# Health or Wealth: Juggling HSA and 401(k) Contributions

*Richard Barrington | MoneyRates.com Senior Financial Analyst, CFA*
Last updated: February 12, 2020 Investment
5 min read

Health or wealth -- which is more important to you?

Saving money for healthcare and building retirement wealth at the same time can be challenging for many Americans.

A previous study by the Employee Benefits Research Institute (EBRI) illustrates the competition for dollars in terms of lifetime savings needed for healthcare premiums:

The EBRI estimates that a 65-year-old couple on Medicare today will need a lifetime total of $174,000 to have a 50/50 chance of being able to afford health premiums and a typical level of prescription drug charges.

For those who want more than a 50/50 chance of being able to afford those healthcare expenses, the EBRI estimates that a 65-year-old couple would need $296,000 in savings to have a 90-percent certainty of being able to meet their health premiums plus a median amount of prescription drug charges.

Saving this much for healthcare while also saving for retirement is no easy feat, and some workers feel the pinch.

Rising healthcare costs can make the choice even more difficult -- but 401(k)s and health savings accounts (HSAs) are two tax-advantaged savings vehicles that can help you strike the right balance for your situation.

## Health Savings Accounts -- Designed for Double Duty

An EBRI survey found that nearly a quarter of workers report having to cut back their retirement plan contributions because of rising healthcare costs, and 41% report that those costs have inhibited other savings. But a health savings account (HSA) can play a dual role in helping you pay for healthcare as you save for retirement.

You can contribute to an HSA if you participate in a high deductible health plan (HDHP). These are employer-sponsored health insurance programs that offer coverage with lower premiums but higher deductibles. If you are fairly healthy and don't usually incur much in the way of healthcare costs over the course of the year, an HDHP can be a cost-effective option for you.

HSAs are designed to accompany HDHPs by helping you save up money to meet the out-of-pocket healthcare costs you might incur because of the high insurance deductible. The money you contribute to an HSA is tax-free, and you can take money out of the HSA at any time without tax consequences as long as the money is used for qualified healthcare expenses.

Crucially, while you can tap into your HSA savings for routine medical expenses, you can let amounts you don't use accumulate and grow in these accounts. Thus, an HSA can help you both meet healthcare expenses in the year ahead and accumulate savings to meet healthcare expenses in retirement.

## How to Reach Contribution Limits for a 401(k) and an HSA

As long-term savings vehicles, HSAs and 401(k)s have different advantages.

Unlike 401(k) withdrawals, HSA withdrawals are not subject to taxes as long as the money is used for qualified healthcare expenses. That makes the tax characteristics of an HSA superior even to those of a 401(k).

However, if the 401(k) has an employer match, the matching of your contributions often has more economic value than the tax break on HSA contributions.

If you are trying to decide how to allocate savings between an HSA and a 401(k), here is how you can make the most of the advantages each has to offer:

1. **First, put enough in your HSA to meet routine healthcare expenses over the year ahead**
   If you are likely to need this money for premiums and out-of-pocket healthcare expenses, putting it aside in an HSA will make sure it is available without tax consequences.

2. **Next, max out your 401(k) match**
   Once you have enough allocated to the HSA to meet ongoing healthcare expenses, make sure you put enough into the 401(k) to take full advantage of any 401(k) match from your employer.

   So, for example, if your employer matches half of the first 5% of salary you put into the 401(k), make sure you contribute 5% to your 401(k) to get the full amount of employer dollars available.

3. **Contribute up to the HSA contribution limit once your 401(k) match limit is reached**
   Once you have reached the 401(k) match limit, your next priority should be to contribute as much as you can to the HSA. This is because, in the long run, HSA contributions offer superior tax advantages to 401(k) contributions.

For 2020, you can contribute up to $7,100 if you have family coverage in an HDHP, or $3,550 if you have individual coverage.

4. **Finally, contribute any remainder up to the 401(k) contribution limit**
   If you still have money available after maxing out your employer match and reaching the HSA contribution limit, you should still have plenty of room to add to your tax-advantaged retirement savings.

   In most cases, you can contribute up to $19,500 to a 401(k) plan for 2020 and $19,000 for 2019. If you can reach the contribution limits for both your HSA and your 401(k), congratulations -- you have taken maximum advantage of your tax-advantaged retirement savings opportunities.

Saving for retirement and providing for healthcare expenses are both big jobs. Trying to stretch your dollars far enough to cover both isn't easy, but the above will help your money go as far as possible toward these goals.

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| Bank/Institution | APY | Min. to earn APY | |
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| Capital One — Capital One<br>Advertiser Comments | 1.70%<br>Rates as of 2/13/2020 | $0 | Type: Savings<br>Start Saving<br>FDIC Insured |

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