



## SALARY CENTER

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### **Budget Your 2006 Bonus**

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Memo to Americans: As a group, you saved negatively in 2005, spending 100.5 percent of your after-tax income, according to the Commerce Department. You took on debt or raided savings to make ends meet -- or load up on [bling](#).

Why bring up this unpleasant fact? Because if you're anticipating an annual bonus this year, you should probably skip the cruise. Considering [salary increases](#) are barely keeping pace with inflation, no wonder white-collar workers are coveting those bonuses to help cover both wants and needs.

"The temptation to blow the whole wad on a junket to a sunny locale or on a big TV is enormous," says Ellen Weiss, a spokeswoman for financial advisory firm Leonetti & Associates.

What principle should guide you as you allocate your bonus? "Put yourself in a better position with this money than you were before," says financial planner Marc Sussman. Here's how:

#### **Identify Your Financial Priorities**

How you order your financial priorities "really depends on where you are in life," says Darrell Canby, president of Canby Financial Advisors. But for the average overspending American worker, these are the most important financial moves to consider when a bonus lands in your bank account:

- **Pay Uncle Sam:** Even though your employer withholds money from your bonus as legally required, you might owe additional state and federal taxes. Determine your tax liability before proceeding -- no investment is better than the one that keeps you out of federal prison.
- **Create or Bulk Up a Savings Account:** Emergencies happen, but they get a lot more expensive if you have to pay for them with a credit card advance at 24 percent interest. Experts advise keeping at least three months' income in the bank to avoid such credit card calamities.
- **Eliminate Expensive Debt:** Address any credit card balances in order of financial destructiveness. "If you have any credit card debt, apply the bonus to your highest balance or to the card with the highest interest rate," says Cate Williams, vice president of financial literacy for nonprofit debt-counseling firm Money Management International.
- **Invest in Retirement:** Making an extra mortgage payment to move up your debt-free date is tempting, but it's not always the best way to use your bonus. "I'd rather see people put money into retirement than pay off a mortgage," Williams says. If you didn't contribute enough to your 401k last year, be sure to do it this year. If you must, set aside your bonus in a savings account to allow for higher 401k payroll

deductions.

Are you 50-plus and already contribute the maximum to your 401k? Consider using your bonus to make a [catch-up contribution](#) [catch-up\\_contributions.html](#), a retirement investment vehicle designed for the typical Baby Boomer, who hasn't put aside nearly enough. For tax year 2005, the 401k catch-up limit is \$4,000; for IRAs, it's \$4,500.

- **Save for Your Children's Education -- or Your Own:** Retirement should take priority, but investing for education is important, too. Money squirreled away for years in a tax-advantaged vehicle, such as a [529 plan](#), can accumulate and keep pace with rapidly rising college tuitions.

- **Put the Money Toward Your Freedom:** Save for a career change, whether to pay for further education or start your own business. "A worker should put the money into a personal 'freedom fund,' where it can finance some future move up the success ladder," says Rob Bennett, author of *Passion Saving: The Path to Plentiful Free Time and Soul-Satisfying Work*.

- **Live Large -- At Least for One Night:** Do set aside a little money for a dinner out with the smart set or whatever satisfies your urge to consume conspicuously. This will help keep you motivated to earn a big bonus next year -- which you're probably already counting on.

- **Give It Away:** While you may not be totally happy with your bonus or salary this year, rest assured you're doing better than a lot of other people. Find a cause that speaks to you, and dip into your pockets for a related charity. Both getting and giving help make society function smoothly.

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