

# 3 Great Ways to Invest Your Tax Refund

Written by Matthew Goldberg, bankrate.com, 2/14/2022

The average tax refund this year is \$2,201 as of Feb. 4, according to the IRS.

A refund, however, isn't found money and should be utilized carefully. And though the idea of spending it may be tempting, the best use of your refund is boosting your savings, investing or reducing debt.

## 1. Boost your emergency savings

There's some debate which should be done first — paying off high-interest debt or having an emergency fund. At least, starting an emergency fund should be a top priority — and then the rest can be applied toward debt or other priorities.

Achieving financial security requires planning for unexpected events. A recent Bankrate survey found less than 40 percent of Americans could pay an unexpected \$1,000 expense from a savings account. So, setting up (or boosting) an emergency savings account is a key part of a smart financial plan.

## 2. Contribute to an IRA

If you've already filed your return, it's too late to contribute to an individual retirement account for the 2021 tax year, unless you want to file an amended return. But you can take your refund and put it into a traditional IRA for the current tax year, plus what's in the account can compound tax-free until you withdraw it, and the contribution may reduce your 2022 taxable income.

(If you haven't yet filed a return, the deadline for contributing to an IRA for the 2021 tax year is April 18.)

If you're eligible to contribute to an IRA, be aware of contribution limits: \$6,000 for 2021 and 2022 for most filers; \$7,000 for those 50 and older. An IRA contribution can help you boost your retirement balance — and may be a good option, especially if you have sufficient emergency savings, don't have credit card debt or similar at a high APR and you've maximized your 401(k) contributions.

## 3. Pay off debt

Using your tax refund to pay off high-interest debt could be the best use for the money. The average balance on credit cards was \$5,525, according to Experian data from November 2021. If you paid only \$100 a month toward the \$5,525 balance it would take 94 months to pay off and cost an additional \$3,990 in interest, according to Bankrate's Credit Card Payoff Calculator.

There are two key ways to approach paying off debt:

- Avalanche method: Focus on paying off the debt with the highest interest rate. Once that is paid off, move on to the balance with the next-highest rate. This method saves the most money.
- Snowball method: Pay off the smallest balance first for the sense of accomplishment, and then work your way up until you finish.