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Seeing a Tax Refund as a Financial Opportunity

By [ANN CARRNS](#) MARCH 31, 2015

So far this year, the [Internal Revenue Service](#) has processed more than 66 million federal income tax refunds, averaging about \$2,900 each.

Such a lump sum can provide an opportunity to help get your finances on track, [financial advisers](#) say. “It’s hard to overstate how big a financial event this is” for people with low and even moderate incomes, said Timothy Flacke, executive director of the Doorways to Dreams Fund, a nonprofit that promotes savings programs.

So what is the best way to use the money?

For starters, financial advisers say, pay down any outstanding credit card debt. “Paying off high-priced debt is always the first thing to do,” said Kevin McCormally, editorial director of Kiplinger Washington Editors.

If you don’t have credit card debt, a good option is to add to your emergency savings fund — or start one, if you don’t have one already. More than half of United States households have less than one month of income available to tap in an emergency, the Pew Charitable Trusts [reported](#) this year.

The general rule of thumb is to have an easily accessible stash of money to cover three to six months of living expenses. But for many people, a sum of that size is daunting, said Katie Bryan, spokeswoman for the America Saves campaign.

She recommends thinking smaller — perhaps setting aside \$500 from a refund to start. While that will not cover you if you lose your job, it can help pay for a car repair or an unexpected trip to the dentist, she said.

“It’s empowering to people to know they have that amount,” she said, “so they don’t have to rely on a credit card.”

Another way to help people enter a saving mode is the “30-40-30” approach, she said: Use 30 percent of the refund to help pay off past expenses, like outstanding bills; 40 percent for current needs, or for something you want; and 30 percent for savings toward future needs. For someone

with the average \$2,900 refund, that works out to \$870 each for past and future needs, and \$1,160 for current needs.

Scott Bishop, a financial planner and accountant in Houston, takes a different view. If you're getting a refund of nearly \$3,000, he said, you may be having too much money withheld from your paycheck: "You're giving the federal government an interest-free loan."

By adjusting your payroll withholding, he said, you could have that \$240 or so a month automatically directed into a savings account, a workplace [retirement](#) plan, an individual retirement account or a 529 college savings plan.

Mr. Bishop also suggests that if you have some financial flexibility, you might want to use part of your refund to make a charitable donation and reduce your tax bill for next year. Discussing options with your children, he said, is a good way to start them thinking about charitable giving.

Here are some questions about tax refunds to consider:

■ *How can I adjust my paycheck withholding to reduce the size of my refund?*

Fill out a revised W-4 form and give it to your employer. (The more allowances you claim on the form, the less money is withheld from your paycheck.) To help determine how much you should have withheld, the I.R.S. offers a [detailed calculator](#), but it can be a bit daunting.

[Kiplinger's](#) offers a simpler version that asks for just three pieces of information: filing status (married filing jointly, etc.); 2014 taxable income (Line 43, if you used Form 1040); and the size of your 2014 refund. One caveat: The calculator works best if your financial situation does not change drastically from year to year.

■ *Can I purchase United States savings bonds with my tax refund?*

[Yes — the "tax time" savings bond program](#) is the remaining option for purchasing paper savings bonds (otherwise, bonds are issued in digital form).

You can use some of your refund to buy bonds (you must buy them in increments of \$50), and have the remaining funds deposited to a bank account or sent to you as a paper check. To buy the bonds and allocate your refund, file Form 8888 with your tax return: <http://www.irs.gov/pub/irs-pdf/f8888.pdf>.

■ *How can I check the status of my tax refund?*

You can check it on the [I.R.S. website](#) beginning 24 hours after you electronically file your return, or four weeks after you mail a paper return.