

Money Matters: What to do with your tax refund

By Rick Gross

The average refund for individual income taxpayers who received one for the fiscal year ending in September 2016 topped \$3,000, according to the IRS. If you expect to receive a refund on your 2017 tax return, will you save or spend it? While you may be tempted to indulge, consider using the money to solidify your long-term financial position.



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No matter the size of your refund, there are ways you can use it to help reach your current and future financial goals. Here are a variety of ways you might be able to apply a refund based on your life stage:

For people starting out in their careers:

- Add to your emergency fund. Consider saving enough to have the equivalent of at least three-to-six months' worth of income in an emergency fund. This could come in handy if you experience a sudden interruption to your income or a major unexpected expense.
- Pay off student loans. If you are carrying college debt or other loans, applying your refund to the balance can help reduce the total interest you pay or eliminate the debt

entirely. Once you pay off your loans, allocate the amount you spent each month on student loans to another financial goal to keep building your financial foundation.

- Invest in an IRA. Think about starting a habit of investing your tax refund each year into an IRA, where any earnings can accumulate on a tax-deferred basis. While you are limited to contributing \$5,500 annually (\$6,500 for those age 50 and older), the savings can add up. For example, investing a \$3,000 refund each year from age 26 to 65 earning seven percent annually would build to more than \$640,000.

For those starting families:

- Save for a down payment on a home. A tax refund can make a meaningful impact as you accumulate enough to purchase your first home. Consider saving enough to cover at least 20 percent of the home's value. Doing so will eliminate the need for private mortgage insurance, which will cost you extra in interest payments.

- Start or add to a college fund for your children. With the cost of higher education continuing to rise, starting early and saving often can help you make funding tuition a reality. Many options may provide tax advantages so work with your financial and tax professionals to find the best strategy for you.

- Invest your refund. Consider adding your refund to your portfolio, using it to accelerate progress toward your long-term goals. Your refund could be used to purchase stocks, bonds, mutual funds, or other investments that are aligned with your goals, risk tolerance and time horizon.

- Create or update your legacy plan. Developing a will, trust, or other estate documents is important so that your wishes are clear in the event of your death. If you need to create or update legal matters, use your refund as a reason to take the next step.

For those who have a solid financial foundation:

- Apply to home improvements. If you are planning to remodel your home, you may want to use the money to fund specific upgrades, or to keep as a contingency fund throughout the project.
- Save for starting a new business. If you want to start your own business now or in retirement, the refund can provide a cash buffer to help you get started. It can either replace some of your regular income or be used to fund expenditures required to get the business up-and-running.

For those approaching retirement:

- Increase your retirement savings. As your retirement date and goals get clearer, maximizing your retirement savings should take priority. Your refund can help you make an additional investment towards your financial future. If you are 50 or older and have earned income, current tax laws allow you to invest extra dollars in your IRA and workplace retirement plan. Work with your tax professional to learn what the opportunities and limitations may be for your situation.
- Pay down your mortgage. Consider using your refund to make an additional principal payment to your home mortgage. Erasing debt prior to retirement can minimize a major financial burden.

For retirees:

- Spend it on your retirement dream. If you plan to travel or pursue a hobby in retirement, use the refund as a trigger to make your dream happen. Allow yourself to spend the money without guilt – after all, you've earned and planned for this opportunity.
- Invest in a Roth IRA. If you have any earned income that allows you to make retirement contributions, your tax

refund can potentially be placed into a Roth IRA. This vehicle allows contributions after age 70-1/2 (contributions are not possible in a traditional IRA) and provides potential tax-free growth of any earnings.

- Pay health care expenses. Today's rising health care costs are often one of the biggest expenses for retirees. Consider applying the funds to Medicare or long-term care policy premiums. If your health care expenses are manageable, save the refund to pay for future expenses.

Review your tax withholding

If you regularly receive a large tax refund, you may want to adjust the withholding on your paycheck. Decreasing your refund may increase your monthly net pay, allowing you to allocate extra income each month to your financial goals. This strategy isn't right for everyone. Consult with your tax attorney and financial advisor before making adjustments or decisions on how to use your windfall.

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