to your deferral rate won't lead to you exceeding the annual contribution limit.
- Consider increasing your deferral rate by one percentage point each year. Some companies implement an automatic escalation feature, so make sure you know your employer's policy beforehand.
- Perhaps the best time to increase your deferral rate is during your employer's annual enrollment period — when you're considering other benefits and taking a good look at your household budget.

## Strategy #3: Make It Last Longer

These days, it's not unusual for retirement to last 30 years or more. For many people, that's longer than they've accumulated enough savings to support them. One way to augment your retirement income plan may be to purchase an annuity contract. Most annuity contracts offer the option to convert your principal into a stream of income guaranteed (by the issuing company) for the rest of your life.

In recent years, some employers have begun offering an annuity option within their 401(k) plan. This is a little ironic since 401(k)s were meant to supplant the traditional, defined-benefit pension plan, but that's similar to how an annuity option works. With an annuity, however, the guarantees are backed by the insurance company, not the employer.

The SECURE Act of 2019 contained provisions designed to encourage companies to offer an insurer-issued retirement annuity option by limiting the employer's liability to provide annuity payouts.[3] Slowly but surely, many 401(k) plan providers have begun to adopt an annuity option. One of the features of an employer-sponsored annuity option is that every year, each participant receives a customized estimate of the monthly income expected in retirement based on the current annuity account balance.

Note that you may purchase an annuity either within a 401(k) plan or separately from a licensed financial professional. However, some potential drawbacks exist with annuities, including:[4]

- Higher fees than mutual funds and other types of investments
- Potential early surrender charges for access to funds
- A 10% early withdrawal penalty
- The annuity's guaranteed payout is based on several factors, such as interest rates, the balance accumulated and the participant's age when she starts drawing income

Despite the drawbacks, an annuity option is a way to make your retirement savings continue paying out income regardless of how long you live.

## Strategy #4: Temper Volatility

While a substantial allocation to stocks offers greater potential for growth, it also increases the risk of loss. The investment markets are always subject to dramatic swings, so one of the best ways to help temper that volatility is by appropriately diversifying your assets based on your financial goals, investment timeline and

tolerance for market risk.

Fortunately, most employer-sponsored plans offer a wide array of stock and bond mutual funds and exchange-traded funds (ETFs), as well as cash instruments. Spreading your contributions across a strategic allocation of these options can help protect your account from periodic market declines.

As a general rule, young adults are advised to invest a higher allocation to stocks, and that allocation may grow more conservative over time as they get closer to retirement age. The closer you get to retirement, the more you want to protect your investment from a market downturn — as there is less time to recover large losses.

## Remember to Rebalance

Once you select your 401(k) investment allocation (for example, 50% stock fund, 40% bond fund, 10% money market fund), it's important to rebalance that mix periodically to help keep your investments on track with your goals and comfort with market risk. For example, should your stock fund outperform and represent 65% of your overall retirement portfolio, you may want to sell off some of those gains and reinvest the proceeds in your bond and cash funds. Note that since you are buying and selling within the tax umbrella of an employer-sponsored plan, you won't incur taxes on capital gains because rebalancing isn't the same as withdrawing money.[5]

## Strategy #5: Optimize Taxes

The day will come when you need to begin withdrawing your plan assets for retirement income. At that time, all of the money distributed will be taxed at your then-income-tax rate determined by all of your retirement income sources, including Social Security, pension benefits and any taxable investment income.

But not all retirement investments generate income taxes. For example, Roth IRA contributions are made on a post-tax basis. Not only are contributions not taxed again, but investment gains grow tax free. While an employer-sponsored plan offers the opportunity to save taxes on current income throughout your career, the Roth IRA can save money on income taxes when you're in retirement.

It may be a good idea to diversify your income tax liability so that not everything you receive in retirement is taxable. One way to do this is to transition portions of your tax-deferred assets into a Roth as you approach your retirement date. You will have to pay income taxes as the money is converted, but it's likely best to pay those taxes while you're still working. Then once you retire, you won't owe any taxes on Roth distributions.[6]

If you decide to convert assets to a Roth IRA, consider doing so incrementally so that you don't tip your income into a higher bracket in any one tax year. Also think about converting during market declines. That way, you'll pay less in taxes but have the opportunity to recoup losses on a tax-free basis in the Roth. Some employer-sponsored plans allow in-service withdrawals or an in-plan Roth conversion. It's important to check with your plan's rules and work with an experienced financial professional if you're considering a Roth conversion.

## Final Thoughts

An employer-sponsored plan can be an excellent accumulation vehicle for retirement income, as well as a tax-savings benefit for employees. If you do nothing but set your deferral rate to your employer's match, pick a target-date fund and ignore it until you retire, you're already reaping some of the benefits.

However, with a little effort and strategic planning, you can get your plan to work harder to help pursue your retirement goals. It's important to discuss your employer-sponsored plan with your financial advisor as part of your overall investment portfolio — even if he or she does not actively manage those assets. This helps ensure your investments do not overlap and are appropriately allocated and diversified. It's also helpful in developing a distribution plan for your retirement income that potentially helps minimize your tax bill and addresses your needs for growth, risk management and a long, fulfilling retirement.

*This is a hypothetical example provided for illustrative purposes only; it does not represent a real-life scenario and should not be construed as advice designed to meet the particular needs of an individual's situation. Past performance is not indicative of future performance.*

*Sources*

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[6] IRS. Oct. 28, 2024. "Topic no. 451, Individual retirement arrangements (IRAs)." https://www.irs.gov/taxtopics/tc451. Accessed Feb. 6, 2025.

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