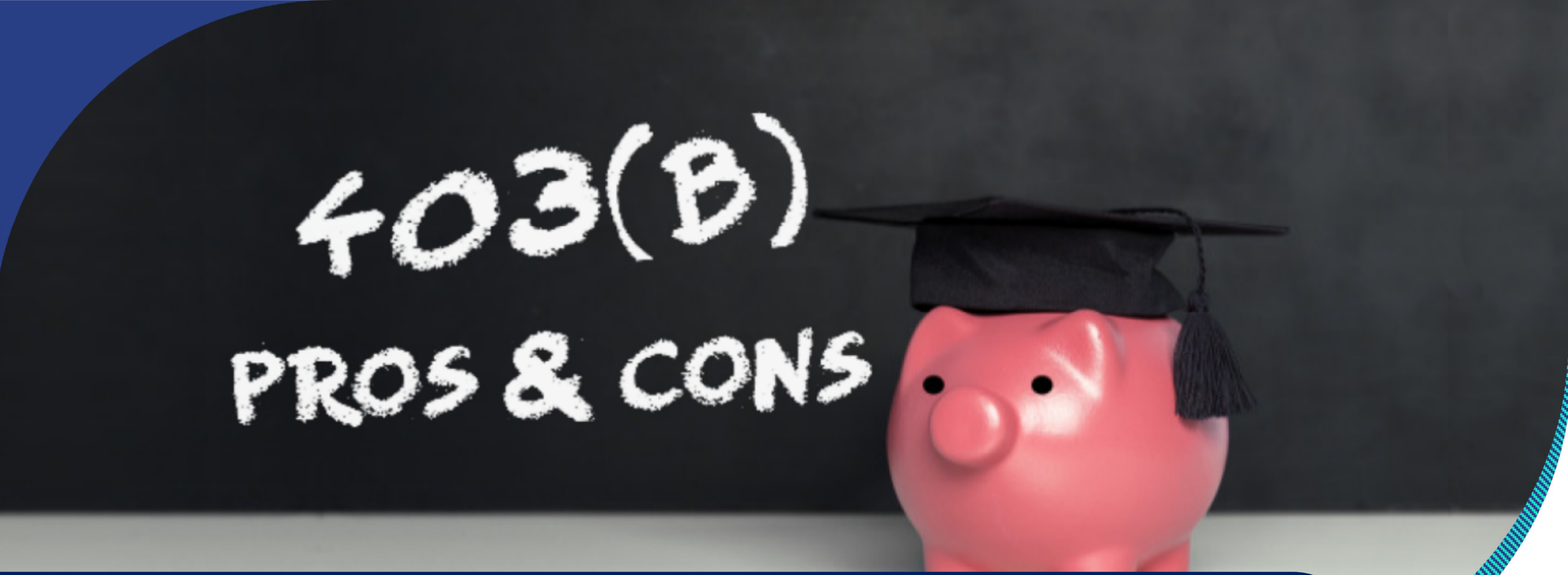

403(b) Plan Pros & Cons for State & County Employees

A 403(b) plan is a retirement plan designed for specific employees of public schools, tax-exempt organizations, and certain religious organizations.

The Basics of 403(b) Plans

First let's review some of the basics of a 403(b). A 403(b) plan can be a good way to save for retirement because typically money goes in tax-free. Normally taxes come out of your salary before you are paid, with a 403(b) contribution the money is invested, without taxes coming out first. There's a catch of course, tax is then paid when the money is taken out, which is typically, in retirement.

Importantly, that deal can work out well for you for two reasons. First, most people will be in a lower tax bracket in retirement, assuming no major changes to the tax code between now and then. So, your 403(b) contributions may have less tax taken out in the long run. That's good news for you. Of course, if you expect to be in a higher tax bracket in retirement, then a 403(b) may not be a good option for you.

Also, along the way to retirement, the money in a 403(b) can grow tax-deferred, which can boost your after-tax returns. Basically, your money will generally grow faster if the IRS isn't taking a share of profits and dividends each year, as it would if your money were just in a normal brokerage account without any special tax arrangements. The math can get a little complex, but if you're paying tax at the end rather than along the way, then that can help your money grow due to compounding on the amount that you would have paid in tax.

403(b) Plans - The Good and Bad

There are good and bad 403(b) plans out there. A few indicators your 403(b) plan could be less desirable. Firstly, a good 403(b) should offer some low-cost, passive investment options such as Exchange Traded Funds (ETFs)[1]. If you're paying more than 0.50% a year in expense ratios for different funds (and, generally, the lower the better), then your plan may not have great investment options. Secondly, if someone is aggressively selling the plan to you, then that's a bad sign too. Thirdly, many 403(b) plans don't have ERISA protection (Employee Retirement Income Security Act), that's a potential problem because ERISA promotes minimum standards for retirement plans, an ERISA plan isn't fool proof, but it puts some helpful safeguards in place for savers.

> "Don't save what is left after spending; spend what is left after saving."
> – Warren Buffet

The best 403(b) plans are low-cost with a broad range of asset classes and probably won't have enough of a marketing budget from their relatively low fees for salespeople to chase you down. Some of the worst plans can involve complex products involving insurance and annuities. While these may sound appealing and can be appropriate for some people, for many, these can be complicated and expensive options with the various costs eliminating any potential tax benefit.

So, if your 403(b) plan has a range of low-cost investment options, it may be a tax-efficient way to save. If it is limited to annuities and insurance offered by salespeople, then it may make sense to skip it. If your plan is covered by the Employee Retirement Income Security Act (ERISA) which requires your employer to ensure your investment choices are of high quality, then that's a bonus, if it's not then you probably want to do a little more homework on whether it's a good plan.

What to Pick Within a 403(b)?

There is no one size fits all way to invest. Generally picking lower cost funds that diversify[2] across different countries and industries is a good idea, as is having some bond and stock representation, since these two assets can move in different directions over time depending on the economic situation, helping smooth performance.

Good asset classes to consider within a fund portfolio can include diversified U.S. bonds; diversified U.S. stocks; some international stock exposure and Treasury Inflation Protected Securities (TIPS) though it's unlikely that your 403(b) has exactly these options. Also, how you want to weight your exposure between these, and other options will depend on things such as your age, risk tolerance and when you expect to retire.

Catch Up Provisions - Can Be Generous for Long-Serving Employees

If you're over 50, 403(b) plans enable you to contribute more in your retirement plan, just as a 401(k) would. However, if you've been with your plan for 15 years, then you may be able to contribute even more in your plan. This can be helpful if you have an attractive 403(b) plan and are behind on retirement savings.

More Flexibility on Using the Money Before Retirement

It may also be possible to use 403(b) plans before retirement if you leave your employer offering a 403(b) plan. Generally it is best to keep retirement money for retirement, as that's when you are more likely to need the money, but whereas 401(k) early withdrawals can be more limited and incur penalties, the rules surrounding 403(b) withdrawals if you're no longer with the employer that offered the plan can be more flexible.

[1] ***Mutual Funds and Exchange Traded Funds (ETF's) are sold by prospectus. Please consider the investment objectives, risks, charges, and expenses carefully before investing. The prospectus, which contains this and other information about the investment company, can be obtained from the Fund Company or your financial professional. Be sure to read the prospectus carefully before deciding whether to invest.***

[2] Diversification does not guarantee a profit or protect against a loss in a declining market. It is a method used to help manage investment risk.

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The DROPBASICS Retirement Planning Program was designed by career retirement plan service professionals to improve outcomes of participants in the Florida Deferred Retirement Option Program (DROP). The technology infrastructure provides a fully responsive experience, so users can access tools on any devices. Our intuitive user interface and core features enable users to easy access to information without the confusing and unnecessary bells and whistles of other websites.

The right advice can help individuals to better reach their financial goals. Our investment advisory partners can make quality investment advice accessible to all investors, regardless of account size.

Retirement planning can be confusing, which causes many individual investors to make poor decisions. This is exacerbated in the absence of good investment advice. The right advice may make the difference between a comfortable retirement and a struggle.

Click to Get Help

Summary

So, 403(b) plans are more of a mixed bag due to lack of minimum ERISA standards, whereas 401(k) plans typically clear a higher bar. Nonetheless, they can be a good way to save for retirement, especially if the investment options are relatively low cost. If your 403(b) plan offers annuities and insurance rather than other investment options, that could be a red flag. 403(b) plans are generally similar in terms of rules to 401(k) plans, but there may be more flexibility around withdrawals and catch-up contributions for longer term employees.

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