

A Hierarchy for Retirement Savings

Confused about which vehicles to fund first? We can help.



Christine Benz • Aug 3, 2025

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It's a rare newbie investor who has the financial wherewithal—and foresight—to hit the ground running on a retirement savings plan, making the maximum allowable IRA and 401(k) contributions at the same time she's getting her career off the ground.

Instead, most investors tiptoe into retirement savings. They might start with token investments in their 401(k) plans (or get automatically enrolled in them, if they're not paying attention). Then, as their finances allow, or if they're dissatisfied with their 401(k)s, they “graduate” into other investment vehicles for their retirement nest eggs, such as IRAs and taxable accounts.

One question investors often ask is, if they have a fixed sum of money to invest every month or every year, how should they deploy that cash for their retirement savings?

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As with many financial-planning questions, there are no one-size-fits-all answers: Variations in investors' company retirement plans, tax situations, and time horizons mean a retirement savings hierarchy that makes sense for one may not add up for another.

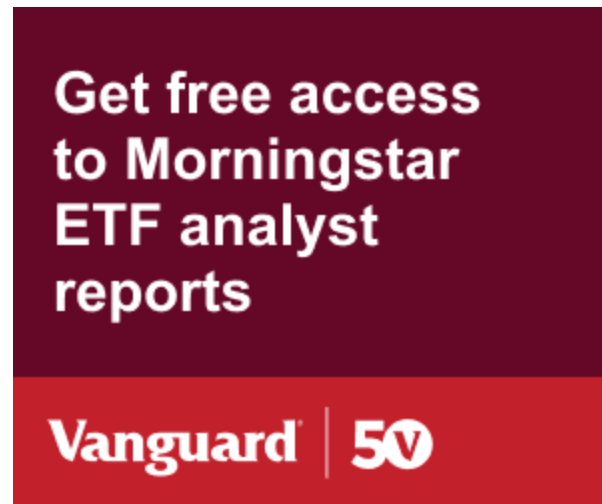
That said, the following framework for retirement savings will be a good starting point for many investors. (Note that this hierarchy does not factor in nonretirement financial goals, such as amassing an emergency fund, saving for college, or investing for short- and intermediate-term financials.)

Stop 1: Invest enough in a 401(k)/other company retirement plan to earn matching contributions.

- *Why prioritize it:* To take advantage of free money.
- *Deprioritize if:* Your 401(k) offers no matching contributions. In that case, proceed directly to Stop 2.

Diversification has been called the only free lunch in investing. But there's another: 401(k) matching contributions. Even if a company's match is lackluster—say, \$0.25 on every dollar invested—it's going to be difficult to outearn that rate of return by

investing outside of the 401(k) (or 403(b) or 457 plan). And remember: Those matching contributions are in addition to any investment earnings. Thus, the first stop for individuals just starting out is to contribute at least enough to earn the full match. For example, if the company provides a match of \$0.50 for every dollar invested up to 6% of pay, the employee should target a 401(k) contribution of at least 6%, too.



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Stop 2: Invest in an IRA.

- *Why prioritize it:* Low costs, flexibility, and the ability to contribute to a Roth.
- *Deprioritize if:* Your company retirement plan features all the bells and whistles, including ultralow costs and a Roth option. Alternatively, if you need the legal protections of a 401(k). In any of those instances, contribute the maximum to the 401(k) before funding an IRA.

It doesn't get much simpler than making contributions to a 401(k) plan: The money comes out of the investor's paycheck, like it or not. Moreover, IRAs enjoy no special tax advantages over 401(k)s. So, why bother with an IRA? Why not fill up that 401(k) to the max, assuming you can spare the \$23,500 maximum allowable contribution (\$31,000 for savers older than 50)?

Costs are one of the key reasons: Many 401(k) plans feature a layer of administrative fees, whereas investors buying into an IRA can invest without that layer. (Investors with

very small IRAs may, however, be on the hook for account-maintenance fees.) And while 401(k) investors are typically wedded to a specific menu of investment choices, some of which may be high-cost, IRA investors are free to invest in a broad gamut of securities, including ultra-low-cost index funds or exchange-traded funds. Additionally, some individuals simply cannot contribute to a 401(k) because their employers don't offer one.

Finally, not all 401(k) plans offer a Roth option, whereas all IRA investors have the option to contribute to a Roth. (High earners will need to go in through the "backdoor.") Roth IRA investors also readily have access to their contributions without any restrictions.

Of course—and here's one of the big exceptions to the hierarchy—some 401(k) plans, especially those from large employers, are rock-solid, featuring no layer of administrative expenses, extra-low-cost investment options, and a full range of features, including the ability to make Roth contributions. If your 401(k) plan ticks all of those boxes, you can go ahead and make a full 401(k) contribution before moving to an IRA.

Stop 2a: Invest in a spousal IRA.

- *Why prioritize it:* Amass retirement savings for a nonearning spouse.
- *Deprioritize if:* The 401(k) of the spouse with earnings is rock-solid; in that case, fully funding that 401(k) plan could reasonably come before funding IRAs for either spouse.

For married couples with a nonearning spouse, funding a spousal IRA should come next in the hierarchy. Assuming the earning spouse has enough income to cover both her contribution and that of her spouse, the nonearning spouse can accumulate retirement savings in his name and also help build up the couple's joint retirement nest egg. Because nonearning spouses don't have the opportunity to contribute to company retirement-savings vehicles such as 401(k)s, 403(b)s, and 457 plans, the spousal IRA is the only game in town.

Stop 3: Invest in your company retirement plan up to the limit.

- *Why prioritize it:* The ability to enjoy tax-free contributions and tax-deferred compounding (traditional), or tax-free compounding and withdrawals (Roth).
- *Deprioritize if:* You have plenty of assets in accounts that will be taxed upon withdrawal, and you're close to retirement. If that's the case, you may want to prioritize saving in a taxable (nonretirement) account instead of maxing out the company retirement plan. Ditto, if there's a chance you'll need the money before retirement.

For higher-income investors who have significant assets to invest toward their retirement savings, taking advantage of all tax-sheltered retirement-savings options should precede investing in nonretirement accounts. And that's true even if the 401(k), 403(b), or 457 plan isn't best of breed. Investors in traditional 401(k)s contribute pretax dollars and enjoy tax-deferred compounding; further, making pretax contributions reduces adjusted gross income, thereby increasing eligibility for valuable credits and deductions. Investors in Roth 401(k)s, meanwhile, enjoy tax-free compounding and tax-free withdrawals in retirement. Those tax benefits are the key reason that investing in a 401(k)—even one that's subpar—trumps investing in a taxable account.

However, it's worth noting that the benefits of investing in a 401(k) are magnified over longer time horizons; investors who are close to retirement will benefit less from the tax deferral of a traditional 401(k) simply because the money will have less time to compound in the account. Moreover, such investors may value tax diversification in retirement. By investing in a taxable account, they'll be able to avoid required minimum distributions and pay capital gains taxes—rather than ordinary income taxes—when they eventually withdraw the money. If that's the case, they may want to prioritize investing in a taxable (nonretirement) account over making additional 401(k) contributions as they get close to retirement.

Stop 4: Make health savings account contributions up to the limit.

- *Why prioritize it:* Health savings accounts offer a tax break every step of the way: pretax contributions go in, funds can be invested and grow inside the account with any tax benefits, and qualified withdrawals for healthcare outlays are also tax-free.
- *Deprioritize if:* You can't contribute; you must be covered by a high-deductible health plan to contribute to an HSA.

Health savings accounts aren't technically retirement savings vehicles. Nonetheless, they can be treated as such if you invest your HSA assets and let the money compound until retirement. In retirement (or sooner), qualified withdrawals are tax-free. In a worst-case scenario where you save more in an HSA than you have in healthcare expenses, withdrawals after age 65 receive the same tax treatment as withdrawals from traditional IRAs or 401(k)s do.

Stop 5: Make aftertax 401(k) contributions to the limit.

- *Why prioritize it:* The ability to enhance a portfolio's share of Roth assets, eventually—provided the 401(k) plan allows for the contribution of aftertax dollars.
- *Deprioritize if:* The 401(k) is especially poor or especially good, as outlined at the bottom of [this article](#).

Investors who have already made the maximum 401(k) contribution of \$23,500 (\$31,000 if older than 50) can contribute at an even higher level—up to \$70,000 in total contributions in 2025—provided their plans allow for contributions of aftertax 401(k) dollars. Those aftertax 401(k) contributions can be converted to Roth inside the plan, assuming the plan allows for it, or once the investor has retired, left the company, or is taking in-service distributions from the plan.

Such contributions will tend to be less attractive for investors who have particularly poor or costly 401(k) plans; the costs of investing in a very poor plan have the potential to erode the eventual tax savings associated with having more Roth assets.

Stop 6: Invest in a taxable account.

- *Why prioritize it:* You're aiming for tax diversification in retirement and already have a sizable share of your assets in tax-deferred and Roth accounts. Ditto if there's a chance you'll need to take out your money before retirement, or you expect to be in the 0% tax bracket for capital gains when you withdraw your money.
- *Deprioritize if:* You haven't yet taken advantage of tax-advantaged accounts that are available to you, and you have a long time horizon for your money.

Investing inside of a taxable (nonretirement) account offers the most possible flexibility, albeit without the tax breaks that accompany the aforementioned

investment wrappers. Not only can you invest in nearly anything inside of a taxable account, but there are no withdrawal requirements either. You can pull the money out whenever you need it, but you can also let it build for as long as you want; any taxable assets that your heirs inherit from you will receive a step-up in basis, too. And while you'll need to invest aftertax dollars in the account, you'll owe capital gains taxes (lower than ordinary income taxes) when you sell. [This article](#) hails some of the important benefits that come along with taxable accounts.

As attractive as all of that flexibility is, the tax benefits conferred by IRAs and company retirement plans usually make up for any extra costs or other drawbacks associated with those plans, especially for investors with longer time horizons.

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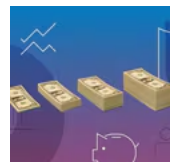
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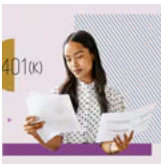
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