

INVESTMENTS



value of your principal. A core intermediate-term bond fund can fit the bill. A few favorites among Morningstar analysts include Dodge & Cox Income (DO-DIX), Fidelity Total Bond (FTBFX), and Metropolitan West Total Return Bond (MWTRX).

If you have an even longer time horizon — anywhere between five and 10 years — you can hold stocks as well as bonds. Morningstar analysts like Vanguard Wellesley Income (VWINX) and Dodge & Cox Balanced (DODBX), which combine stocks and bonds together. If you hold one of these funds and are getting close to needing money to fund your goal, you can transition the assets to cash for safe-keeping.

DAY 8: IDENTIFY THE RIGHT VEHICLE FOR COLLEGE SAVINGS
Degree of difficulty: Moderate

As with retirement investments, the college-savings landscape is far more cluttered and complicated than it needs to be, with myriad vehicles competing for investors' attention.

Due to their generous contribution limits and the potential for tax-free withdrawals, section 529 college-savings plans have emerged as the vehicle of choice for families looking to sock away a substantial sum for school. 529s have generally improved substantially in the past few years, with costs coming down and the quality of investment options going up. To see how these college-savings plan compare, consult Morningstar's annual 529 Plan Ratings (morningstar.com/save-for-college.html).

Some investors, however, would like to invest for their kids outside the confines of a dedicated college-savings vehicle like a 529 or Coverdell Education Savings Account. If that's you, you have a couple of different options. Setting up a UGMA/UTMA account is one simple way to go, but the drawbacks probably outweigh the pluses, in my view.

The assets become the property of the child once he or she reaches the age of majority (varies by state but usually age 18 or 21), when some young people may not yet be equipped to make good financial decisions. And if you're pretty sure your child is college-bound, you should know that those UGMA/UTMA assets will work against your child in financial aid calculations.

For those reasons, investors looking to save outside of a dedicated college-funding vehicle like a 529 or Coverdell should consider saving for their kids in one of a couple ways. The first simply would be to hold tax-efficient investments, such as low-turnover exchange-traded and index funds, individual non-dividend-paying stocks, municipal bonds/funds or tax-managed mutual funds, within the confines of the parents' taxable account. Withdrawals won't be

tax-free, as is the case with qualified withdrawals from a Coverdell or 529, but it's straightforward and investors gain the added flexibility to use the money outside of college expenses — penalty free — if the need arises.

Another option is to use a Roth IRA to save for your kids. In a Roth, you can pull out your contributions (not your gains), tax-free, at any time and for any reason, making the vehicle a great multi-tasker for those looking to save for retirement and college at once.

The key drawbacks? Roth contribution limits are pretty low — currently \$5,500 for those under 50 and \$6,500 for those over — and pulling money out for your kids leaves less money at work for retirement.

DAY 9: INVEST YOUR COLLEGE-SAVINGS ASSETS
Degree of difficulty: Moderate

The bear market of 2008 forced many retirees and pre-retirees to recalibrate their plans and, in some cases, to make meaningful reductions in their spending. But it also had a huge impact on another, much younger group: college-bound students.

Unfortunately, many college-savings plans, including several professionally run 529s, were far too skewed toward stocks in the later stages of their investment paths at that time, resulting in big savings shortfalls for students getting close to college.

If that experience had a silver lining, though, it was that it underscored the importance of holding on to what you already have versus gunning for big returns in your child's college-savings plan, particularly as college draws near.

Many of the investment pros running 529 college-savings programs have scaled back the equity holdings of their age-based options to make them more conservative, and they added index funds in place of poorly chosen actively managed funds, in the hopes of reducing the risk of a big shortfall at the worst possible time.

Investors managing the asset allocations of their own college-savings programs also should take the lessons of 2008 to heart. Here are a few quick tips:

- By the time your child hits the teenage years, more than 50 percent of his or her college fund should be in bonds and cash.
- By the time your child is a junior or senior in high school, equities should compose only a small slice (less than 20 percent) of his or her college dough.

If you have to boost your college savings using a combination of financial aid, student loans or work-study, it's better than risking the money you have been able to set aside.

DAY 10: DECIDE BETWEEN ROTH AND TRADITIONAL CONTRIBUTIONS FOR RETIREMENT SAVINGS
Degree of difficulty: Moderate

Investors who are socking money away for retirement are apt to hit a fork in the road: Should they make traditional or Roth contributions? Investors in a traditional 401(k) will be able to contribute pretax dollars to their accounts; investors in a traditional IRA may be able to deduct their contributions if their income falls below the income limits. Investors in both traditional 401(k)s and IRAs also can take advantage of tax-deferred compounding. That sounds compelling, but the downside of building traditional 401(k) or IRA assets is that the money is taxable upon withdrawal in retirement.

Roth contributions, whether to a 401(k) or IRA, receive exactly the opposite tax treatment: There aren't any tax breaks on contributions, but the money compounds on a tax-free basis and may be withdrawn in retirement without any taxes, too. (There are no income limits on 401(k) contributions, either Roth or traditional, but income limits apply to Roth IRA contributions. Single taxpayers can make at least a partial Roth IRA contribution if their income is less than \$135,000; for married couples filing jointly, that threshold is \$199,000.)

The right answer rests on one big swing factor: whether you expect to be in a higher tax bracket in retirement than you are now. But unless you're quite close to retirement, the answer to that question is all but unknowable.

However, a few categories of individuals are good candidates for making all or at least part of their 401(k) contributions Roth-style. The first would be younger savers who aren't earning a lot currently but may do so in the future. For them, their own earnings trajectory, plus the possibility that future tax rates will trend higher across the board, make a strong argument for a Roth 401(k) and IRA.

Another good candidate for Roth assets is the upper-income individual who has a lot of retirement assets sitting in a traditional 401(k) and/or IRA. Opting for Roth contributions or even undertaking a conversion can give such individuals the opportunity to hedge their bets: If tax rates trend higher in the future, or they're in a higher tax bracket in retirement than they were in their accumulation years, they'll be glad they took the hit by making Roth contributions when tax rates were lower. On the flipside, investors who haven't saved much for retirement and can make a deductible traditional IRA contribution may be better off with that type of IRA. It's unlikely that their tax bracket will be higher than it is when they're working, so they're better off pocketing the tax break now.

DAY 11: CHECK UP ON THE QUALITY OF YOUR COMPANY RETIREMENT PLAN
Degree of difficulty: Moderate to difficult

If you're earning a match on your 401(k) plan contributions, it's a no-brainer to invest at least enough to earn the match. But what if your company isn't matching, or if you'd like to make a larger contribution to your retirement than you're being matched on? Is it best to stick with the 401(k) or turn to another vehicle like a Roth IRA?

The answer to that question depends, at least in part, on the quality of your plan. To help determine whether your plan is worth investing in or is a stinker, ask your HR administrator for a document called a Summary Plan Description, which lays out crucial information about your 401(k).

Beware: This document is apt to be crammed with legalese and not likely to be easy reading. But after a little bit of hunting, you should be able to locate your plan's administrative expenses. These fees may be depicted in percentage or dollar terms; if the latter, divide your plan's costs by the total dollars in the plan. If your plan doesn't have any additional administrative costs, that's a good sign. But if it layers on additional administrative fees that amount to 0.50 percent or more per year, that's a red flag that your plan is a costly one. Check to see whether your plan includes other bells and whistles, such as a brokerage window, which allows you to invest in options outside the plan; the ability to take a loan; and the ability to make Roth 401(k) contributions.

After that, conduct a quick checkup of the breadth and quality of your plan's holdings using the data and Analyst Reports on Morningstar.com. Look for a good array of core-type funds: large-cap U.S. and foreign stock offerings, balanced funds and core intermediate-term bond funds. For stock funds, look for expense ratios of less (preferably much less) than 1 percent per year, though specialized funds like international and small-cap offerings may charge a touch more. For bond funds, expense ratios of less than 0.75 percent are ideal.

If your plan checks out well on the above measures, funding it up to the maximum allowable level is apt to be a good use of your cash, thanks to the tax-deferred compounding that company-retirement plans afford. Before doing so, however, you also should deploy some of your retirement assets into an IRA. You can start and maintain an IRA with very low to no administrative expenses, and you also can access a broader range of investments than you can when investing inside of a company retirement plan like a 401(k).

DAY 12: MAXIMIZE YOUR MATCH
Degree of difficulty: Easy

If you're not earning any matching funds on your 401(k), my usual advice is to fund an IRA up to the maximum allowable level first. The reason is that you can put any investment you'd like into an IRA, and you won't have to pay any additional administrative expenses to invest in one, in contrast with many 401(k) plans. IRA investors also enjoy tax breaks that parallel 401(k)s. If you find yourself with additional assets to invest after that, turn to your 401(k) (provided it's a good one).

If you are lucky enough to earn matching contributions on your 401(k), plan to take advantage of each and every one of those dollars. This is particularly relevant if you're highly compensated and/or you expect to receive a large bonus early in the year. That's because many companies make matching contributions throughout the year, but if you hit your allowable 401(k) contribution well before year-end, you won't be able to take full advantage of any matching contributions your employer would've made in the remainder of the year. (Some companies make an adjustment to help employees receive a match on their full 401(k) contributions regardless of when those contributions were made, but others do not.)

If this is a potential issue for you, you'll need to lower your contribution rate per paycheck to ensure that you don't reach your maximum contribution too early in the year. People who receive large bonuses may be especially vulnerable to missing out on matching contributions; they usually can correct this issue by lowering the percentage of their bonus that goes toward their 401(k).

DAY 13: USE AN IRA TO IMPROVE YOUR PORTFOLIO
Degree of difficulty: Easy

If you have most of your retirement assets in a company-retirement plan and are using an IRA to supplement what you already have, you can use your IRA in one of two ways.

You can hold core-type investments, which tend to be mainstays in most 401(k) plans: index stock and bond funds, large-cap actively managed funds, balanced funds and so forth.

Alternatively, you can use your IRA to fill holes in your company retirement plan. For example, say your plan includes adequate stock funds, but its bond funds charge more than 1 percent per year in annual expenses — sure to cut into your long-term returns. If that's the case, you can fill your company retirement plan with the decent stock funds and leave the bond