

Money Matters: How to spend tax returns

By Rick Gross

More than 110 million Americans collected a tax refund – worth an average of just under \$3,000 – after filing their 2015 tax returns, according to statistics released by the Internal Revenue Service.



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If you're one of the many Americans who expect to receive a financial windfall this year, what do you plan to do with the money? It's tempting to treat yourself to a new TV or a pricey vacation. However, if you refrain from spending your refund impulsively, the money presents an opportunity to treat yourself to additional financial security.

Here are five ways to extend the benefits of any refund you receive this year or in the future:

1. Give your retirement savings a boost

While your refund may not seem like a large sum compared to the amount you need to live the life you want in retirement, every dollar you put aside matters. Keep in mind that the money will have a chance to grow, particularly if you are several years or even decades from retirement.

This year, think about using your refund to “max out” your

contributions to an individual retirement account. Individuals age 50 or older can set aside \$6,500 per year in an IRA while those under 50 can save up to \$5,500 annually. You may be able to deduct your IRA contributions if you qualify, which may help reduce your 2017 tax bill. You can also put your refund to work in a Roth IRA, potentially qualifying you for tax-free withdrawals in retirement.

2. Save for another long-term goal

If you are saving money for a down payment on a home, a home improvement, or higher education needs, your refund can make a big difference. Consider using your tax refund to establish a separate savings account, or invest the money in its own investment vehicle. Keeping your goal-specific savings separate from your day-to-day accounts will help you focus on reaching the goal because you'll be less tempted to spend the money elsewhere.

3. Expand your rainy day fund

A basic rule of thumb is for you to have at least three-to-six months of income set aside in an emergency fund. This is money that should be left in cash (such as a savings account or a money market fund) in the event an unexpected financial need occurs. A tax refund is a great way to bolster your rainy day fund if it's lacking.

4. Focus on being financially independent

If you have any credit card debt, consider first using your refund to reduce this costly form of borrowing. After that debt is eliminated, you may want to focus on tackling any outstanding student loan balances. If you're fortunate enough to have your consumer debts paid off, think about making an additional mortgage payment. Many Americans make it a goal to pay off their home before they retire, and several lump sum payments can help make this goal more attainable for you.

5. Adjust your tax withholding

If you tend to receive a sizable tax refund each year, a better approach may be to reduce the tax withheld from your paycheck. Rather than giving the IRS a “tax-free loan” while you wait for a big refund, keeping the money may make more sense for you. Apply the extra cash you’ll receive in each paycheck toward your most important goals, such as retirement or a child’s education. Adjusting your withholding may affect your tax situation, so talk to your tax advisor before making a change.

You want to use your refund where it will have the greatest positive impact on your financial situation. If you need help weighing competing priorities, talk with a financial professional who can give you an objective perspective on how to best divvy up your refund.

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