Tax Refund Decisions

A tax refund is a welcome bonus. Whether it is $300 or $3,000, the way you use that money can have a real impact on your personal and financial well-being. Want a new computer? Better car? Flat screen TV? Those are nice ideas but…

Follow These Strategies

Plan ahead before spending your refund. Without a plan, you may use the money on the first thing that comes to mind and later realize something else was more important. Planning ahead and involving the family increases the chances that you will identify all the possibilities and identify which are most important.

Devote a portion of your tax refund to build long-term financial security. Money put into retirement savings may also make you eligible for the Savers Credit (formerly known as Retirement Savings Contributions Credit).

You may be eligible for the Savers Credit with a filing status and income of:

- Single, married filing separately, or qualifying widow(er) with income up to $30,000*.
- Head of Household, with income up to $45,000*.
- Married Filing Jointly, with income up to $60,000*.

*Figures are based on 2014 tax year allowances.

Do not throw away part of your refund on loan fees. Never have a tax refund deposited into a bank account other than your own.

Four Smart Uses for Your Tax Refund

1. Pay off bills.
   Your first priority should be monthly bills for needs (utilities, phone, etc.) you have gotten behind on. Prioritize your other debts so that the ones with the highest interest rate get paid off first.

2. Save for needs in the coming year.
   *Emergency Funds* – Having money saved for emergencies can get you through small emergencies like a car repair or medical expense. If you lose your job, an emergency fund can keep you afloat until you find another income source.
Occasional Expenses - Big bills that come once a year or every few months cause huge problems for families. Avoid problems by being ready for the bills! Use your tax refund to start a special savings fund and then keep adding to it throughout the year.

Use direct deposit to receive tax refunds fast. You can split direct deposit refunds in up to three different accounts. These could be joint checking, savings, health savings, retirement, or education savings accounts. More information is available online at www.irs.gov; search for Form 8888.

3. Save for long-term goals.
You can make progress toward long-term goals using your tax refund! 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. Take the ‘small amount’ plan one step further by making a monthly contribution too. If you contribute $500/year and $25/month, earning 9% return, in 30 years you will have $113,800!

4. Save for special purchases.
Do you need a new refrigerator? Or furnace? Or…? Those purchases are valuable too. Some may be essential, while others simply add enjoyment to life.

Plan for the best use of your tax refund! Here is a sample situation:

Sue and John have filed their tax return and find that they will receive $3,120 in tax refunds. They have an overdue gas bill of $275 and a credit card balance of $645 (23.9% interest rate or APR). They pay car insurance month-by-month and are often late incurring late fees. They have not had a vacation with their two children in four years. Neither Sue nor John has any retirement savings or money saved for emergencies.

Using the “Five Steps to a Good Decision” (from Dollar Works 2 curriculum) see how Sue and John worked through their decision of what to do with their tax refund.

Now, use “Five Steps to a Good Decision” to make your own tax refund decisions. By carefully considering all the options - what is good and not so good - you will be able to make the best decision on how to use tax refund dollars. To learn more, visit www.extension.umn.edu/family/personal-finance/dollarworks2/.

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For more information on Dollar Works 2: A Personal Financial Education Program, visit www.extension.umn.edu/dollarworks.

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**Five Steps to a Good Decision: Case Study**

On step 1, write a money goal or decision you need to make. Thinking about this goal, answer each question through step 5.

1. **My money goal or decision:**
   - How to use tax refund of $3,120

2. **How important is this? Is it a want or a need?**
   - Have both needs and wants

3. **What options or choices do I have?**
   1. Pay overdue gas bill ($275) and credit card balance ($625 @ 23.9% APR)
   2. Set aside money for emergencies and vacation
   3. Pay ahead on car insurance

4. **What's good and not good about each option or choice?**
   1. Pay overdue bill and credit card. Good — less late fees and interest, and less stress.
      - Not good — less money to use otherwise.
   2. Set aside. Good — peace of mind and family fun. Not good — money could be used elsewhere such as for retirement or new computer.
   3. Pay ahead on car insurance. Good — no late fee and peace of mind.
      - Not good — money could be used elsewhere.

5. **My decision is..**
   - Divide money up to accomplish all 3 choices.
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1. My money goal or decision:
   ___________________________________

2. How important is this? Is it a want or a need?
   ___________________________________

3. What options or choices do I have?
   ___________________________________
   ___________________________________
   ___________________________________

4. What's good and not good about each option or choice?
   ___________________________________
   ___________________________________
   ___________________________________
   ___________________________________

5. My decision is..
   ___________________________________