Everything you need to know about a 401(k)

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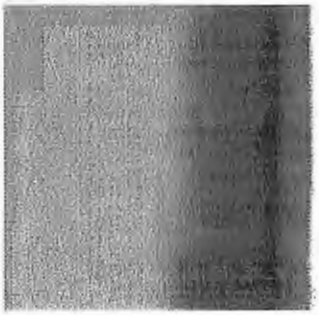

We've all heard of a 401(k), but how much do you really know? A recent CNBC survey reported that 63% of Americans are confused by 401(k) plans and it's hard to blame them.[1] After all, between contribution amounts, fund allocations, employer matching[2], tax implications, and rollovers, participating in a 401(k) can sound more like a headache and less like a helpful path towards a successful retirement. Thankfully, it doesn't have to be.

To help get you started and alleviate any stress we spoke with John Hancock's Head of Financial Planning, Misty Lynch, CFP®, to get the 411 on 401(k)s.

What is a 401(k)?

A 401(k) is a retirement plan offered by your employer that gives you the option to contribute a percentage of your salary on a tax-deferred basis. Depending on your target retirement date and financial needs, you can choose the type of investment funds within the plan that makes the most fiscal sense—from conservative to aggressive. You can also choose how much of your paycheck to invest and how frequently you wish to contribute throughout the year. Your investments may grow over time and when you turn 59½, you may be able to withdraw these

How can you get started?

If your company offers a 401(k), all it takes is some paperwork to sign up and human resources is available to guide you through the process. Once you've enrolled, you'll be able to select a contribution amount and the investment funds you wish your contributions to be allocated. Plus, your 401(k) can be accessed online, where you can monitor contributions, growth, and

How do you choose?

A 401(k) offers several funds for you to invest your contributions. Every plan is different, but funds typically include a specific blend of stocks and bonds. Depending on your appetite for risk and growth, you may choose a fund with a higher percentage of stocks to bonds or vice versa. If you'd like to maximize the different funds offered by your 401(k), you can choose investments that best suit your preference and continually refine your funds to optimize your returns. By the same token, you can choose funds by your targeted retirement date for a portfolio that adjusts its asset mix over time. For advice on which 401(k) funds make the most sense for you, you can see what resources your plan offers for advice or speak to a financial advisor. Remember, there is no guarantee that any investment strategy will achieve its objectives. Diversification does not guarantee a profit or eliminate the risk of a loss. The target date is the expected year in which investors in a target-date portfolio plan to retire and no longer make contributions. The investment strategy of these portfolios is designed to become more conservative over time as the target date approaches (or, if applicable, passes) the target retirement date. Investors should examine the asset allocation of the portfolio to ensure it is

How do contributions work?

A 401(k) gives you the ability to contribute a percentage of your pre-tax earnings, deducted from your paycheck, and deposited right into your retirement account, potentially reducing taxable income and growing tax free until withdrawn, typically at retirement3. For example, if you earn $50,000 a year and contribute 10% to your 401(k), at the year's end, your taxable income will be $45,000 and your 401(k) contributions will be $5,000 (10% of your salary). Please note that while your contributions aren't taxed, they are limited—the IRS changes the amount from year to year, but the 2019 limit for individual contributions is $19,000. If you have excess income, an FA could advise you on additional qualified and non-qualified investment opportunities.

How much should you contribute?

Everyone has different financial needs, but here's a golden rule: Whatever percentage your employer is willing to match, try to take full advantage of it. Anything less, and you could be leaving money on the table. Additionally, if financially possible, you may want to max out your

How often should you change your contributions?

Having children, buying a new house, sending your kids to college, or covering emergency expenses might change what you're comfortable contributing. It's also worth considering an increase to your contributions when you won't necessarily feel the change, like when you get a

What happens to your 401(k) if you leave your job?

It's entirely dependent on your circumstances. If your 401(k) balance is less than $5,000, your company may remove you from their plan and send you a check, unless you elect otherwise to ***roll this money into an IRA or your new employer's 401(k) plan*** —both of these options are not taxed. If you receive and cash a distribution check and are younger than 59½, you'll pay both federal and state taxes, as well as a 10% penalty imposed by the IRS.

What if you need your 401(k) before you turn 59½?

Unfortunately, the IRS imposes a 10% penalty for early withdrawal. However, there are certain exceptions—e.g. if you are disabled—that allow you to receive your money penalty-free. To see if you qualify for a hardship withdrawal, you can speak with a financial advisor, an

What's the most important thing to know about a 401(k)?

A 401(k) has different components that you'll need to manage in order to maximize your retirement savings opportunities. You will need to monitor your contribution rate and investment choices to ensure they are aligned with your financial goals, your stage in life, and your risk

With steady contributions and some employer matching along the way, a 401(k) can be a great way to create your plan for amazing. Speak with a John Hancock Financial Advisor today to build a plan that works as hard as you do.