

Smart Uses for Your Tax Refund...

A tax refund is always a welcome bonus. Whether it's \$300 or \$3,000, the way you use that money can have a real impact on your personal and financial well-being.

New computer? New recliner? Nice vacation? Those are all nice ideas, but...

Before you spend your refund, try to think through *all* the options – even ones that aren't especially glamorous.

Follow Three General Rules

1. **DO plan ahead before spending your refund.** Without a plan, you may use the money on the first important thing that comes to mind and then later realize something else was *more* important. Planning ahead and involving the family increases the chances you will identify all the possibilities and think about which ones are most important.
2. **DO devote a portion of your tax refund to build long-term financial security.**
3. **DON'T throw away part of your refund on preparation fees and/or loan fees.** Did you know that those companies that offer “quick refunds” are just giving you a loan? It's a high-cost, high-risk loan. Look for FREE tax preparation programs like VITA (<http://irs.treasury.gov/freetaxprep/>) and AARP's TaxAide (www.aarp.org/taxaide). Trained volunteers can assist in preparing your return and file it electronically for FREE. By using one of these free programs and having your refund direct deposited into a checking or savings account, you can get your refund in 7-10 days.

Four Smart Uses for Your Tax Refund

1. Pay off bills.

- Your first priority is to pay your regular monthly bills if you have fallen behind (utilities, phone).
- Most other debts should be prioritized, with highest interest rate debts being paid off first.

Suppose you have a credit card balance of \$2,000 at an interest rate of 18%, and you're making payments of \$50/month. At that rate, it will be 62 months – a little over 5 years – before the bill is paid off, and it will cost you \$1,077 interest.

If you use your tax refund to pay off \$1,000 of that bill and then continue to pay \$50/month, the bill will be paid off in 24 months, at an interest cost of only \$198. **You will save \$800** interest by paying \$1000 toward the debt now.

2. Save for needs in the coming year.

Emergency Funds. Having money saved for emergencies can get you through small emergencies, like car repair or medical bills, without breaking a sweat. In the ultimate emergency (loss of income), an emergency fund can keep you afloat until you find another income source. Use part of your tax refund to start or build your emergency fund!

Occasional Expenses. Those big bills that come once a year or every few months (car insurance) can cause huge problems for families. Avoid those problems by being ready for the bills! Use your tax refund to start a special savings fund. Then, keep adding to it throughout the year.



3. Long-term savings!

You CAN make progress toward long-term goals, and your tax refund can help make that happen.

Even small amounts add up. Adding just \$500 a year into a retirement account, such as an IRA, can make a difference over a period of decades.

If the account earns an average annual return of 5%, a contribution of \$500/year would yield \$34,880 after 30 years.

Take the “small amount” theory one step further. Build on the momentum created by that once a year contribution, and make a monthly contribution, too.

If you contribute \$500/year *and* \$25/month, earning a 5% return, in 30 years you will have \$55,247!

Contributing to your retirement *may* pay off with a tax credit!

Moderate-income workers who make voluntary contributions to a retirement account (like a 401k or IRA) may qualify for a tax credit! For example, a married couple filing jointly with an adjusted gross income of less than \$34,000 would qualify for a 50% credit. That means that if they contribute \$2,000 to eligible retirement accounts, they will receive a tax credit of \$1,000! Consult with the IRS for details!

4. Special Purchases

What about that new refrigerator?

Or the sofa? Or ... ?

Those purchases are valuable, too.

Some may be essential, while others simply add enjoyment to life.

Are you fulfilling a *want* or a *need*?

Your Best Bet

First, put some of your tax refund toward financial security by:

- **Saving** part of your refund. You can do this automatically by splitting your refund; put part in your checking account and part in your savings account, or use part to purchase a U.S. Savings Bond. Complete and attach Form 8888 to your tax return to split your refund.
- **Paying off** a debt. Start with a debt with the highest interest rate to save the most in interest charges.
- **Planning** for needs in the coming year (like insurance premiums).
- **Saving** some money for long-term goals (like the down payment on a new car or retirement).

Then use part of your tax refund to make your day-to-day life better. Among all the items on your “wish list,” choose the most important, and shop wisely for it!

And, if your refund was more than \$1000, consider lowering your withholding so you will receive more take-home pay each payday. The additional dollars in your paycheck can be used to meet monthly expenses and could be the difference between making ends meet or not! To change your withholding, file a new W-4 with your employer.

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