You Received a Tax Refund, What Now?

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As the recipient of a federal tax refund last week, I like many others, began to think – what do I do with this money? My first inclination was towards those that appeal to me most: spending a portion of it on a night out. However, my responsible financial advisor mind kicked in and I started to think about all the other ways I and my other millennial peers should use this money for their long-term benefit instead of short-term thrills.

Use the money to pay down debt. This is the first rule of thumb at our firm and for many financial advisors. A report from The Institute of College Access and Success found that the average undergraduate has $30,100 in student loan debt. If you just received a tax refund – aka money you had planned to live without – this should be your first move. Paying down your debt faster will benefit you enormously over the long term and leave you with more money to spend down the line when you are likely to have higher expenses. If you have college debt, applying excess payments against higher-interest loans from private lenders should be a no-brainer.

Build an emergency fund. Keeping up with the costs of life can be difficult. However, time and time again I am surprised to hear that my peers don't have an emergency fund ready for unexpected costs that could come up. Typically, we advise that an emergency fund be equal to at least three months' salary and that it be available to you in a liquid savings account. In the unfortunate event that an emergency comes up, be it a medical expense, loss of job or even an unexpected home expense, you will be happy that you have this cushion to support you.

Contribute to a Roth IRA. In addition to employer sponsored 401(k) plans, most millennials would benefit from contributing to a Roth IRA. I imagine most millennials haven't stashed away enough money this year or last in their qualified accounts due the other various costs they have (debt, living expenses etc.) so, now may be a good time to try to catch up. The Roth option is especially beneficial to young people, who will most likely see pay increases throughout their professional careers. In fact, CNBC highlighted a Fidelity analysis showing that a 25-year-old could generate $1,000 in monthly retirement income by contributing just $160 a month (assuming a 5.5 percent annual return). A 35-year-old just starting out would need to save $270 a month to achieve the same goal, and a 45-year-old would need to contribute $500. So, any amount that you can put aside into a qualified account will benefit you greatly later in life.

If you are already set on all of the items above, then go ahead, have fun – travel or spend some of that money on hobbies/interests. I know my suggestions above aren't nearly as exciting as the initial knee jerk thoughts you may have about what to do with your money. However, allowing debt to accrue, being caught with your pants down in the case of an emergency or not having the proper savings for retirement (a long way down the road) will prove much more painful than using this money strategically.

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