



and shareBUILDER 401K present

Six Rules

for Making Smart Investment Choices

"Most investors, both institutional and individual, will find that the best way to own common stocks is through an **index fund that charges minimal fees**. Those following this path are sure to beat the net results (after fees and expenses) delivered by the great majority of investment choices." *

— Warren E. Buffet
1996 Annual Report of
Berkshire Hathaway Corporation

* It's important to remember that investing in stocks, bonds, and even money market instruments involves risk. Markets are unpredictable and may or may not act in the future the way they have in the past. Investing over time does not assure a profit or guarantee against a loss.

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401(k) plans are: Not FDIC insured · Not bank guaranteed · May lose value

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“I’m ready to save. Now what do I do?”

Anyone who has ever set up a 401k account has asked these important and challenging questions...

“Should I buy funds made up of stocks, bonds, or a money-market — or all three?”

“What’s the right choice for me?”

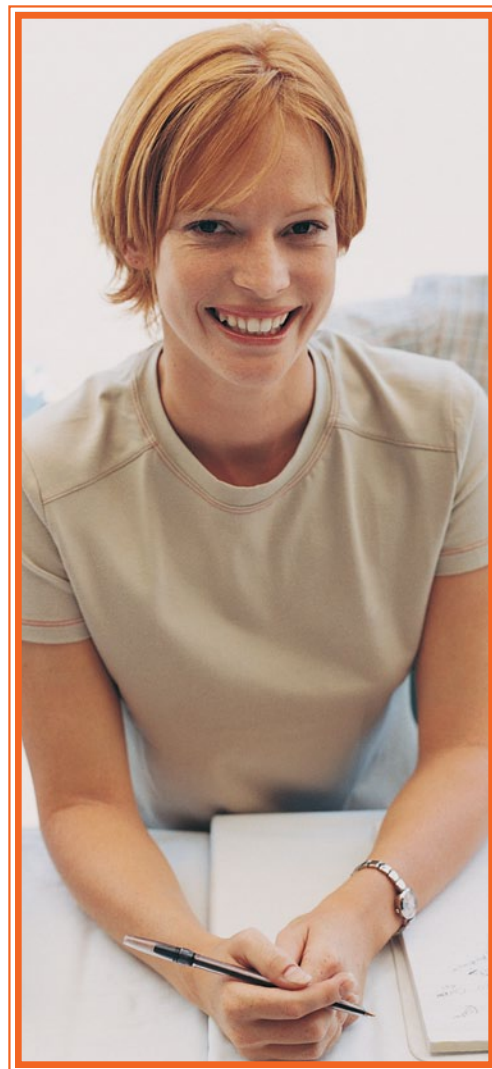
“How many funds do I really need?”

And that’s just for starters!

Yes, investing can seem intimidating. But we’re convinced that if you make diversified and cost-efficient choices, you can find it easy, and even fun, to save for tomorrow.

If you haven’t done so already, may we suggest that you read the companion guide titled *Five Rules for Creating a Sound Investment Strategy*. It contains useful information on how to allocate your savings among the various asset classes.

The guide you’re reading now will provide you with some important background information and explain how to choose the right types of investments and create a portfolio mix designed to help you meet your savings goals.



An important word about risk: It’s important to remember that investing in stocks involves risk. Markets may or may not act in the future the way they have in the past. However, we believe that by following sound principles and applying them consistently over time, you can get on track to meet your goals and achieve financial peace of mind.

RULE

1

Select **index-based** funds for maximum diversification.

ShareBuilder 401k advocates using index-based investments for your long-term savings plans. Why? Because index-based funds tend to be well-diversified and have low expense ratios, so your money can work harder over time. We believe this so strongly that our entire ShareBuilder 401k offering is comprised of a particular kind of index-based funds called Exchange Traded Funds (ETFs).

Index-based funds hold a portfolio of securities or bonds that work to mirror those comprising a market index (like the Dow Jones Industrial Average or the S&P 500). The goal of these funds is to match the performance of the index it tracks, less the costs needed to run the fund (the expense ratio).

Investments that track the major indexes are by their nature diversified, which means you're not putting all your eggs in one basket.



RULE 2

Costs really do matter.

Index-based funds also offer the great advantage of cost efficiency. The following example illustrates why costs matter so much and why knowing the expense ratios of your investment selections is so critical.

Consider these results: From 1980–2005, the S&P index-based mutual funds averaged 12.3% net return (12.5% gross return less 0.2% expense ratio). The average mutual fund provided a net return of 10.0% during the same period. In other words, **investors gained a 2.3% advantage by owning the index-based funds.**

Compare how this adds up over time for a single \$1,000 investment made in 1980:

Net Return of \$1,000 (1980–2005) ¹	
S&P Mutual Index Fund	\$17,080
Average Mutual Fund	<u>\$9,820</u>
Advantage:	\$7,260

IMPORTANT: Costs can be a real drag on your fund’s ability to produce outstanding results for you. The reason index-based funds are cost-efficient is that you’re not paying for an expensive active fund manager or the extra costs associated with higher portfolio turnover that are more typical in actively-managed funds.

Because actively-managed funds often charge expenses that are 1–2% above those of their index-based fund peers, **index-based funds can be tough to beat over the long run.**

¹ Investment Choices and Human Values, Bogle Financial Markets Research Center, April 2006

Note: The important assumptions in the comparison above are that all returns are reinvested, and that data does not include tax considerations. The data cited here represents past performance, which is not a guarantee of future results. Investment returns do and will fluctuate. Current performance may be lower or higher than the performance data cited.

RULE 3

Keep it simple with a few **well-diversified** funds.

Don't worry — if you're confused about which investments to make, you're not alone. It should come as no surprise that many people find it hard to make investment decisions.

Some providers offer over 100 options in their 401ks alone. Invest at any retail brokerage and you can face over 10,000 investment products! The simple fact is, you can have a prudent, well-diversified savings plan with just **one** investment, often referred to as a model portfolio.

A closer look at model portfolios. Model portfolios consist of a specially selected basket of funds, allocated across stocks, bond, and cash instruments in different ways. Model portfolios are developed and balanced to meet the needs of specific investor profiles that take into account your risk tolerance and time horizon until retirement. (See the *Three Sample Portfolios to Consider* section on page 7 of this guide for more information.)

You may have heard of **target** or **life-cycle funds**. These are a form of model portfolios that adjust asset allocations as you get closer to actually using your funds in retirement.

For those that prefer to choose their own investments, a well-diversified selection strategy might be to choose one broad stock market index-based fund and one bond market index-based fund.



RULE

4

Choose the **right mix** of stocks and bonds.

Asset allocation simply refers to the process of deciding how much of your money goes into which kind of investments — stocks, bonds, or cash. Experts and respected studies indicate that **your asset allocation is the most important decision** you'll have to make. It's even more important than choosing specific funds.

Some important performance facts. Since 1926, U.S. stocks have delivered 10.4% returns, bonds 5.4%, and cash 2%.¹ And since 1960, inflation has averaged 4% a year. It stands to reason that a sizeable amount of your investment should be in stocks.

Watch out for volatility. Given the fact that stocks have historically provided better returns than bonds and cash, why wouldn't you put all your savings into stocks?

There are two answers to this question.

First, there's no guarantee of future returns. Past results are not a guarantee of future results.

Second, stocks have had years when returns were over 20%, and periods where they have declined 20% or more. Remember the Internet bubble that burst in 2000?

Because the stock market is volatile and bonds are often worth more in periods when stocks are going down (and vice versa), investing a percentage of your savings away from stocks is a good idea. You'd hate to reach retirement age at a time when stocks are down significantly and you have no other investments!

Put time on your side. It's a simple fact: the more time you have until retirement, the more time you have to travel safely through market ups and downs. A person in her mid-twenties might consider investing more in stocks — upwards of 90% — and just 10% in bonds. A person who is 62 and will be retiring in three years may be better served with an allocation of 60% in stocks and 40% in bonds. Remember, even at 65, you won't be accessing all of your stock funds for 10 or 20 years or more. This gives you some time to ride out the inevitable storms ahead.

What's your tolerance for risk? When it comes to investing, it's extremely important to know yourself. If you're uncomfortable seeing your savings swing with the markets, or lose value for a period of a year or more, you should build a more conservative portfolio comprised of perhaps 60% in bonds and 40% in stocks. If you take a conservative approach, you may not reach your goals quite as fast, but you'll likely sleep a whole lot better at night.

Three sample portfolios to consider. It's impossible to suggest a specific portfolio in this guide, because everyone's needs are different. Your specific time horizon, current financial situation, goals, and risk tolerance all have to be taken into account. Given this fact, we present below three **sample** portfolios for you to review. They are appropriate for people in different life stages. They demonstrate how ShareBuilder 401k funds can be used to align with a designated asset allocation goal to provide a custom financial solution for you.

Young Investor

Asset Allocation	Percent	Potential ShareBuilder 401k Funds	Fund Goal	Ticker
Domestic large-cap stocks	55%	SPDR Trust, Series 1	Seeks to mirror the S&P 500 Index	SPY
Domestic mid-cap stocks	15%	MidCap SPDR Trust, Series 1	Seeks to mirror the S&P Mid-Cap 400 Index	MDY
Domestic small-cap stocks	10%	iShares Russell 2000 Index	Seeks to mirror the Russell 2000 Index, a small-cap blend	IWM
Intermediate-term bonds	20%	iShares Barclays Aggregate Bond	Seeks to mirror the Barclays U.S. Aggregate Index of U.S. investment-grade bonds	AGG

Middle-Aged Investor

Asset Allocation	Percent	Potential ShareBuilder 401k Funds	Fund Goal	Ticker
Domestic large-cap stocks	50%	SPDR Trust, Series 1	Seeks to mirror the S&P 500 Index	SPY
Domestic mid-cap stocks	10%	MidCap SPDR Trust, Series 1	Seeks to mirror the S&P Mid-Cap 400 Index	MDY
Domestic small-cap stocks	5%	iShares Russell 2000 Index	Seeks to mirror the Russell 2000 Index, a small-cap blend	IWM
REITs (Real Estate Investment Trusts)	5%	iShares Cohen & Steers Realty Majors Index Fund	Seeks to mirror the Cohen & Steers Realty Majors Index	ICF
Intermediate-term bonds	30%	iShares Barclays Aggregate Bond	Seeks to mirror the Barclays U.S. Aggregate Index of U.S. investment-grade bonds	AGG

Retirement-Preparation Investor

Asset Allocation	Percent	Potential ShareBuilder 401k Funds	Fund Goal	Ticker
Domestic large-cap stocks	40%	SPDR Trust, Series 1	Seeks to mirror the S&P 500 Index	SPY
Domestic mid-cap stocks	10%	MidCap SPDR Trust, Series 1	Seeks to mirror the S&P Mid-Cap 400 Index	MDY
Domestic small-cap stocks	5%	iShares Russell 2000 Index	Seeks to mirror the Russell 2000 Index, a small-cap blend	IWM
REITs (Real Estate Investment Trusts)	5%	iShares Cohen & Steers Realty Majors Index Fund	Seeks to mirror the Cohen & Steers Realty Majors Index	ICF
Intermediate-term bonds	20%	iShares Barclays Aggregate Bond	Seeks to mirror the Barclays U.S. Aggregate Index of U.S. investment-grade bonds	AGG
Inflation-protected funds	20%	iShares Barclays TIPS Bond	Seeks to mirror the Barclays U.S. Treasury Inflation Notes Index	TIP

¹ Ibbotson Associates, a subsidiary of Morningstar Inc. The numbers referenced reflect returns for the S&P 500, U.S. government bonds, and cash from 1926 through 2005.

It's important to remember that investing in stocks, bonds, and even money market instruments involves risk. Markets are unpredictable and may or may not act in the future the way they have in the past. Investing over time does not assure a profit or guarantee against a loss.



RULE 5

Tax-advantaged accounts can save you money

For those who invest in non-tax-deferred accounts — i.e. outside of an IRA or 401k — taxes can really take a big bite. Between dividends and short-term and long-term capital gains, taxes can eat up an investor's return. The amount of turnover in a fund, and other factors outside of your control, contribute to the tax problem. A Charles Schwab study showed that high-tax-bracket investors can lose more than half of their returns to taxes in a non-tax-deferred account versus holding the same investments in a tax-deferred account like an IRA or 401k.¹

This is a major reason why most financial experts recommend 401ks and IRAs as the number one place to save for a secure retirement.

Tax advantages help you save more. With the government's blessing, 401ks and IRAs come with built-in tax advantages designed to make saving more attractive. Traditional 401ks are designed with three features that encourage participation and saving:

- 1. Your pre-tax contributions get a tax break today.** This means that the amount you contribute from your paycheck is not taxed. But once you withdraw that money in retirement, the government taxes it as income — growth and all.
- 2. Loans and hardship withdrawals are available.** The interest, though, must be paid back to your account. However, if you do not repay your loan to your 401k, those funds withdrawn before the age of 59½ are subject to taxes plus an additional 10% penalty. NOTE: We do not recommend taking loans from your 401k unless absolutely necessary as these loans will negatively affect retirement savings growth.
- 3. You can take your money with you.** If you leave (or are an owner who sells your company), you can move your funds to the 401k plan of your new company or move it to an IRA without any tax penalty. In other words, you can continue to save for retirement without incurring tax liabilities due to changing jobs.

How to enjoy a tax-free retirement. Thanks to the latest round of legislation, the Roth 401k is available as a permanent option for participants. A Roth 401k offers you and your employees the option to invest some or all of your paycheck contributions after taxes. You benefit because your Roth 401k contributions and earnings cannot be taxed again upon reaching retirement age. Any and all profits that were generated by these investments will grow tax-free. And unlike its IRA counterpart, there's no qualifying income limit.

So what's the catch? There is no catch, but your paycheck will take a bigger tax hit today. If you can afford to take the hit, you stand to benefit greatly come retirement when that money could really come in handy.

Does a Roth make sense for you? It all depends on whether you think you'll be in a higher tax bracket in retirement, and whether or not you can afford taking home less pay today. There are significant advantages to putting some or all of your contributions in a Roth 401k. The younger you are, the better off you'll probably be, since workers in their twenties and thirties are more likely to move up the ladder over time into higher-paying jobs. This means they're in the best position to benefit from compounded growth over time.

To see just how much more money you could make, let's take a look at two investors in a hypothetical example. Both are 45 years old, making \$75,000 annually, and both will retire at age 65 with a retirement span of 20 years. One chooses to put 8% of his income into a Roth 401k; the other opts to contribute 8% to a traditional 401k:

More Income in Retirement: Traditional Pre-Tax 401k or Roth 401k?²

Age 45 earning \$75K per year	Pre-tax 401k	Roth 401k	A look at the numbers
Take-home pay pre-retirement	\$1,035,120	\$1,005,120	Pre-tax 401k saves you \$30K, a monthly take-home pay advantage of \$369
Nest egg at age 65	\$294,510	\$294,510	Savings are the same, given the same contribution percentage and rate of return
Post-tax retirement income	\$502,560	\$591,120	Roth 401k will provide you with \$88,560 more in retirement
Advantage: Roth 401k		\$58,560	Roth wins this scenario with \$58,560 more for you to live on

In this simple example, the Roth investor comes out ahead by \$58,560. We strongly recommend you run some numbers of your own to see what makes the most sense for you. You may even wish to hedge and contribute to both types of account, so that you stand to benefit no matter where you end up.

¹ *Ranking Mutual Funds on an After-Tax Basis*, John Shoven and Joel Dickson, sponsored by Charles Schwab

² This hypothetical example assumes a fixed 8% annual return compounded annually over 20 years, a 25% tax rate pre-retirement, and a 15% tax rate post-retirement. The example also assumes a post-retirement horizon of an additional 20 years (age 85) for retirement income disbursement based on current tax and IRS rules. No matches or raises are factored in. Actual investment results can and do vary.

RULE

6

Put your **savings plan** on “autopilot”

Financial experts agree that the best way to make a savings plan work is to **make the process automatic**. Most people these days live hectic lives, which makes it hard to stay on top of your investments. That’s a great advantage of a 401k; it can put your savings plan on autopilot. This means that each pay period you’ll automatically contribute the amount you elect to your individual 401k account and into the specific investments you select. It couldn’t be easier!

Some providers even offer auto-rebalancing as a feature, so your asset allocation (how much you have in each investment) is reset to your desired mix or percentage. That’s another useful tool that can help you meet your goals.



Let's summarize the keys to making smart investment choices:

1. Select index-based funds for maximum diversification.
2. Costs really matter — select low expense-ratio funds (like ETFs).
3. Keep it simple — you only need a few well-diversified funds.
4. Choose the right mix of stocks and bonds for you.
5. Take advantage of 401k tax benefits.
6. Put your saving plan on “autopilot”.

We hope these tips have helped you get ready to invest and save with confidence. The process really isn't as hard or intimidating as “Wall Street” makes it seem. Just get started and discover for yourself how easy it is to start saving for a secure retirement.

Read our companion guide:

Five Rules For Creating a Sound Investment Strategy

It's loaded with practical, valuable information to help you put together your saving and investment plans. If you haven't read it yet, you can [download it now](#).

Other online resources:

- [Index investing tutorial](#)
- [Retirement planning tutorial](#)
- [ShareBuilder 401k Investment Center](#)
- [Advantages of Exchange-Traded Funds \(ETFs\)](#)
- [More on tax-deferred saving](#)
- [The ShareBuilder Roth 401k](#)

Want to learn even more? Then let us suggest these books to help you invest with confidence:

Bill Shultheis, *The Coffeehouse Investor* — a little book with a great message on how to invest and keep it simple

Frank Armstrong III, *The Informed Investor* — a straightforward overview of how the market works

Benjamin Graham, *The Intelligent Investor* — the renowned and thorough book for investors

David Bach, *The Automatic Millionaire* — an easy, one-step guide to help make saving automatic

About ShareBuilder 401k

ShareBuilder 401k is a subsidiary of ING DIRECT, the nation's largest direct bank. We are part of an exciting mission to inspire Americans to become a nation of savers.

We launched ShareBuilder 401k in 2005 with a pioneering new breed of online retirement plan designed to serve America's small businesses.

ShareBuilder 401k brings together leading on-demand technologies with a smart index-based approach to investing. Our 401k plans are supported with fully licensed 401k Consultants and Customer Success Managers to help serve employers and participants at the highest level.

As proof of our dedication, consider our founding principles:

Easy:

- our on-demand 401ks are 100% paper-free
- set up a plan online in less than 20 minutes
- employers manage their plan with just minutes a month

Affordable:

- our inexpensive pricing makes 401k plans available to any size business, including sole proprietors
- we fully disclose all our pricing to you
- we keep participant fees low, giving your savings the opportunity to work harder for you

Smart:

- we are a leader in providing 100% ETF 401k plans — a smart, index-based approach to long-term saving
- our diversified funds and model portfolios make it easy for customers to make sensible investment choices.

Whether you visit us online (www.401kpricing.com/costco) or call one of our consultants ([866-817-1719](tel:866-817-1719) x1), you will see how simple it is to save. Open a plan for your business and start putting your money to work for an exciting tomorrow!

We wish you great success in all you do.